

October 30, 2003



Acquisition

Contracts for Professional,
Administrative, and
Management Support Services
(D-2004-015)

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Acronyms

COR	Contracting Officer's Representative
CPFF	Cost-Plus-Fixed-Fee
FAR	Federal Acquisition Regulation
GAO	General Accounting Office
IGCE	Independent Government Cost Estimate
PNM	Price Negotiation Memorandum
T&M	Time-and-Materials
TINA	Truth in Negotiations Act



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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October 30, 2003

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION,
TECHNOLOGY, AND LOGISTICS
ASSISTANT SECRETARY OF THE AIR FORCE
(FINANCIAL MANAGEMENT AND COMPTROLLER)
NAVAL INSPECTOR GENERAL
AUDITOR GENERAL, DEPARTMENT OF THE ARMY
DIRECTOR, DEFENSE MICROELECTRONICS ACTIVITY

SUBJECT: Report on Contracts for Professional, Administrative, and Management
Support Services (Report No. D-2004-015)

We are providing this report for review and comment. We considered management comments from the Under Secretary of Defense for Acquisition, Technology, and Logistics, acquisition executives for the Army, the Navy, the Air Force, and the Defense Microelectronics Activity on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. We request that the Under Secretary of Defense for Acquisition, Technology, and Logistics reconsider its position on Recommendation 1.c and 1.e. We request that the acquisition executives for the Army, the Navy, and the Air Force, and the Director, Defense Microelectronics Activity provide specific actions on Recommendation 2.a. We also request that the Director, Defense Microelectronics Activity reconsider his position on Recommendation 2.d. We request that management provide the comments on the final report by December 29, 2003.

If possible, please send management comments in electronic format (Adobe Acrobat file only) to Audcm@dodig.osd.mil. Copies of the management comments must contain the actual signature of the authorizing official. We cannot accept the / Signed / symbol in place of the actual signature. If you arrange to send classified comments electronically, they must be sent over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Questions should be directed to either Mr. Timothy E. Moore at (703) 604-9282 (DSN 664-9282) or Mr. Terry L. McKinney (703) 604-9288 (DSN 664-9288). See Appendix F for the report distribution. The team members are listed inside the back cover.

By direction of the Deputy Inspector General for Auditing:

Robert K. West

Robert K. West
Deputy Director
Contract Management Directorate

Office of the Inspector General of the Department of Defense

Report No. D-2004-015

October 30, 2003

(Project No. D2002CF-0216)

Contracts for Professional, Administrative, and Management Support Services

Executive Summary

Who Should Read This Report and Why? DoD contracting officials, program managers, and Military personnel involved in contract award and administration should read this report. The report discusses recurring problems initially identified in Inspector General of the Department of Defense Report No. D-2000-100, "Contracts for Professional, Administrative, and Management Support Services," March 10, 2000. We reexamined the area as a result of an increase in expenditures for services. This report stresses a need for defining performance requirements, supporting price reasonableness decisions, and monitoring cost contracts for Professional, Administrative, and Management Support Services.

Background. From FY 1992 through FY 2002, DoD spent more money on contracts for Professional, Administrative, and Management Support Services than for any other category of services, with the exception of research and development services. Procurement of Professional, Administrative, and Management Support Services rose in cost from \$6.7 billion to \$14.4 billion, an increase of 115 percent. This report evaluates the steps in the contracting process for services to determine if the Government receives the best value in cost and contractor performance.

Results. Problems continue to exist in the award and administration of contracts for Professional, Administrative, and Management Support Services. Contracting officials continue to award and administer contracts for services without following prescribed procedures. Our review included 113 contract actions with an estimated value of \$17.8 billion. Of the 113 contract actions reviewed, 98 had one or more problems with either nonuse of historical information for defining requirements, inadequate competition or questionable sole-source awards, inadequate basis for price reasonableness determinations, inadequate contract surveillance, or noncompliance with Truth in Negotiations Act procedures. As a result, contractors continued to receive noncompetitive contract awards to perform the same services they have provided for years. The Government often guarantees a profit by paying contractors on a cost reimbursable basis without adequately determining whether prices are reasonable or whether contractors efficiently perform the contracted tasks. The Under Secretary of Defense for Acquisition, Technology, and Logistics needs to monitor the establishment and use of centers of excellence in service contracting as required by the National Defense Authorization Act for FY 2001 and make sure that program office personnel are trained on the use of performance-based contracting methods used in service contracts. The Under Secretary of Defense for Acquisition, Technology, and Logistics also needs to ensure that contracting officers designate in writing any personnel who perform surveillance on cost reimbursable and time-and-materials service contracts and ensure that surveillance personnel are properly trained. The Military Departments and the Defense Microelectronics Activity

need to make program and contracting offices aware of the recurrent problems found in the development of price negotiation memorandums, technical evaluations, and independent Government cost estimates and implement an enforcement program to ensure that these problems do not reoccur. (See the Finding section of the report for the detailed recommendations.)

We also reviewed the management control program as it related to the award and administration of contracts for Professional, Administrative, and Management Support Services. We identified a material management control weakness for the Military Departments and the Defense Microelectronics Activity. Military Departments and the Defense Microelectronics Activity management controls were inadequate to ensure that requirements for contracts were defined and price reasonableness determinations were sufficiently supported. Also, controls were not in place that would ensure adequate surveillance was performed on contracts, particularly cost reimbursable and time-and-materials type contracts.

Management Comments and Audit Response. The Under Secretary of Defense for Acquisition, Technology, and Logistics, the Army, the Navy, the Air Force, and the Defense Microelectronics Activity generally concurred with the recommendations. The Under Secretary nonconcurred with requiring that follow-on cost reimbursable and time-and-materials service contracts be approved at a level above the contracting officer to ensure efforts are being made to award fixed-price contracts. Our audit showed that contracting officers disregarded historical information, the basic consideration for fixed price contracts. Specifically, contracting officers disregarded historical information in 69 percent of the instances we reviewed where the information was available to support fixed-price contracts. As a result, we are advocating that another level review the decision. The Under Secretary concurred with requiring that contracting officers designate in writing any personnel who perform Government surveillance on cost reimbursable and time-and-materials contracts and include a list of duties and limitations. The Director, Defense Procurement and Acquisition Policy, responding for the Under Secretary, stated that guidance would be issued concerning designation of surveillance personnel according to the Defense Federal Acquisition Regulation Supplement. However, we ask that the Under Secretary clarify his position because the Defense Federal Acquisition Regulation Supplement does not make the written designation of surveillance personnel a requirement.

The Army, the Navy, the Air Force, and the Defense Microelectronics Activity concurred with placing greater emphasis on defining requirements and the use of fixed-price contracts, especially where contracts are follow-on contracts. However, we request that they provide specific actions with implementation dates on how they will place greater emphasis on fixed-price contracts. The Defense Microelectronics Activity nonconcurred with developing and employing adequate management controls that will ensure that service contracts are properly awarded and administered. The Defense Microelectronics Activity believed the procurement contracting officer, administrative contracting officer, and project engineer serve as a team in the oversight of their assigned contracts. We believe the administrative contracting officers have no control over the award of service contracts and that the contracting activity can develop controls to document the delegation of administrative controls to administrative activities.

We request that the Under Secretary of Defense for Acquisition, Technology, and Logistics, and the acquisition executives for the Army, the Navy, and the Air Force, and the Director, Defense Microelectronics Activity provide comments on the final report by December 29, 2003. See the Finding section of the report for a discussion of management comments and the Management Comments section of the report for the complete text of the comments.

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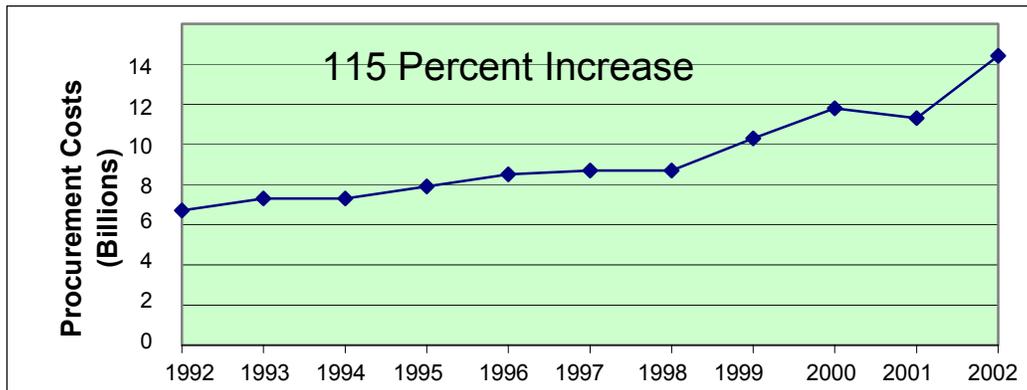
Background

Office of Federal Procurement Policy Letter No. 93-1, “Management Oversight of Service Contracting,” May 18, 1994, encourages Inspectors General to conduct vulnerability assessments of service contracting. This report represents the second DoD audit of professional, administrative, and management support service contracts that continue to grow in both dollar amount and in significance for DoD readiness.

Prior Audit Report. Inspector General of the Department of Defense (IG DoD) Report No. D-2000-100, “Contracts for Professional, Administrative, and Management Support Services,” March 10, 2000 (Report No. D-2000-100), identifies substantial growth in DoD procurement of services. The audit reviewed 105 contract actions, valued at \$6.6 billion, dated from 1997 through 1998 and revealed that numerous problems with contracts for Professional, Administrative, and Management Support Services exist. Specifically, contracting officials did not sufficiently define requirements using historical data and did not prepare adequate independent Government cost estimates (IGCEs). In addition, contracting officials failed to adequately compete contract actions and, in some cases, did not appropriately award multiple-award contracts. Contract files also contained cursory technical reviews as well as inadequate price negotiation memorandums (PNMs). Further, several cases of inadequate contract surveillance and lack of cost control were present. See Appendix D for a discussion of the status of recommendations from Report No. D-2000-100.

Service Contract Trends. Washington Headquarters Service records indicate that from FY 1992 through FY 2002, the cost of DoD procurement of goods and services increased from \$121.4 billion to \$170.8 billion, an increase of 41 percent. However, the cost of procurement of services alone increased from \$61.7 billion to \$92.9 billion, an increase of 51 percent. In FY 2002, 54 percent of DoD spending for goods and services was spent on service contracts.

The types of services DoD procures are categorized into 24 Service Categories. With the exception of research and development services, DoD spent more money from FY 1992 through FY 2002 on contracts for the Professional, Administrative, and Management Support Services category of service contracts (Service Category Code-R) than for any other category of services. The following figure shows annual DoD expenditures for Professional, Administrative, and Management Support Services from FY 1992 through FY 2002, which rose from \$6.7 billion to \$14.4 billion—an increase of 115 percent.



Professional, Administrative, and Management Support Services

Contracting for Services. The contracting process for services involves many steps that ensure the Government receives the best value in cost and contractor performance. Those steps include selecting a contract type, performing market research, determining that proposed prices are fair and reasonable, and planning measures that will ensure the contractor performs efficiently.

Fixed-Price Versus Cost Reimbursable Contracts. The Federal Acquisition Regulation (FAR) 16.202 states that when the contracting officer can establish fair and reasonable prices at the outset, a fixed-price contract is suitable for acquiring commercial items or other supplies or services on the basis of reasonably definite functional or detailed specifications. The use of fixed-price contracts imposes a minimum administrative burden on the contracting parties.

FAR 16.301 states that a cost reimbursable contract is suitable only when the uncertainties involved in contract performance are of such a magnitude that the cost or performance cannot be estimated with sufficient accuracy for permitting use of any type of fixed-price contract. Cost reimbursable contracts provide for payment of allowable incurred costs, to the extent prescribed in the contract. A cost reimbursable contract may be used only when appropriate Government surveillance during contract performance provides reasonable assurance that efficient methods and effective cost controls are used.

FAR 16.601 states that a time-and-materials (T&M) contract may only be used when it is not possible to estimate the extent or duration of the work or anticipate costs with any reasonable degree of confidence at the time of placing the contract. A T&M contract may be used only after the contracting officer executes a determination and findings that no other contract type is suitable. Because it does not encourage effective cost control, a T&M contract requires appropriate surveillance.

Market Research. According to the FAR, contracts should generally be awarded using full-and-open competition. Agencies must conduct market research before developing new requirements documents for acquisitions and determine through use of the results of the market research if sources capable of satisfying the requirements exist. If a contract is awarded on a sole-source basis, a sole-source justification will include an account of the market research conducted.

Price Reasonableness Determination. The FAR requires that contracting officers purchase at fair and reasonable prices supplies and services from responsible sources. The tools used for determining the price reasonableness of a service contract include IGCEs, technical evaluations of labor hours and labor mix, and PNMs.

Efficient Operations. The contract type directly affects the incentives for efficiency of contractor operations. The FAR states that a firm-fixed-price contract provides maximum incentive for the contractor to control costs and perform effectively. Contracts that contain incentive provisions also encourage the contractor to control costs and improve performance by relating the amount of profit or fee payable under the contract to the contractor's performance. A cost reimbursable contract may be used only when Government surveillance during performance of the contract can provide reasonable assurance that efficient methods and effective cost controls are used. Likewise, a T&M contract provides no positive profit incentive to the contractor for cost control or labor efficiency. To give reasonable assurance that efficient methods and effective cost controls are used, close Government surveillance of contractor performance is therefore required for cost reimbursable and T&M contracts.

Other Requirements. Contracts that exceed \$550,000 may be subject to the Truth in Negotiations Act (TINA). The FAR requires that the contractor submit certified cost or pricing data for contract actions exceeding \$550,000 unless an exception is cited. Certified cost or pricing data are not required if price competition exists, if commercial items are being purchased, if prices are set by law or regulation, or if a waiver is obtained. See the "TINA Compliance" section of the finding for further discussion of TINA requirements.

According to the FAR, an indefinite-delivery/indefinite-quantity contract provides for indefinite quantities, within limits, of supplies or services during a fixed period. The Government places orders for individual requirements on separate task or delivery orders.

FAR 37.102 states that performance-based contracting methods are the preferred method for acquiring services. It also states that agencies must use performance-based contracting methods to the maximum extent practicable.

Objectives

Our overall objective was to determine whether contracting officials were following prescribed procedures when awarding and managing contracts for Professional, Administrative, and Management Support Services. Specifically, we examined the market research, the types of contracts used to purchase services, the adequacy of competition and price reasonableness determinations, and the Government surveillance. We also evaluated the management control programs as they applied to the overall objective. See Appendix A for a discussion of the scope and methodology and our review of the management control programs. See Appendix B for prior coverage related to the audit objectives.

Continuation of Problems in the Award and Administration of Service Contracts

Contracting officials continue to award and administer contracts for services without following prescribed procedures. Many of the problems identified in Report No. D-2000-100 continue to exist. Of 113 contract actions reviewed, 98 contract actions had 1 or more of the following problems:

- nonuse of historical information for defining requirements,
- inadequate competition or questionable sole-source awards,
- inadequate basis for price reasonableness determinations,
- inadequate contract surveillance, and
- noncompliance with TINA procedures.

Contracting organizations and program offices did not place adequate emphasis on defining performance requirements, supporting determinations that prices were fair and reasonable, or monitoring cost reimbursable and T&M type contracts. In addition, contracting officials awarded 14 contract actions that did not comply with TINA requirements. As a result, the same contractors continue to receive noncompetitive contract awards for performing the same services they have provided for years. Often, the Government guarantees profits to the contractors by assuming cost risks, paying the contractors on a cost reimbursable basis without adequately determining whether prices are reasonable or whether contractors efficiently perform the tasks.

Contract Actions Reviewed

Our review included 113 contract actions awarded at 12 DoD locations. The contract actions related to 69 contracts with an estimated value of \$17.8 billion¹ and 44 task orders awarded from those contracts valued at \$100.1 million. The estimated value included \$16.3 billion representing six multiple-award contracts. The contract actions reviewed were awarded during FY 2000 and FY 2001 and included 16 fixed-price actions, 75 cost reimbursable actions, and 22 actions that could have been either fixed-price or cost reimbursable. The contract actions represented awards from numerous contract types including indefinite-quantity/indefinite-delivery contracts. Table 1 provides a breakdown by DoD Component of service contract actions reviewed.

¹Estimated value represents the amount that contracting officials estimate as the value of an entire contract including all option years. If the term estimated value is not used, the dollar value will refer to the value of contract orders in effect at the time of the audit.

Table 1. Service Contract Actions Reviewed by DoD Component

DoD Component	Locations Visited	Contract Actions Reviewed	Estimated Value (millions)
Army	3	30	\$ 2,044
Navy	4	45	15,277
Air Force	4	29	413
Defense Agency	1	9	23
Total	12	113	\$17,757

Service Contract Problems

Of the contract actions examined, 87 percent (98/113²) had at least 1 award or administration problem. Specifically, we identified nonuse of historical information for defining requirements, inadequate competition or questionable sole-source awards, inadequate basis for price reasonableness determinations, inadequate contract surveillance, and noncompliance with TINA procedures. Table 2 summarizes problems identified during the audit. Appendix C identifies the problems for each contract action examined.

Table 2. Summary of Problems Found

Problem Areas	Occurrences/ Universe	Percent
Nonuse of Historical Information for Defining Requirements	61/89 ¹	69
Inadequate Competition or Questionable Sole-Source Awards	32/113	28
Inadequate Basis for Price Reasonableness Determinations	79/90 ²	88
Inadequate Contract Surveillance	29/43 ³	67
Noncompliance with TINA Procedures	14/91 ⁴	15

¹Represents the number of contract actions examined for which historical information existed.

²Represents the number of contract actions examined that contained specific tasks (excludes basic indefinite-delivery/indefinite-quantity contract actions).

³Represents the number of cost reimbursable and T&M contract actions examined that contained specific tasks for which the adequacy of surveillance was determinable.

⁴Represents the number of contract actions for which contracting officials were aware that the dollar value exceeded or should have exceeded the \$550,000 threshold.

²Judgment sample percentage does not generalize to universe.

Use of Historical Information for Defining Requirements

Several of the cost reimbursable and T&M contracts examined were for follow-on requirements to previous cost reimbursable and T&M contracts originating at least 10 years earlier. Instead of using prior contracts for defining requirements and determining prices for contracts, contracting officials continued to use cost reimbursable and T&M contracts without explaining why those types of contracts are still necessary as opposed to fixed-price contracts. Usually, contract files include a brief statement that cost reimbursable or T&M type contracts were necessary because contracting officials could not sufficiently define requirements. However, some of the files examined contained no explanation. Also, contracting officials did not regularly use performance-based contracting methods to better define requirements as well as develop metrics for contractor performance.

Use of Historical Information. FAR 16.104(d) states that:

Complex requirements, particularly those unique to the Government, usually result in greater risk assumption by the Government. This is especially true for complex research and development contracts, when performance uncertainties or the likelihood of changes makes it difficult to estimate performance costs in advance. As a requirement recurs or as quantity production begins, the cost risk should shift to the contractor, and a fixed-price contract should be considered.

In 61 of the 89 contract actions reviewed that had a history, little indication existed that contracting officials had examined the information from prior contracts to better define requirements. Instead, contracting officials stated that they could not use fixed pricing arrangements for follow-on contracts because the requirements could not be clearly defined. In 28 of the 89 contract actions reviewed that had a history, contracting officials used the historical information. However, officials only awarded 12 of the actions on a fixed-price basis. Table 3 contains examples of contracts with notable history that were awarded on either a cost-plus-fixed-fee (CPFF) or a T&M basis.

Table 3. Cost Reimbursable Contracts With Significant History

Contract Number	Estimated Value (millions)	Type of Service	Contract Type	History (years)
DAAH01-01-C-0141	\$111.0	Engineering Technical	CPFF	17
DAAB07-01-C-C206	23.3	Engineering Technical	CPFF	13
N00024-00-C-5393	23.9	Program Management/Support	CPFF	30+
N00421-00-D-0361	17.0	Program Management/Support	CPFF	13
F09603-01-C-0402	2.7	Systems Engineering	T&M	30

An example of a contract awarded without adequately using historical information to define requirements was when Army contracting officials awarded contract DAAH01-01-C-0141 in 2001. The contract, with an estimated value of \$111 million, was awarded on a CPFF basis for general system support services related to the Multiple Launch Rocket System. The contract file identified that dating back to 1984 Army contracting officials had awarded 17 sole-source contract actions to the same contractor for services related to the Multiple Launch Rocket System. The contracting officer stated that it was almost certain that the 17 prior contract actions had also been awarded on a cost reimbursable basis. However, no explanation as to why a CPFF contract was still needed for the eighteenth contract existed. In addition, the contracting officer's representative (COR) had transferred to another position and the COR position remained vacant. After accumulating 17 years of historical information from earlier contracts, accepting that contracting officials were still unable to define the requirements is difficult. Contracting officials should not have awarded a cost reimbursable type of contract without considering the use of another contract type more favorable to Government interests.

Two Air Force activities continue to define requirements and award contracts for services on a fixed-price basis. In 2000, Air Force contracting officials awarded, for example, contract F42610-01-C-0004, with an estimated value of \$13.6 million, for engineering services related to the Electromagnetic Pulse Hardness Evaluation of U.S. Air Force Minuteman Intercontinental Ballistic Missile Systems. Documentation in the contract files indicated that contracting officials chose a fixed-price arrangement for \$13 million of the \$13.6 million total contract cost after determining that contractor data supported a realistic basis for determining probable performance costs.

Air Force contracting officials were able to award contract F33657-01-C-5003, with an estimated value of \$1.9 million, contract F33657-00-C-4050, with an estimated value of \$2 million, and contract F33657-00-C-4063, with an estimated value of \$1.6 million, as firm-fixed-price contracts because of the well-defined requirements for the services to be performed. In each of those three contracts, the contracting officer stated that a fixed-price contract was used because over the years the contracting and program offices developed a close working relationship with the contractor. Although system engineering services were obtained under the Air Force contracts and engineering technical services were obtained under the Army contract, the Air Force used the historical information to better define requirements whereas the Army did not.

Some of the Army contracting officials we interviewed were concerned that the use of fixed-price contracts would result in higher prices while Air Force contracting officials stated that in many cases, fixed-price contracts for services were feasible. Higher prices for fixed-price contracts are a possibility. However, clear requirements with fixed prices should increase competition and thereby reduce prices. The FAR states that as a requirement recurs cost risk should shift to the contractor and a fixed-price contract should be considered. Military Departments, Defense contracting organizations, and program offices need to place greater emphasis on defining requirements, especially in situations where contracts are for follow-on requirements for the same or similar requirements.

Performance-Based Contracts. Performance-based contracts offer significant benefits. Primarily, performance-based contracts encourage that contractors are innovative and find cost-effective ways of delivering services. By shifting the focus from process to results, contractors may also deliver better outcomes. To ensure that DoD realizes savings and performance gains, the Under Secretary of Defense for Acquisition, Technology, and Logistics has established that 50 percent of dollars awarded for service acquisitions³ must be performance-based by year 2005.

FAR 37.602-5 provides guidance for the use of performance-based contracting methods when historical information exists. The FAR states that:

When acquiring services that previously have been provided by contract, agencies shall rely on the experience gained from the prior contract to incorporate performance-based contracting methods to the maximum extent practicable. This will facilitate the use of fixed-price contracts for such requirements for services.

Contracting officials interviewed were familiar with the term performance-based contracting; however, they used performance-based contracting methods in only 12 of the 89 contract actions reviewed that had a history. If they are going to meet the mandate of the Under Secretary of Defense for Acquisition, Technology, and Logistics to use performance-based methods for at least 50 percent of service acquisitions measured both in dollars and actions by the year 2005, Military Departments and Defense agencies should ensure that program office personnel are properly trained in the use of performance-based contracting methods. See Appendix E for a discussion of legal guidance on contracts for services.

Competitive and Sole-Source Awards

The best method for the Government to determine that prices paid for services are fair and reasonable is to award service contracts on a competitive basis. Full-and-open competition assures cost effectiveness as well as reduces the potential for favoritism and conflicts of interest. However, of the 113 contract actions reviewed, only 42, valued at \$121 million, were awarded competitively.⁴ The other 71 contract actions, valued at \$472.7 million, were awarded on a sole-source basis. Even when awarded competitively, the Government awarded several high-value contracts after receiving only one offer, a circumstance that can nullify the benefits of competitive awards. Table 4 identifies, by DoD Component, the number of contract actions examined that were competed and received more than one offer, the contract actions that were competed but received only one offer, and the contract actions that were sole-source awards.

³Certain types of services identified by the Office of Federal Procurement Policy as not particularly suited to performance-based efforts will be excluded when computing the percentage of contract dollars awarded for performance-based service acquisitions.

⁴For purposes of this report, competition includes FAR 16.5 provisions regarding expectation of fair opportunity to be considered.

Table 4. Competitive and Sole-Source Contract Actions

DoD Component	Competitive Multiple Offer	Actual Value (millions)	Competitive One Offer	Actual Value (millions)	Sole-Source	Actual Value (millions)
Army	5	\$ 3.2	3	\$ 5.0	22	\$144.7
Navy	25	23.0	6	86.7	14	116.7
Air Force	2	2.2	1	0.9	26	198.0
Defense Agency	0	0.0	0	0.0	9	13.3
Total	32	\$28.4	10	\$92.6	71	\$472.7

Competitive Awards. In the contract process, competition for contract actions and receipt of multiple offers ensures that the prices for goods and services are fair and reasonable. Of the 42 contract actions examined that were subject to competition,⁵ 32 actions, valued at \$28.4 million, were competed and received multiple offers. The remaining 10 contract actions, valued at \$92.6 million, were awarded after contracting officials received only one offer.

Competitive (Multiple Offer) Contract Actions. The 32 contract actions that received multiple offers represented only 23 percent (28.4/121²) of the value of contract actions reviewed that were subject to competition. In the instances when competition among multiple offerors existed for both labor rates and labor hours, the Government and taxpayers had reasonable assurance that the prices paid for the services were fair and reasonable.

Competitive (One Offer) Contract Actions. The 10 contract actions that received only one offer represented 77 percent (92.6/121²) of the value of contract actions reviewed that were subject to competition. Contracting officials generally contended that competition had occurred because the expectation of competition existed. FAR 15.403-1 states that when the Government receives one offer, the price is based on adequate competition if the offeror and the contracting officer believed that the offer was submitted with the expectation that other offers would be received. However, for 3 of the 10 contract actions examined, valued at \$40.8 million, the contracting officials did not convincingly show that the contractors who submitted the only offers submitted those offers with the expectation of competition from other contractors. For 2 of those 3 contract

⁵Contract actions reviewed were separated into two categories for purposes of this analysis. The first group was competitive awards and the second was those contract actions awarded on a sole-source basis or as a directed small business set-aside. Actions “subject to competition” refers to those awards considered competitive awards.

actions, the sole offeror was an incumbent contractor who had been receiving follow-on contracts for the same or similar requirements that originated many years earlier.

Navy contracting officials awarded contract N00421-01-C-0046, valued at \$36.7 million, for systems engineering, analysis, development, and integration of warfare systems in Navy aircraft. Market research consisted of synthesizing the requirement in the Commerce Business Daily and publishing on the Internet. Although several contractors expressed interest in the requirement, the Government received only one offer. Because of the interest by other contractors, the contracting officer determined that competition had occurred. Documentation in the contract files states that:

The contract specialist's expectation of more than one offeror is based on the response to the CBD [Commerce Business Daily] announcement. Due to the competitive environment in which [the offeror] thought they were bidding and because the contract specialist expected more than one offeror, the contracting officer and contract specialist believed that the requirements of adequate price competition, as specified in FAR 15.403-1(c) were met.

Contract N00421-01-C-0046 was a follow-on contract awarded to the same contractor who had been awarded at least five prior contracts over a 14-year time period for the same services. The incumbent contractor had submitted the only offer in three of the five prior contracts. In another contract, the incumbent contractor performed work as a subcontractor for a contract that had been awarded after two other bidders were eliminated as a result of technical considerations. Documentation in the contract files describes concern by contracting officials with the extent of competition that had occurred up to that point in 1992. However, those contracting officials awarded three more contracts to the same contractor who, in each case, submitted the only offer.

Navy contracting officials at another location awarded contract N00244-01-C-0040, valued at \$3.2 million, to the same contractor. The contract was also considered a competitive contract even though only one offer was received. The purpose of the contract was to develop, prepare, and conduct war games using the enhanced naval warfare gaming system. According to the contracting officer, the contract was a follow-on contract awarded to a contractor that had been performing those services for many years. In addition, market research was very limited and consisted of posting the solicitation on the Navy Electronic Commerce Internet site.

Sole-Source Awards. Of the 113 contract actions reviewed, contracting officials awarded 63 percent (71/113²) on a sole-source basis. The 71 sole-source awards represent nearly 80 percent (472.7/593.7²) of the value of the contract actions reviewed. Contracting officials did not adequately justify the use of a specific contractor for 27 contract actions, valued at \$201 million.

An example of an inadequate sole-source justification is Army contract DAAH23-01-D-0266. Contracting officials justified a sole-source contract award for 2001 with an estimated value of \$40 million by stating that the contractor was

the only contractor that could provide the required support services without interruption of current services for the Advanced Threat Infrared Countermeasures/Common Missile Warning System. FAR 6.302-1 states that services may be deemed available only from the original source in the case of follow-on contracts. The follow-on contracts must be for highly specialized services and award to any other source must be likely to result in unacceptable delays in fulfilling the agency's requirements. However, the contract action was for a new requirement and was not a follow-on contract. Unacceptable delays were, therefore, not a valid reason to sole-source the contract. Better value may have been provided by the three other companies that expressed an interest in providing the support services.

Army contracting officials at another location kept the award amount of a directed Section 8(a) contract under the \$3 million threshold requiring competition. Contracting officials awarded order number 1 under DAAE07-00-D-T049 for \$949,170. The value increased, however, to \$11.3 million and was significantly over the \$3 million threshold. Documentation in the contract file indicates that the award amount was kept under the competitive threshold. According to the contracting officer:

The proposed contract will be a 5 (five) year, indefinite-quantity Time and Materials [T&M] contract with a minimum of \$25,000 and a maximum ceiling for the total contract of \$15 million. The initial [Section] 8(a) contract is restricted by the SBA [Small Business Administration] to not greater than \$3 million at this time, however the local SBA office has acknowledged that when we near the actual Basic Contract ceiling of \$2,950,000, if the contractor continues to perform in a manner acceptable to the government, a petition may be sent to the SBO [Small Business Office] by the contracting office to extend the ceiling, in less than \$3M [sic] increments, with the total contract not to exceed \$15 million.

FAR 19.805-1(a) states that an acquisition offered to the Small Business Administration under the Section 8(a) program shall be awarded on the basis of competition limited to eligible Section 8(a) firms if the anticipated value of the total value of the contract, including options, will exceed \$5 million for acquisitions assigned manufacturing North American Industry Classification System Codes and \$3 million for all other acquisitions. FAR 19.805-1(c) also states that a proposed Section 8(a) requirement with an estimated value exceeding the applicable competitive threshold amount shall not be divided into several requirements for lesser amounts in order to use Section 8(a) sole-source procedures for award to a single firm.

The amount of inadequately justified sole-source awards appears to indicate that contracting officials and program offices are attempting to use sole-source provisions to avoid FAR competition requirements. Table 5 shows the types of sole-source justifications used and how many were deemed adequate.

Table 5. Sole-Source Justifications

Justification	Number	Adequate
One Responsible Source	38	27
Urgency of Need	3	0
Industrial Mobilization	5	3
International Agreements	2	1
National Security	8	1
Directed Section 8(a) Set-Aside	15	12
Total	71	44

Price Reasonableness Determinations

In 79 of the 90 contract actions reviewed that contained specific tasks, contracting officials did not adequately support price reasonableness determinations. Contracting officers often determined that prices were fair and reasonable based on the favorable results of technical evaluations the program office generated. However, the technical evaluations lacked detail, and in most cases, did not explain the basis for the determination that contractor-proposed hours, labor mixes, and material costs were reasonable. In addition, IGCEs were often vague and did not adequately explain the basis for determining the estimated amounts for labor rates, labor categories, labor hours, and direct and indirect costs. When questioned about the lack of detail in the technical evaluations and IGCEs, contracting officers stated that they were not technical experts and had to rely on the expertise of the technical people. At one location, contracting officers stated that they did not want to burden program offices by asking for more detail. Also, contracting officials stated that the General Services Administration did not require Government cost estimates or technical evaluations to award service contracts on Federal Supply Schedules. The contracting officials stated that they were worried that if DoD contracting officers insisted on receiving detailed Government cost estimates and technical evaluations, the program offices would take their business to the General Services Administration.

Because of the lack of adequate support documentation in contract files, determining whether contracting officials obtained fair and reasonable prices for services was, in most cases, impossible. The following example describes the information that one contracting officer used to determine that prices paid were fair and reasonable. The contracting officer determined that the \$1.1 million price paid for order 27, awarded under Army multiple-award contract DAAH01-00-D-0021, was fair and reasonable based on information contained in

the technical evaluation and the IGCE. The technical evaluation was vague and states that the contractor's proposed hours and proposed labor categories were reasonable because the same amounts were contained in the IGCE. The technical evaluation also states that no reviews of travel or material costs were performed. Those costs, however, were reasonable because a presumption existed that the contractor would not propose for any items not stated within the statement of work. The value of travel and material costs was \$179,020. The IGCE was also vague; it consisted only of a list of labor categories, labor hours, direct and indirect costs, and amounts for material. The estimate did not provide a basis for those estimates. The IGCE took on greater importance because the Government provided a suggested number of labor hours for which the contractor could bid. Based on that information, the contracting officer certified that the \$1.1 million price paid was fair and reasonable.

IGCEs. Of the 90 contract actions reviewed that contained specific tasks, 88 either did not contain or contained inadequate IGCEs. When prepared, the estimates were usually unsigned, undated, and consisted of only a list of labor categories, labor rates, and labor hours, with no explanation of how the program office determined those amounts. The development of the estimates took on greater importance in those situations where the Government recommended the amount of labor hours, labor rates, and labor categories used for completing tasks. Report No. D-2000-100 recommends that Acquisition Executives for the Army, the Navy, and the Air Force make acquisition personnel aware of the problems found in IGCEs, technical evaluations, and PNMs. The problems, however, are still occurring.

Technical Evaluations. Technical evaluations for 73 of the 90 contract actions examined containing specific tasks were cursory and did not adequately explain the basis for determining the acceptability of contractor-proposed costs, especially for the proposed hours of the contractor. For the most part, the technical evaluations consisted of nothing more than a few sentences or an e-mail message from the technical evaluator to the contracting officer stating that contractor-proposed prices were acceptable. Contracting officials then used the technical evaluations as their basis for determining that prices paid were fair and reasonable. When questioned on the level of detail contained in the technical evaluations, contracting officials stated that they were not technical experts and, therefore, had to rely on technical evaluator statements that the contractor-proposed prices were acceptable with no basis.

In one situation, Army contracting officials quickly awarded a fifth follow-on contract to a contractor without performing adequate contracting procedures to make the award before the expiration of funds. When awarding contract DAAB07-01-C-C206, with an estimated value of \$23.3 million, contracting officials did not adequately justify awarding a CPFF contract as the fifth follow-on contract awarded to the same contractor. According to contracting officials, a technical evaluation had to be accomplished quickly "since funds will expire [at the] end of this fiscal year." As a result, the technical evaluation consisted of only a one-line e-mail stating that "material cost, travel cost, and labor hours are acceptable." The contract file contained an IGCE; however, the estimate was unsigned and undated and consisted of a list of labor categories, labor rates, and labor hours—with no explanation of the basis for the estimated

information. Contracting officials did not request Defense Contract Audit Agency assistance. Also, the PNM was lacking because it did not answer the basic question about whether the price was fair and reasonable.

Price Reasonableness Decisions. Contracting officers need to better document their price reasonableness determinations and make price reasonableness decisions based on the results of detailed analysis rather than from unsupported statements and opinions. In 79 instances of the 90 contract actions reviewed that contained specific tasks, the information in contract files was incomplete and did not clearly support the contracting officers' determinations that prices paid were fair and reasonable. The contracting officers generally documented in the PNM the basis for price reasonableness decisions. In some instances, however, although program offices developed an IGCE, no mention of the estimate was in the PNM and no mention of whether the contracting officer relied on the IGCE as part of the overall price reasonableness determination was in the contract file. In other instances, the Defense Contract Audit Agency identified cost issues and no mention of the identified issues was in the PNMs. Instances existed where the PNMs did not identify whether the prices paid were fair and reasonable. Labor rates and labor hours were the areas most lacking in price validations.

Labor Rates. In 24 of the 90 contract actions reviewed that contained specific tasks, contracting officials did not adequately justify labor rates. Contracting officers usually requested assistance from the Defense Contract Audit Agency to validate labor rates. The assistance provided, however, was often either limited or would take too long to provide so the contracting officer used other methods to validate labor rates. Sometimes, labor rate validation consisted simply of a telephone request for labor rate checks. In those cases where contracting officers did not obtain Defense Contract Audit Agency assistance, labor rates were usually validated using questionable methodology or were accepted simply on the word of an unsupported technical evaluation.

Labor Hours. In 67 of the 90 contract actions reviewed that contained specific tasks, the PNM insufficiently validated labor hours and labor mixes. In most cases, contracting officers considered the number of labor hours proposed satisfactory based on unsubstantiated technical evaluations.

Contract Surveillance

FAR 16.301-3 states that cost reimbursable type contracts can be used only if appropriate Government surveillance during performance will provide reasonable assurance that efficient methods and effective cost controls are used. Defense Federal Acquisition Regulation Subpart 201.6, "Contracting Authority and Responsibilities," states that contracting officers may designate qualified personnel as their authorized representatives to assist in either technical monitoring or administration of a contract.

Of the 113 contract actions reviewed, we met with CORs or program office officials for 43 contract actions awarded for specific tasks on a cost reimbursable basis. Surveillance was inadequate for 29 of the 43 contract actions.

CORs. Contracting officers designated in writing a COR for 21 of the 43 contract actions reviewed. Contract surveillance for 13 of the 21 contract actions was inadequate. COR surveillance files were limited and usually consisted of a copy of the contract as well as a few contractor monthly status reports and invoices. Some of the CORs did not have a copy of the contract. In addition, COR surveillance consisted primarily of a review of contractor invoices and contractor-generated monthly status reports. Surveillance measures focused more on the expenditure of funds, or “burn rates,” than on whether contractors were performing efficiently. In one instance, the COR position was vacant, and the position had not been replaced.

In 22 of the 43 contract actions reviewed, contracting officers did not designate in writing a COR. In each of those situations, contracting officers attempted to provide the audit team with program office officials who could answer surveillance-related questions. However, little evidence existed that program officials were performing surveillance. The officials did not have adequate surveillance files and, in some cases, did not have a copy of the contract. They also expressed difficulty in describing specific steps performed. When asked to describe specific surveillance steps, officials stated that they reviewed contractor-generated monthly reports and invoices. In one instance, contracting officials had difficulty determining which program office official the audit team should interview.

For Air Force contract F42610-00-C-0011, the value of which was estimated at \$2.1 million, a contracting officer not assigned to this contract was identified as the COR performing surveillance. Contracting officials subsequently provided two additional people from the program office to be interviewed for surveillance-related questions. However, neither of the persons identified could answer detailed surveillance-related questions about the contract and appeared confused about why they were being interviewed.

On the other hand, two CORs assigned surveillance duties under Navy contract N00421-00-C-0184 were able to provide detailed information on their surveillance duties. They also provided a detailed surveillance file. During a meeting, the CORs stated that their contracting office would not accept a requirements package from their program office unless the procurement package included a copy of a COR designation letter and a copy of the training certificate for the COR.

Report No. D-2000-100 recommends that Acquisition Executives for the Army, the Navy, and the Air Force review the assignment of contract surveillance work for contracts for services and adjust assigned workload and staffing to resolve imbalances. As a result, the Army established the Army Contracting Agency. To reduce the need for surveillance, the Navy planned to increase the use of performance-based contracting principles and rely more on past performance information in source selection. The Air Force believed that the review was an installation-level issue and Air Force Instruction 63-124, “Performance-Based Service Contracts (PBSC),” already requires that the installation Performance Management Council, as one of its key management duties, provide synergy in addressing installation issues. However, during this audit, we saw no

improvement in this area. The CORs and others performing surveillance should be specifically trained to perform adequate contract surveillance on cost reimbursable and time-and-materials service contracts.

Effective Cost Controls. DoD officials need to make sound judgments on service contract requirements including estimating costs and be able to determine whether the contractor is performing according to the contract terms and conditions. Officials must retain control over, and remain accountable for, policy decisions that may be based, in part, on a contractor's performance and work products.

Of the 113 contract actions reviewed, 35 included questionable cost growth of \$90.3 million over originally estimated prices. Of those 35 contract actions, 30, with increased costs of \$52 million, were cost reimbursable contracts or included cost reimbursable provisions. For example, Navy contracting officials awarded T&M contract N00421-00-D-0264, task order 1, for a total award of \$393,192. Additional work was added to the task order after the initial award, for a total cost growth of \$1.8 million. The final task order price was more than \$2.2 million, which is nearly six times the amount of the initial task order. According to the contracting officer, the initial award may have been awarded for the amount of funding available at the time of award. When cost reimbursable contracts are used, contracting and program officials need to ensure that contractors have incentives for controlling costs. If contract incentives are not sufficient, close surveillance of contractor performance is necessary for ensuring that effective cost controls are present.

TINA Compliance

FAR 15.403-4 states that contracting organizations will obtain certified cost or pricing data for all contract actions valued over \$550,000 except when:

- the price is based on adequate price competition,
- prices are set by law or regulation,
- a commercial item is being acquired,
- a waiver has been granted, or
- contracts or subcontracts for commercial items have been modified.

FAR 15.403-4 also states that unless an exception applies, certified cost or pricing data are required before awarding negotiated contracts, subcontracts, and modifications for any sealed bid or negotiated contract (whether or not cost or pricing data were initially required). Of the 113 contract actions examined, contracting officials were aware that 91 either exceeded or should have exceeded the \$550,000 threshold. Of those 91 contract actions, contracting officials did not comply with TINA procedures for 14, valued at \$63.2 million. In several

instances, contracting officials were either not able to explain why certified cost or pricing data were not obtained or did not understand when certified cost or pricing data were required.

In one situation, an Army contracting officer kept the award value under the \$550,000 threshold. On July 5, 2001, contracting officials awarded contract DAAE07-01-C-M037 for \$548,267; \$1,733 under the \$550,000 threshold requirements for certified cost or pricing data. The award amount being slightly under the threshold was no coincidence. According to documentation in the contract file, the contracting officer wanted the contract to be awarded under the TINA threshold. The contracting officer stated:

I'd like to keep the priced effort under \$550k [\$550,000] so we need to talk about how to structure this. Some of the travel could be left out and added when it becomes clear he will travel.

Contracting officials subsequently issued eight modifications that increased the contract from \$548,267 to \$1,629,278.98.

Service Contract Requirements

Defining requirements up front has several benefits: it makes it easier for contractors to price proposals; it increases the probability that competition will occur; and it also increases the probability that fixed pricing arrangements can be used, resulting in less cost risk to the Government and in less human resource expenditures to perform surveillance functions. However, contracting officials did not demonstrate a serious effort on defining requirements, especially in situations where contracts were repetitively awarded to the same contractors for the same or similar services over extended time frames.

Report No. D-2000-100 recommends that the Deputy Under Secretary of Defense (Acquisition Reform), now called the Director of Defense Procurement and Acquisition Policy, develop a training course and train contracting and program personnel on planning and defining requirements as well as using historical data when awarding contracts for Professional, Administrative, and Management Support Services. However, no indication exists that the process is substantially improving. Accordingly, we believe that contracting organizations need to place more emphasis on defining requirements.

Emphasis on Defining Requirements. Contracting officials claimed that requirements could not be defined well enough to consider the use of fixed pricing arrangements while at the same time identifying the existence of years of historical data related to prior contracts awarded to the same contractors, for the same or similar services. During meetings, contracting officials appeared more comfortable in using cost reimbursable and T&M type contracts and in some instances believed that the use of fixed-price contracts for services would almost certainly increase the cost of the contract. In some instances, indications were present that decisions regarding whether to use a cost reimbursable or T&M type contract were made solely by the program offices.

Management Controls. At the sites visited, the Military Departments and the Defense Microelectronics Activity did not include the award and administration of Professional, Administrative, and Management Support Services as an area of review in their management control programs. Therefore, the management control programs were inadequate for providing reasonable assurance that Federal regulations were properly adhered to during the contract award and administration process for Professional, Administrative, and Management Support Services. In our review of the contract files, inadequate support for price reasonableness determinations existed. Contracting officials determined that prices were fair and reasonable based on technical evaluations and IGCEs that lacked sufficient detail for supporting labor rates, labor categories, labor hours, and direct as well as indirect costs. Therefore, determining if the Government received the best value was impossible. Adequate management controls would help ensure that the Government obtained fair and reasonable prices for Professional, Administrative, and Management Support Services.

Current Status of Centers of Excellence. The Military Departments have made ineffectual efforts at implementing centers of excellence. Report No. D-2000-100 recommends that Acquisition Executives from the Army, the Navy, and the Air Force establish and use centers of excellence with personnel that have performed research and received training to become expert buyers of Professional, Administrative, and Management Support Services. Subsequently, the requirement to develop centers of excellence for Professional, Administrative, and Management Support Services became law. The National Defense Authorization Act for FY 2001 (Public Law 106-398), section 821(c) directed that the Military Departments had 180 days from October 30, 2000, to establish centers of excellence for service contracts. The Army had Major Army Commands develop centers of excellence but reported that the centers are subject to major revisions as a result of the establishment of the Army Contracting Agency. The Navy reported that the development of a center of excellence was delayed because of technology infrastructure changes and a departmental reorganization. The Air Force established a center of excellence in the Office of the Deputy Assistant Secretary of the Air Force (Contracting) but does not require the use of the center of excellence.

Service Contracting Management Structure and Strategic Plan. General Accounting Office (GAO) Report No. GAO-03-935, "Contract Management: High-Level Attention Needed to Transform DoD Services Acquisition," September 10, 2003, reports that DoD and the Military Departments each have a management structure in place for reviewing individual services acquisitions valued at \$500 million or more, but that approach does not provide a DoD-wide assessment of how spending for services could be more effective. In addition, the Military Departments are in the early stages of separate initiatives that may lead them to adopt a strategic approach to buying services, but DoD lacks a plan that coordinates these initiatives or provides a road map for future efforts.

The GAO recommended that DoD strengthen its contracting management structure for services to promote use of best practices such as centralizing key functions, conducting spend analyses, using commodity teams, achieving strategic orientation, reducing purchasing costs, and improving performance. DoD also needs a strategic plan on how the Military Departments could best accomplish

those best practices. DoD concurred in principle with the recommendation to change its management structure and partially concurred with the recommendation for a strategic plan.

Conclusion

The Office of Federal Procurement Policy has addressed procurement of services in guidance. Problems related, however, to contracts awarded for services are still abundant. In 1994, the Office of Federal Procurement Policy stated:

. . . it is important that procurement officials work closely with program and other officials to develop clear and precise statements of work for the products and services being acquired. Contracting for services is especially complex and demands close collaboration between procurement personnel and the users of the service to ensure that contractor performance meets contract requirements and performance standards.

The Office Of Federal Procurement Policy also announced the following policies for the Federal Government when contracting for services.

- Program officials are responsible for accurately describing the need to be filled or problem to be resolved through service contracting to assure full understanding and responsive performance by contractors, and should obtain assistance from contracting officials, as needed.
- Services are to be obtained in the most cost-effective manner, without barriers to full-and-open competition, and free of any potential conflicts of interest.

Contractors are more likely to submit proposals when clearly understanding the requirement. The lack of contracting and program officials working together to define requirements has resulted in a lack of competitive contracts for services that receive multiple offers. Additionally, the program office may become familiar and satisfied with the performance of a specific contractor and wish to continue working with that contractor. Those factors cause the same contractors to continue to receive contract awards for performing the same services for inordinate time periods. To exacerbate matters, the contractors operate without risks as all work is accomplished on a cost reimbursable basis. Furthermore, surveillance is often insufficient to ensure efficient contractor operations and no contract incentives exist to motivate contractors to work efficiently. The Government is not receiving good value for its money under such circumstances.

Clearly defined requirements on fixed-price contracts can provide opportunities for contractors to use innovative methods to increase efficiencies. Additionally, the use of fixed pricing arrangements would result in less expenditure of human resources for surveillance related duties. Accurate performance measurements contained in performance-based contracts can ensure satisfactory accomplishment of contracted tasks even by less experienced contractors performing the

contracted services. When a valid service requirement exists, DoD officials are required to obtain the service in the most cost-effective manner possible. If contractor support is appropriate, DoD procurement and program officials must ensure that the service is acquired from a quality vendor that constitutes the best value considering cost and other relevant factors.

Management Comments on the Finding and Audit Response

Air Force Comments. The Associate Deputy Assistant Secretary of the Air Force for Acquisition Integration in the Office of the Assistant Secretary of the Air Force for Acquisition commented that this report failed to address the actions the Air Force has taken to satisfy the mandates of section 801 of the National Defense Authorization Act for FY 2002. The Assistant Secretary of the Air Force for Acquisition has established the Program Executive Office for Services that will provide oversight and management of service acquisitions over \$100 million or 300 full-time equivalents. For smaller services acquisitions, heads of contracting activities have oversight and management responsibilities. In addition, the Assistant Secretary of the Air Force for Acquisition is in the process of identifying Air Force officials who will have statutory obligations to review and approve all services acquisitions and ensure they are performance-based. The Assistant Secretary of the Air Force for Acquisition is also amending the Air Force Federal Acquisition Regulations to designate the identified officials. Further, the Assistant Secretary of the Air Force for Acquisition and the Program Executive Office for Services have developed internal training packages in source selection techniques, past performance evaluations, and developing performance objectives and metrics as stopgap measures for meeting general education and training requirements relative to services contracting. The Air Force has also requested that the Defense Acquisition University allocate more resources to develop and add to its services contracting training curriculum.

Audit Response. As stated, contract actions reviewed in this audit were awarded in FY 2000 and FY 2001. We commend the Air Force for recognizing services contracting problems occurring during that time and taking actions to improve. Future audits of services contracts will no doubt reflect the contract improvements resulting from Air Force actions taken in response to section 801 of the National Defense Authorization Act for FY 2002.

Recommendations, Management Comments, and Audit Response

1. We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics:

a. Monitor the establishment and use of centers of excellence in service contracting as required by section 821(c) of the National Defense Authorization Act for FY 2001 (Public Law 106-398).

Management Comments. The Under Secretary of Defense for Acquisition, Technology, and Logistics concurred. The Director, Defense Procurement and Acquisition Policy, responding for the Under Secretary, stated that the Director's office will send a memorandum to the Military Departments and Defense agencies within 10 working days asking them to report on efforts to establish centers of excellence, how such centers have been used, and the experience gained at the centers.

b. Train program office personnel on using performance-based contracting methods for service contracts, including how to develop performance-based statements of work and performance measures.

Under Secretary of Defense for Acquisition, Technology, and Logistics Comments. The Director, Defense Procurement and Acquisition Policy responded for the Under Secretary. The Director concurred and attached an August 19, 2003, memorandum that establishes the requirement for personnel who prepare statements of work, including program office personnel, to be trained on performance-based service acquisitions by September 30, 2005.

Air Force Comments. Although not required to comment, the Assistant Secretary of the Air Force for Acquisition, with reservation, concurred with the recommendation that additional training is necessary in the area of performance-based services acquisition. However, the Associate Deputy Assistant Secretary of the Air Force for Acquisition Integration stated that the report failed to address all that the Air Force is doing to improve training. The Assistant Secretary of the Air Force for Acquisition is in the process of revising Air Force Instruction 63-124, "Performance-Based Service Contracts," April 1, 1999, which will expand the application of performance-based services acquisition throughout the life of an acquisition. The Air Force is also developing a performance-based services acquisition guide that outlines the philosophy of performance-based services acquisition, discusses the elements of performance-based services acquisition, and provides various approaches for meeting the requirements of performance-based services acquisition. In addition, the Assistant Secretary of the Air Force for Acquisition and the Program Element Office for Services held a services symposium in January 2003 with industry, major command contracting representatives, and other customers to identify initiatives the Air Force must implement to develop an effective services program.

c. Require that contracting officers designate in writing any personnel who perform Government surveillance on cost reimbursable and time-and-materials contracts and include a list of duties and limitations.

Management Comments. The Under Secretary concurred. The Director, Defense Procurement and Acquisition Policy, responding for the Under Secretary, stated that the Director's office would issue guidance in the next 10 working days emphasizing that in accordance with Defense Federal Acquisition Regulation Supplement 201.602-2(5), all contracting officers should designate representatives in writing, and shall specify the contracting officer representatives authority and limitations.

Audit Response. Although the Under Secretary concurred, the response is unclear as the Defense Federal Acquisition Regulation Supplement citation states that a contracting officer may designate a COR in writing. The intention of the recommendation is to create a requirement that for cost reimbursable and T&M contracts, contracting officers must designate a COR in writing unless unusual circumstances exist. We ask that the Under Secretary provide additional comments on the final report to clarify his position.

d. Require that contracting officer’s representatives and others performing surveillance be specifically trained to perform contract surveillance on cost reimbursable and time-and-materials service contracts that includes, at a minimum:

(1) Basic contract information, including the contract type and the implications on surveillance requirements, and

(2) Cost risk and any other Government concerns related to contract administration.

Management Comments. The Under Secretary concurred. The Director, Defense Procurement and Acquisition Policy, responding for the Under Secretary, stated that the Director’s office would issue guidance in the next 10 working days emphasizing that in accordance with Defense Federal Acquisition Regulation Supplement 201.602-2(2), all CORs must be trained for their required duties.

e. Require that follow-on cost reimbursable and time-and-materials service contracts be approved at a level above the contracting officer to ensure that efforts are being made to award fixed-price contracts.

Management Comments. The Under Secretary nonconcurred. The Director, Defense Procurement and Acquisition Policy, responding for the Under Secretary, stated that the contract type decision must be made on a contract-by-contract basis and that the contracting officer is in the best position to make that decision. Nevertheless, the Director, Defense Procurement and Acquisition Policy will issue a memorandum emphasizing the importance of using the appropriate contract type based on the criteria in the regulations.

Audit Response. The Under Secretary’s comments are nonresponsive. Our audit showed that in 69 percent of the instances we reviewed, where historical information was available on how a contractor performed a service, the contracting officer did not consider that information when determining contract type and continued to use cost reimbursable or T&M type contracts that placed unnecessary cost risks on the Government⁶. We agree that the contracting officer is the best person to make the contract-type decision. However, historical information is a basic consideration for fixed-price contracts and because contracting officers often ignored that required basic consideration, even when a contractor performed essentially the same services for decades, a serious problem exists among contracting officers in the selection of contract type. We are

⁶Use of historical information to define requirements is explained more fully on Page 6 of this report.

advocating that another level review the decision to make sure that it is based on sound judgment. We request that the Under Secretary reconsider his position and provide additional comments or alternate solutions to the final report.

f. Issue a memorandum for senior contracting officials and program managers that clearly defines manager responsibilities regarding stewardship of taxpayer dollars and states that fixed-price contracts are in the best interest of the Government and that for a program manager to insist on a cost reimbursable contract when a fixed-price contract is appropriate is a denunciation of his duties.

Management Comments. The Under Secretary partially concurred. The Director, Defense Procurement and Acquisition Policy, responding for the Under Secretary, stated that the Director's office would issue guidance in the next 10 working days asking Military Departments and Defense agencies to ensure that appropriate contract types are used when acquiring services.

Audit Response. The comments are responsive to the intent of the recommendation.

2. We recommend that Acquisition Executives for the Army, the Navy, and the Air Force, and the Director, Defense Microelectronics Activity:

a. Place greater emphasis on defining requirements and the use of fixed-price contracts especially in situations where contracts are follow-on contracts.

Army Comments. The Deputy Assistant Secretary of the Army (Policy and Procurement) concurred in principle, stating that the Army continues to believe that the contracting officer remains in the best position to make the determination of contract type. The Army also believes that the existing guidance on the selection of contract type is clear; however, the Army will stress the importance of selecting the appropriate contract type.

Navy Comments. The Chief of Staff/Policy for the Deputy Assistant Secretary of the Navy for Acquisition Management concurred in principle, stating that Navy contracting officers recognize the advantages of fixed-price contracts but make contract type decisions based on specific circumstances surrounding the instant requirement in accordance with FAR Part 16.

Air Force Comments. The Associate Deputy Assistant Secretary of the Air Force for Acquisition Integration concurred, stating that the Air Force is aware of the problems identified in the report and has already started addressing them.

Defense Microelectronics Activity Comments. The Director, Defense Microelectronics Activity concurred with the recommendation, stating that Defense Microelectronics Activity contracting officials already review the requirements and available history to ensure that the appropriate pricing arrangement and contract type are used.

Audit Response. Our audit showed that in 69 percent of the instances we reviewed, where historical information was available on how a contractor performed a service, the contracting officer did not consider that information when determining contract type and continued use of either cost reimbursable or T&M type contracts that placed unnecessary cost risks on the Government. Historical information is a basic consideration for fixed-price contracts, and because contracting officers often ignored that required basic consideration, even when a contractor had performed essentially the same services for decades, shows that a serious problem exists among contracting officers in selection of a contract type. We request that the Acquisition Executives provide specific actions with implementation dates on how they plan to place greater emphasis on the use of fixed-price contracts.

b. Establish and use centers of excellence in service contracting as required by section 821(c) of the National Defense Authorization Act for FY 2001 (Public Law 106-398).

Army Comments. The Deputy Assistant Secretary of the Army (Policy and Procurement) concurred, stating that in November 2000, the Army directed major commands to develop centers of excellence in service contracting in accordance with section 821(c) of the National Defense Authorization Act for FY 2001.

Navy Comments. The Chief of Staff/Policy for the Deputy Assistant Secretary of the Navy for Acquisition Management concurred, stating that the Navy Virtual Center of Excellence for Services Contracting is scheduled to be fielded in the first quarter of FY 2004.

Air Force Comments. The Associate Deputy Assistant Secretary of the Air Force for Acquisition Integration concurred, stating that the Air Force is aware of the problems identified in the report and has already started addressing them.

Defense Microelectronics Activity Comments. The Director, Defense Microelectronics Activity concurred, stating that management will ensure that personnel are familiar with and encourage the use of the Army's centers of excellence.

c. Make program and contracting offices aware of any recurring problems in the development of independent Government cost estimates, technical evaluations, and price negotiation, and implement an enforcement program that ensures those problems do not reoccur.

Army Comments. The Deputy Assistant Secretary of the Army (Policy and Procurement) concurred, stating that the Army Procurement Management Assistance Program provides assessment of the effectiveness and efficiency of Army-wide procurement through outcome-based analysis. The Army believes that the existing program accomplishes the goal of improving its effectiveness and efficiency without establishment of a new enforcement program.

Navy Comments. The Chief of Staff/Policy for the Deputy Assistant Secretary of the Navy for Acquisition Management partially concurred, stating that the Navy Virtual Center of Excellence and the Navy Procurement Performance

Management Assessment Program will allow contracting activities to evaluate the quality of their contracting processes and know when corrective action is appropriate. The Navy does not agree with establishing an enforcement program.

Air Force Comments. The Associate Deputy Assistant Secretary of the Air Force for Acquisition Integration concurred, stating that the Air Force is aware of the problems identified in the report and has already started addressing them.

Defense Microelectronics Activity Comments. The Director, Defense Microelectronics Activity concurred, stating that their training in developing Independent Government Cost Estimates, writing technical evaluations, and completing price negotiation memorandums was updated and conducted in March 2003.

d. Develop and employ adequate management controls that ensure service contracts are appropriately awarded and administered.

Army Comments. The Deputy Assistant Secretary of the Army (Policy and Procurement) concurred, stating that the Army Management and Oversight of Services process and its implementation are critical for ensuring that Army acquisitions are properly awarded and administered.

Navy Comments. The Chief of Staff/Policy for the Deputy Assistant Secretary of the Navy for Acquisition Management concurred in principle, stating the Navy now has management controls in place that ensure appropriate award and administration of services contracts.

Air Force Comments. The Associate Deputy Assistant Secretary of the Air Force for Acquisition Integration concurred, stating that the Air Force is aware of the problems identified in the report and has already started addressing them.

Defense Microelectronics Activity Comments. The Director, Defense Microelectronics Activity nonconcurred, stating that the contracts identified in the report were administered by either the Defense Contract Management Agency or the Office of Naval Research in accordance with FAR Part 42. The procurement contracting officer, administrative contracting officer, and project engineer serve as a team in oversight of their assigned contracts. The cognizant administrative contracting officer accomplishes the on-site surveillance and payment.

Audit Response. The Defense Microelectronics Activity comments are nonresponsive. Administrative contracting officers have no control over the award of contracts and the contracting activity can certainly institute controls that ensure the administrative contracting officers accept delineated responsibilities for contract administration. We request that the Director reconsider his position and provide additional comments to the final report.

Appendix A. Scope and Methodology

Using the DD-350 [Individual Contracting Action Report] database, we judgmentally selected 113 contract actions awarded during FY 2000 and FY 2001. We used judgmental sampling to limit the number of sites visited and to ensure that we selected only contract actions valued at more than \$250,000. The 113 contract actions included 69 contracts that had an estimated value of \$17.8 billion and 44 task orders valued at \$100.1 million issued from those contracts. We focused on three major service categories: Program Management/Support Services (Service Category Code R-408), Systems Engineering Services (Service Category Code R-414), and Engineering Technical Services (Service Category Code R-425). We performed this audit from August 2002 through August 2003 in accordance with generally accepted government auditing standards. Our audit included four steps:

1. The first step determined if contracting officials attempted to use historical information to define requirements. For each contract action reviewed, we determined if historical information from other contracts was available. If historical information was available, we determined if contracting officials considered the information when they chose the contract type.
2. The second step determined if contracting officials appropriately competed contracts. If contracting officials awarded a contract competitively and received multiple proposals, we determined if they considered price during the source selection process. If contracting officials awarded a contract competitively and received only one proposal, we determined if a realistic expectation that multiple bids would be received existed. If contracting officials awarded a contract on a noncompetitive basis, we evaluated the sole-source justification.
3. The third step determined if contracting officials adequately supported their determinations that contract prices were fair and reasonable. For each contract action reviewed, we determined if the contract file included a certification that the price was fair and reasonable. We then determined if contracting officials adequately supported their certification that the price was fair and reasonable.
4. The fourth step determined if contracting officials performed adequate surveillance on cost-reimbursement contracts. We focused on whether contracting officials used surveillance techniques that adequately ensured cost control. We determined if contracting officials had controls in place that would ensure contractors worked efficiently and ensured that contractors charged the Government only for actual allowable costs.

We performed the steps by reviewing contract files and by interviewing contracting officials and program officials. We reviewed basic contracts, task orders, statements of work, PNMs, technical reviews, source selection documents, cost analyses, and miscellaneous correspondence.

Limitations of Scope. We did not review the adequacy of contracting officials' price reasonableness determinations and surveillance measures for 23 contract

actions that were indefinite-delivery/indefinite quantity contracts because we performed this analysis when reviewing orders issued from those contracts.

Our review of Government surveillance consisted of interviews of program office and contract administration office officials, whose names were provided to the audit team by contracting officials assigned to the contracts reviewed. We could not verify that surveillance was adequate if we could meet with and examine surveillance files of the officials who performed the surveillance. Therefore, we could not determine the adequacy of surveillance in situations where interviews were performed by telephone or e-mail.

Use of Computer-Processed Data. Although we relied on data retrieved from the DD-350 database during the audit, we did not evaluate the general and application controls relating to this information system that processes contract action reports. We used the DD-350 database as only a starting point to obtain the universe data and contract actions selected. Therefore, we did not evaluate the controls.

General Accounting Office (GAO) High-Risk Area. The GAO has identified several high-risk areas in DoD. This report provides coverage of the high-risk area to “Improve processes and controls to reduce contract risk.”

Management Control Program Review

DoD Directive 5010.38, “Management Control (MC) Program,” August 26, 1996, and DoD Instruction 5010.40, “Management Control (MC) Program Procedures,” August 28, 1996, require that DoD organizations implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls.

Scope of the Review of the Management Control Program. We reviewed management control procedures related to contract actions awarded for three major service categories: Program Management/Support Services (Service Category Code R-408), Systems Engineering Services (Service Category Code R-414), and Engineering Technical Services (Service Category Code R-425). We were concerned about whether contracting officials were following prescribed procedures for awarding and managing contracts for services. We specifically reviewed adequacy of the contract type, market research techniques, competition, price reasonableness determinations, and Government surveillance. We reviewed management’s self-evaluation applicable to those controls.

Adequacy of Management Controls. We identified a material management control weakness for the Military Departments and the Defense Microelectronics Activity as defined by DoD Instruction 5010.40. Military Departments and the Defense Microelectronics Activity management controls were inadequate for ensuring that requirements for contracts were defined and price reasonableness determinations were supported. Also, controls did not ensure that adequate surveillance was performed on contracts, particularly cost reimbursable and T&M type contracts. Recommendation 2.d., if implemented, will improve procedures

that the Military Departments and Defense Microelectronics Activity use for awarding and managing contracts. A copy of the report will be provided to the senior official responsible for management controls within the Military Departments and the Defense Microelectronics Activity.

Adequacy of Management's Self-Evaluation. DoD contracting activities did not identify contracts for services as an assessable unit and, therefore, did not identify or report the material management control weaknesses identified by the audit.

Appendix B. Prior Coverage

During the last 5 years, the GAO, the IG DoD, and the Army Audit Agency have issued 12 reports related to service contracts. Unrestricted GAO reports can be accessed over the Internet at <http://www.gao.gov/>. Unrestricted IG DoD reports can be accessed at <http://www.dodig.osd.mil/audit/reports>.

GAO

GAO Report No. GAO-03-935, "Contract Management: High-Level Attention Needed to Transform DoD Services Acquisition," September 10, 2003

GAO Report No. GAO-03-661, "Best Practices: Improved Knowledge of DoD Service Contracts Could Reveal Significant Savings," June 9, 2003

GAO Report No. GAO-02-1049, "Guidance Needed for Using Performance-Based Service Contracting," September 23, 2002

IG DoD

IG DoD Report No. D-2003-113, "Franchise Business Activity Contracts for Medical Services," June 30, 2003

IG DoD Report No. D-2003-099, "Service Contracts at the National Imagery and Mapping Agency," June 6, 2003

IG DoD Report No. D-2003-029, "Contract Actions Awarded To Small Businesses," November 25, 2002

IG DoD Report No. D-2001-189, "Multiple Award Contracts for Services," September 30, 2001

IG DoD Report No. D-2001-129, "Contracting Officer Determinations of Price Reasonableness When Cost or Pricing Data Were Not Obtained," May 30, 2001

IG DoD Report No. D-2001-102, "Service Contracts at the National Security Agency," April 17, 2001 (Confidential)

IG DoD Report No. D-2000-100, "Contracts for Professional, Administrative, and Management Support Services," March 10, 2000

IG DoD Report No. 99-116, "DoD Use of Multiple Award Task Order Contracts," April 2, 1999

Army

Army Audit Agency Report No. A-2002-0580-AMA, "Managing Service Contracts," September 23, 2002

Appendix C. Summary of Problems

Contract Action	Nause of History for Defining Requirements	Inadequate Competition	Questionable Sole-Source Awards	Inadequate Government Cost Estimates	Inadequate Technical Evaluations	Inadequate Price Reasonableness Determinations	Inadequate Surveillance
DAAB07-01-C-C206	•			•	•	•	
DAAB07-01-D-C002	•			•	•		•
Order #10							
DAAB07-01-D-G602				•			
Order #2							
DAAB07-01-D-L660				•			
Order #3							
DAAE07-00-C-M020	•		•	•	•	•	
DAAE07-00-C-M071			•	•	•	•	•
DAAE07-00-C-N131			•	•	•	•	
DAAE07-00-D-T049			•		•		
Order #1							
DAAE07-01-C-M003				•	•	•	
DAAE07-01-C-M035				•	•	•	
DAAE07-01-C-M037			•	•	•	•	
DAAB07-01-D-M008							
Order #1							
DAAH01-00-C-0010	•		•	•	•	•	
DAAH01-00-C-0025	•		•	•	•	•	•
DAAH01-00-D-0021							
Order #27	•			•	•	•	
Order #39	•			•	•	•	
Order #40	•			•	•	•	
DAAH01-01-C-0121	•			•		•	•
DAAH23-00-C-0187	•		•	•	•	•	
DAAF23-01-D-0266	•		•	•			
Order #1	•		•	•		•	
Order #2	•		•	•	•	•	•
Order #3	•		•	•	•	•	•

Appendix C. Summary of Problems (cont'd)

Contract Action	Noause of History for Defining Requirements	Inadequate Competition	Questionable Sole-Source Awards	Inadequate Government Cost Estimates	Inadequate Technical Evaluations	Inadequate Price Reasonableness Determinations	Inadequate Surveillance
Order #5	●		●	●	●	●	
N00024-00-C-2302	●			●			
N00024-00-C-5136	●			●		●	
N00024-00-C-5393	●		●	●	●	●	
N00024-01-C-5162	●		●			●	
N00024-01-C-5402	●		●	●		●	●
N00024-01-D-7019		●					
Order #3	●			●	●	●	
Order #5	●			●	●		●
N00244-00-D-0019	●			●			
Order #68	●			●		●	●
Order #75	●			●	●	●	●
Order #94	●			●	●	●	●
Order #179	●			●	●	●	●
N00244-01-C-0040	●	●		●	●	●	●
N00244-01-D-0029							
Order #2				●	●	●	
Order #3				●	●	●	
Order #4				●	●	●	
N00421-00-C-0184	●			●	●	●	
N00421-00-D-0127	●			●	●	●	
Order #1	●			●	●	●	●
Order #8	●			●	●	●	●
N00421-00-D-0264	●			●			
Order #1	●			●	●	●	●
Order #2	●			●	●	●	●
N00421-00-D-0338	●			●	●	●	●
Order #6	●			●	●	●	
N00421-00-D-0361	●			●	●	●	

Appendix C. Summary of Problems (cont'd)

Contract Action	Nonuse of History for Defining Requirements	Inadequate Competitions	Questionable Sole-Source Awards	Inadequate Government Cost Estimates	Inadequate Technical Evaluations	Inadequate Price Reasonableness Determinations	Inadequate Surveillance
Order #1 N00421-00-D-0577	●			●	●	●	
Order #2	●			●	●	●	●
Order #3	●			●	●	●	●
Order #4	●			●	●	●	●
N00421-01-C-0046	●	●		●			
N66001-00-D-5083	●			●			
Order #1	●			●	●	●	●
Order #11	●			●	●	●	●
Order #14	●			●	●	●	●
Order #19	●			●	●	●	●
N66001-01-D-0023	●			●			
Order #1	●	●		●	●	●	●
N66001-01-D-5022	●			●			
Order #4	●			●			
Order #5	●			●			
Order #6	●			●			
F09603-00-C-0026	●			●	●	●	
F09603-00-C-0247	●		●	●	●	●	
F09603-00-D-0296	●			●			
Order #3				●	●	●	
F09603-01-C-0106				●	●	●	
F09603-01-C-0338	●			●	●	●	
F09603-01-C-0402	●			●	●	●	
F09603-01-C-0518				●	●	●	
F09603-01-D-0211				●	●	●	
Order #1		●		●	●	●	
F33657-00-C-3005			●	●	●	●	
F33657-00-C-4005			●	●	●	●	

Appendix C. Summary of Problems (cont'd)

Contract Action	House of History for Defining Requirements	Inadequate Competition	Questionable Sole-Source Awards	Inadequate Government Cost Estimates	Inadequate Technical Evaluations	Inadequate Price Reasonableness Determinations	Inadequate Surveillance
F33657-00-C-4026	●		●	●	●	●	
F33657-00-C-4037			●	●	●	●	
F33657-00-C-4050			●	●	●	●	
F33657-00-C-4053			●	●	●	●	
F33657-01-C-5003			●	●	●	●	
F33657-01-C-5006	●			●			
F34601-01-C-0008				●			
F34601-01-C-0026				●	●	●	
F34601-01-C-0030			●	●	●	●	
F34601-01-C-0034				●	●	●	
F42610-00-C-0011				●	●	●	●
F42610-01-C-0004				●			
F42620-00-C-0106	●			●	●	●	
F42620-01-C-0002				●	●	●	
F42620-01-D-0026				●	●	●	
Order #3				●	●	●	
Order #7	●			●	●	●	
DMEA90-00-C-0005				●	●	●	●
DMEA90-00-C-0102				●	●	●	●
DMEA90-01-C-0006				●	●	●	●
DMEA90-01-C-0009			●	●	●	●	●
DMEA90-01-C-0010			●	●	●	●	●
DMEA90-01-D-0001				●	●	●	
Order #1				●	●	●	
DMEA90-01-D-0002				●	●	●	
Order #1				●	●	●	●
Totals	61	5	27	89	73	79	29

Appendix D. Status of Report No. D-2000-100 Recommendations

Report No. D-2000-100, “Contracts for Professional, Administrative, and Management Support Services,” was issued March 10, 2000. The following are recommendations from the report and actions taken in response to those recommendations or the status of planned actions.

Deputy Under Secretary of Defense (Acquisition Reform) Recommendations

1. We recommend the Under Secretary:

a. Develop a training course on planning and defining requirements and using historical contract for services data.

b. Train contracting and program personnel on the award and administration of Professional, Administrative, and Management Support Services emphasizing future prevention of the types of deficiencies noted in this report.

DoD issued a number of initiatives that provide additional guidance on how to “define, acquire, and manage service acquisitions.” They also developed a desktop Performance-Based Service Acquisition Guidebook. A commercially developed on-line training course for Performance-Based Service Acquisition was also developed and available.

Acquisition Executives Recommendations

2. We recommend that Acquisition Executives for the Army, Navy, and Air Force:

a. Make all acquisition personnel aware of the problems found in independent Government cost estimates, technical evaluations, and price negotiation memorandums.

The Assistant Secretary of the Army (Acquisition, Technology, and Logistics) directed that the Procurement Management Assistance staff, the Principal Assistants Responsible for Contracting, and the U.S. Army Materiel Command Acquisition Reform Implementation Assessment Team add, as a special area of emphasis, the review of contracting procedures for Professional, Administrative, and Management Support Services.

The Office of the Assistant Secretary of the Navy provided a copy of Report No. D-2000-100 to the contracting activities.

The Secretary of the Air Force distributed a memorandum explaining the need for “greater diligence in each of the cited areas.”

b. Evaluate the seven contracts identified that should have been awarded as multiple-award contracts in accordance with the Federal Acquisition Regulation and if feasible, terminate or convert them to multiple-award contracts upon completion.

The Army reviewed the Army contract identified and determined that all actions were completed.

The Navy reviewed the six Navy contracts identified and determined that termination was not appropriate.

c. Establish centers of excellence with personnel that have performed research and received training to become expert buyers of Professional, Administrative, and Management Support Services.

The Army used each of the Major Army Commands to develop one or more of the centers of excellence. The centers are, however, subject to major revisions as a result of the establishment of the Army Contracting Agency.

The Navy is exploring consortiums and a virtual center of excellence. However, the action was delayed as a result of technology infrastructure changes and a departmental reorganization.

The Policy and Implementation Division of the Deputy Assistant Secretary of the Air Force (Contracting) is serving as the Air Force Center of Excellence for service contracting.

d. Require personnel acquiring the Professional, Administrative, and Management Support Services to:

1. Use the centers of excellence.

The Army centers of excellence are subject to major revisions as a result of establishment of the Army Contracting Agency.

The Navy will direct its acquisition community to use the virtual center of excellence when it is deployed. However, as a result of technology infrastructure changes, deployment of the virtual center of excellence was delayed.

The Air Force believes that the mandate is unnecessary and impossible to enforce. However, they stated their intent was to provide a useful Web site that would become the resource of choice for contracting personnel in the field. In addition, training on service contracts was integrated into several annual functional training courses.

2. Establish a time-phased plan with goals and performance measures that require the review of all Professional, Administrative, and Management Support Services contracts.

Office of the Assistant Secretary of the Army Acquisition Logistics and Technology representatives conduct visits to Army contracting offices and survey cost-type contracts as well as advise contracting offices to convert cost-type contracts to firm-fixed-price whenever possible.

The Navy distributed a memorandum encouraging the acquisition community to review the report and ensure that concerns are addressed in planning and awarding contracts. Furthermore, the Navy will review procurement history and fixed-price service requirements to the maximum extent possible. Follow-on contracts for existing contracts will be reviewed within the 5-year cycle.

The Air Force partially concurred with the recommendation and did not intend to review all contracts. Instead, they did the following:

- a. Issued a memorandum to the Directors for Contracting at the Centers outlining the Directors' responsibilities for training and self-inspection;
- b. Developed a special interest item checklist for the Office of Inspector General of the Air Force Materiel Command to use in monitoring compliance with service contract requirements outlined in Air Force Instruction 63-124, "Performance-Based Service Contracts (PBSC)," April 1, 1999, at the reviewed Centers;
- c. Held detailed discussions at two reviews at the executive director level on IG DoD findings and corrective actions; and
- d. Required that Centers develop plans for correcting deficiencies and increasing the robustness of the process for acquiring services.

3. Convert, over 3 to 5 years, those repetitive cost reimbursable contracts, or portions of contracts, to fixed price.

The Army strongly encourages migration of cost-type contracts to firm-fixed-price contracts and has reemphasized that policy to field contracting organizations. However, the Army will not direct that contracting officers award firm-fixed-price contracts because the contract type is a judgment call made by the contracting officer.

The Navy reviews acquisitions for supplies or services with the intent of selecting the most appropriate type of contract based on specific circumstances for the requirement. A field memorandum that encourages contract personnel to review available procurement history and use fixed-price contracts to the maximum extent possible was distributed.

The Air Force distributed an electronic memorandum to the Air Force senior leadership in contracting that identifies concerns on the use of long-term cost reimbursable contracts. The memorandum stresses that careful consideration is

given to converting the contracts to fixed price. In addition, the Secretary of the Air Force (Acquisition) conducted a Performance-Based Service Acquisition training program designed to reach contracting activities and a variety of functional communities that create requirements and acquire service contracts.

4. Review the assignment of contract surveillance work for contracts for services and adjust assigned workload and staffing to resolve imbalances.

The Army established the Army Contracting Agency. The Army has maintained, however, over the last couple of years that it does not have the resources to accomplish the contract surveillance work needed for the service contracts it awards.

The Navy constantly reviews staffing and work assignments with the goal of matching resources with requirements. They also have new and ongoing initiatives that will increase use of performance-based contracting principles and establish a greater reliance of past performance information in source selection that should reduce the need for surveillance. The Navy distributed a field memorandum that encourages acquisition personnel to review Report No. D-2000-100 and to ensure that the planning for, as well as award and administration of, service contracts are appropriately addressed.

The Air Force believes this is an installation-level issue. Air Force Instruction 63-124, "Performance-Based Service Contracts (PBSC)," April 1, 1999, already requires contract surveillance as one of the key management duties of the installation Performance Management Council to provide synergy in addressing installation issues.

e. Develop and implement work measures on contracts for Professional, Administrative, and Management Support Services, and measure improvements through the options, modifications for additional work, and future contracts.

The Army issued a letter encouraging that migration occur when sufficient procurement history exists. The Army also established centers of excellence and emphasized, through procurement management assistance visits, methods for improving performance standards.

The Navy stated that to ensure consistency such work measures should be developed at the DoD level.

The Air Force is spreading Performance Based Service Acquisition policy and implementation throughout the various functional and acquisition communities in the Air Force. The Air Force is conducting a Services Acquisition Road Show that details the policy and elements of service contract-related issues.

Appendix E. Summary of Recent Statutory and DoD Guidance on Service Contracts

From FY 1992 to FY 2002, DoD expenditures for services steadily increased. Legislation enacted from FY 2001 through FY 2003 specifically addresses acquisition of services. The legislation addresses establishment and use of centers of excellence that specialize in services, training for service contracting, establishment and implementation of a management structure for the procurement of services, achievement of efficiencies in the procurement of services before awarding multiple-award contracts through the use of performance-based services contracting, and competition for task orders under service contracts.

National Defense Authorization Act for FY 2001. The National Defense Authorization Act for FY 2001 (Public Law 106-398), October 30, 2000, section 821(c), “Centers of Excellence in Service Contracting,” required that not later than 180 days after the date of the enactment of this Act, the Secretary of each Military Department shall establish at least one center of excellence in contracting for services. Each center of excellence shall assist the acquisition community by identifying, and serving as a clearinghouse, the best practices in contracting for services in both the public and private sectors.

Section 821(d), “Enhanced Training in Service Contracting,” required that the Secretary of Defense ensure classes focusing specifically on contracting for services are offered by the Defense Acquisition University and the Defense Systems Management College and are available to contracting personnel throughout DoD. In addition, Congress directed that the Secretary of each Military Department and the head of each Defense agency ensure that the personnel of each department or agency responsible for awarding and managing contracts for services receive appropriate training focused specifically on contracting for services.

National Defense Authorization Act for FY 2002. The National Defense Authorization Act for FY 2002 (Public Law 107-107), December 28, 2001, section 801(b), “Requirement for Management Structure,” required that the Secretary of Defense establish and implement a management structure for the procurement of services for DoD. The management structure would require a designated official for each Military Department, Defense agency, and DoD Component. The designated official would be responsible for managing the procurement of services and developing a way in which employees in Military Departments, Defense agencies, and DoD Components can be held accountable for carrying out the requirements for the procurement of services, and establishment of specific dollar thresholds and other criteria for advance approvals of purchases. The Secretary of Defense was required to establish and implement the management structure no later than 180 days after the enactment of the Act. Also, the Under Secretary of Defense for Acquisition, Technology, and Logistics was required to issue management structure guidance to officials on how to carry out their responsibilities. As reported in GAO Report No. GAO-03-935:

“Contract Management: High-Level Attention Needed to Transform DoD Services Acquisition,” September 10, 2003, DoD had not issued such guidance as of September 2003.

Section 802(a), “Savings Goals for Procurements of Services,” required that DoD establish savings goals through the use of improved management practices for procurements of services, including performance-based services contracting; competition for task orders under service contracts; and program review, spending analyses, and improved management of services contracts.

Section 802(b), “Annual Report,” established that the Secretary of Defense must submit a progress report to the congressional Defense committees no later than March 1, 2002, and then annually through March 1, 2006. The report should show the progress made toward meeting the objective and goals established for savings of procurements of services. Each report should at a minimum include the following:

- (1) a summary of steps that would improve the management of procurements of services in the fiscal year of the report and the following fiscal year,
- (2) an estimate of the expenditures for procurements of services in the fiscal year of the report and the following fiscal year, and
- (3) an estimate of savings as a result of improvement of management practices for the procurement of services in the fiscal year of the report and in the following fiscal year.

Section 803, “Competition Requirement for Purchase of Services Pursuant to Multiple Award Contracts,” required that not later than 180 days after the date of the enactment of the Act, the Secretary of Defense should publicize in the DoD Supplement to the FAR regulations that would require competition when purchasing services by DoD before awarding multiple-award contracts. The regulations would require that each individual purchase of services in excess of \$100,000 prepared under a multiple-award contract should be made on a competitive basis. A DoD contracting officer can waive the requirement under certain conditions.

National Defense Authorization Act for FY 2003. The National Defense Authorization Act for FY 2003 (Public Law 107-314), December 2, 2002, section 805, “Performance Goals for Procuring Services Pursuant to Multiple Award Contracts,” amended subsection (a) of section 802 of the National Defense Authorization Act for FY 2002. The DoD objective should now be to achieve efficiencies in procurements of services before awarding multiple-award contracts through the use of performance-based services contracting; competition for task orders under service contracts; and program review, spending analyses, and improved management of services contracts. Therefore, DoD should have the following goals for procurement of services made under multiple-award contracts: increase the percentage of purchases of services made under a competitive basis

where more than one offer is obtained from qualified contractors and increase the percentage of purchases of services specifying firm-fixed prices for specific tasks performed on the contract.

Performance-Based Service Acquisition Plan, April 2000. The Under Secretary of Defense for Acquisition, Technology, and Logistics issued a memorandum on April 5, 2000. The memorandum states that DoD policy emphasizes maximized performance, innovation, and competition as well as the use of performance-based strategies for the acquisition of services whenever possible. The Under Secretary of Defense for Acquisition, Technology, and Logistics established that a minimum of 50 percent of service acquisitions by the year 2005 should be performance-based. To achieve the goal, the Military Departments and the Defense Logistics Agency should develop an acquisition implementation plan for performance-based services that would increase the use of acquisition strategies no later than 60 days from the date of the memorandum. The memorandum also discusses the importance of training for increasing performance-based acquisition for services. The National Association of Purchasing Management and the National Contract Management Association have developed a Performance-Based Services Acquisition course. The relevant personnel are required to take within 12 months of the memorandum that particular course or an equivalent performance-based services acquisition training course.

Guidebook for Performance-Based Services Acquisition, December 2000. The Under Secretary of Defense for Acquisition, Technology, and Logistics issued a memorandum dated January 2, 2001. In the memorandum, the Under Secretary states that DoD developed a guidebook for performance-based services acquisition to provide a better understanding of the basic principles of performance-based services acquisition. The guidebook was designed to promote performance-based strategies for services acquisitions; educate acquisition workforce on performance-based services acquisition; encourage innovative business practices; promote the use of the commercial market place; and increase awareness that performance-based services acquisitions require participation from the users, acquisition workforce personnel, and industry to ensure that the requirement is met.

Integrated Process Team, January 2001. The Under Secretary of Defense for Acquisition, Technology, and Logistics issued a memorandum dated January 5, 2001. The memorandum states that to ensure high quality in the acquisition of services, the Under Secretary would establish an ongoing Integrated Process Team. The team would focus on identifying best practices, developing guidance, reviewing training, and identifying additional policy needs for performance-based service acquisitions. DoD used the Integrated Process Team results to develop current service acquisition policy.

Services Contracts Oversight Process, May 2002. The Under Secretary of Defense for Acquisition, Technology, and Logistics issued a memorandum dated May 31, 2002. In the memorandum, the Under Secretary states that section 801 through section 803 of the National Defense Authorization Act for FY 2002 established requirements that would affect DoD acquisition of services. Therefore, within 60 days of the date of the memorandum, each of the Military

Departments was directed to propose a Services Contracts Oversight Process. The Services Contracts Oversight Process is a process and a set of procedures for managing and overseeing the acquisition of service acquisitions. DoD used the responses to this memorandum to develop new policy as stated in the August 2003 performance based service acquisitions memorandum.

Performance-Based Service Acquisitions, August 2003. The Under Secretary of Defense for Acquisition, Technology, and Logistics issued a memorandum dated August 19, 2003, that updates goals for performance-based service acquisitions. The current goals for the use of performance-based service acquisitions are:

FY 2003	25 percent of dollars awarded
FY 2004	35 percent of dollars awarded
FY 2005	50 percent of dollars awarded

Measurement against the above goals will be based solely on the percentage of contract dollars awarded using performance-based service acquisitions, excluding services the Office of Federal Procurement Policy identified as not particularly well suited to performance-based service acquisitions. In addition, the memorandum encourages the use of statements of objectives and provides a goal to train all personnel who prepare statements of work appropriate training on preparing performance-based statements of work by September 30, 2005.

GAO Report No. GAO-03-935: “Contract Management: High-Level Attention Needed to Transform DoD Services Acquisition,” September 10, 2003. As mandated by the National Defense Authorization Act for FY 2002, GAO assessed DoD compliance with the requirements of Public Law 107-107, section 801. The GAO concluded that DoD does not have a plan for a DoD-wide assessment of how spending for services could be more effective. The GAO reported that DoD lacks a plan that both coordinates each of the Military Department’s on-going initiatives and provides a road map for future efforts. The GAO recommended that DoD strengthen its contracting management structure for services to promote use of best practices such as centralizing key functions, conducting spend analyses, using commodity teams, achieving strategic orientation, reducing purchasing costs, and improving performance.

Appendix F. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition, Technology, and Logistics
Director, Acquisition Education, Training, and Career Development
Director, Defense Procurement and Acquisition Policy
Under Secretary of Defense (Comptroller)/Chief Financial Officer
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)

Department of the Army

Assistant Secretary of the Army (Financial Management and Comptroller)
Auditor General, Department of the Army

Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)
Auditor General, Department of the Air Force

Unified Command

Inspector General, U.S. Joint Forces Command

Other Defense Organizations

Director, Defense Contract Audit Agency
Director, Defense Microelectronics Activity

Non-Defense Federal Organizations and Individuals

Office of Management and Budget
Office of Federal Procurement Policy

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Efficiency and Financial Management Committee
on Government Reform
House Subcommittee on National Security, Emerging Threats, and International
Relations, Committee on Government Reform
House Subcommittee on Technology, Information Policy, Intergovernmental Relations,
and the Census, Committee on Government Reform

Under Secretary of Defense for Acquisition, Technology, and Logistics Comments



ACQUISITION,
TECHNOLOGY
AND LOGISTICS

OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000

September 23, 2003

DPAP/P

MEMORANDUM FOR PROGRAM DIRECTOR, CONTRACT MANAGEMENT
DIRECTORATE, DODIG

THROUGH: DIRECTOR, ACQUISITION RESOURCES AND ANALYSIS *WBS 9/25/03*

SUBJECT: DoDIG Draft Report No. D2002CF-0216, Contracts for Professional,
Administrative, and Management Support Services

This is in response to your request for comments on the Draft Report, "Contracts for Professional, Administrative, and Management Support Services," dated August 11, 2003, (OIG Project No D2002CF-0216). My comments to the OUSD(AT&L) recommendations are attached.

My point of contact is Mr. William C. Timperley who can be reached at (703) 697-8336 or via e-mail at william.timperley@osd.mil.

Deidre A. Lee
Director, Defense Procurement and
Acquisition Policy

Attachment:
As stated

OUSD(AT&L) COMMENTS TO THE RECOMMENDATIONS ON

OIG DRAFT REPORT (PROJECT NO. D2002CF-0216)
DATED AUGUST 11, 2003

“CONTRACTS FOR PROFESSIONAL, ADMINISTRATIVE AND MANAGEMENT
SUPPORT SERVICES”

RECOMMENDATION 1a: We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics monitor the establishment and use of centers of excellence in service contracting as required by section 821(c) of the National Defense Authorization Act of FY 2001 (Public Law 106-398).

OUSD(AT&L) RESPONSE: Concur. The Director, Defense Procurement and Acquisition Policy will send a memorandum to the Military Departments and Defense Agencies in the next 10 working days asking them to report on their efforts to establish centers of excellence, how such centers have been used, and the experience gained at the centers.

RECOMMENDATION 1b: We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics train program office personnel on using performance-based contracting methods for service contracts, including how to develop performance-based statements of work and performance measures.

OUSD(AT&L) RESPONSE: Concur. In a August 19, 2003 memorandum (attached), the Under Secretary of Defense for Acquisition, Technology, and Logistics established a requirement that 50 percent of all personnel who prepare statements of work, including program office personnel, be trained on performance based service acquisitions by September 30, 2004, and that the remaining 50 percent be trained by September 30, 2005.

RECOMMENDATION 1c: We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics require that contracting officers designate in writing any personnel who perform Government surveillance on cost reimbursable and time-and-materials contracts and include a list of duties and limitations.

OUSD(AT&L) RESPONSE: Concur. The Director, Defense Procurement and Acquisition Policy will issue guidance in the next 10 working days emphasizing that in accordance with DFARS 201.602-2(5), all contracting officers shall designate representatives in writing, and shall specify the contracting officer representatives (CORs) authority and limitations.

RECOMMENDATION 1d: We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics require that contracting officer's representative and others performing surveillance be specifically trained to perform contract surveillance on cost reimbursable and time-and-material services contracts that includes, at a minimum: (1) Basic contract information, including the contract type and the implications on surveillance requirements and (2) Cost risk and any other Government concerns related to contract administration.

OUSD(AT&L) RESPONSE: Concur. The Director, Defense Procurement and Acquisition Policy will issue guidance in the next 10 working days emphasizing that in accordance with DFARS 201.602-2(2), all CORs must be trained for their required duties.

RECOMMENDATION 1e: We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics require that follow-on cost reimbursable and time-and-materials services contracts be approved at a level above the contracting officer to ensure that efforts are being made to award fixed-price contracts.

OUSD(AT&L) RESPONSE: Non-Concur. It is important to use the appropriate contract type based on the criteria specified in the FAR Part 16 and DFARS Part 216. FAR 16.103 specifies the preference to award fixed-price contracts when the risk is minimal or can be predicted with an acceptable degree of certainty and that cost type contracts shall only be used when a reasonable basis for firm pricing does not exist. The contract type decision must be made on a contract by contract basis and the contracting officer is in the best position to make that decision. Nevertheless, as mentioned in the following reply to recommendation 1f, the Director, Defense Procurement and Acquisition Policy will issue a memorandum emphasizing the importance of using the appropriate contract type based on the criteria in the regulations.

RECOMMENDATION 1f: We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics issue a memorandum for senior contracting officials and program managers that clearly defines management responsibilities regarding stewardship of taxpayer dollars and states that fixed-price contracts are in the best interest of the Government and that for a program manager to insist on a cost reimbursable contract when a fixed-price contract is appropriate is a denunciation of his duties.

OUSD(AT&L) RESPONSE: Partially Concur. The Director, Defense Procurement and Procurement Policy will issue a memorandum to the Military Departments and Defense Agencies in the next 10 working days asking them to ensure that the appropriate contract type is used when acquiring services based on the criteria specified in FAR Part 16 and DFARS Part 216.

Department of the Army Comments



DEPARTMENT OF THE ARMY
OFFICE OF THE ASSISTANT SECRETARY OF THE ARMY
ACQUISITION LOGISTICS AND TECHNOLOGY
103 ARMY PENTAGON
WASHINGTON DC 20310-0103

OCT 23 2003

SFCA-CP

MEMORANDUM FOR PROGRAM DIRECTOR, CONTRACT MANAGEMENT
DIRECTORATE, OFFICE OF THE INSPECTOR
GENERAL, DEPARTMENT OF DEFENSE,
400 ARMY NAVY DRIVE, ARLINGTON, VA 22202-4704

SUBJECT: Draft Report on Contracts for Professional, Administrative, and
Management Support Services (Project No. D2002CF-0216)

Thank you for the opportunity to respond to the subject draft audit. I will confine my remarks to those recommendations directed to the Service Acquisition Executives (Recommendations 2.a. through 2.d.).

Recommendation 2.

We recommend that the Acquisition Executives for the Army, Navy, Air Force, and the Defense Microelectronics Activity:

a. Place greater emphasis on defining requirements and the use of fixed-price contracts especially in situations where contracts are follow-on contracts.

Response: Concur with intent. Since at least 1994, it has been the unambiguous policy of the Army to use performance-based contracting methods to the maximum extent practicable. In part, these performance-based methods require that performance requirements define the work in measurable, mission-related terms. We believe that the existing guidance on requirements definition and our on-going emphasis on performance requirements, indicates that we are committed fully to the goal of emphasizing the importance of requirements definition. We continue to believe that the contracting officer remains in the best position to make the determination of contract type. While we also believe that the existing guidance on the selection of contract type is clear, we will continue to stress the importance of selecting the appropriate contract type.

b. Establish and use centers of excellence in service contracting as required by section 821(c) of the National Defense Authorization Act for Fiscal Year 2001 (FY01) (Public Law 106-398).

Response: Concur. In November 2000, we directed our Major Commands (MACOMs) to develop one or more Centers of Excellence in Service Contracting in accordance with section 821(c) of the FY 2001 Authorization Act.

The intent of these centers is to function as a clearinghouse by soliciting, identifying, consolidating, organizing and disseminating best practices and lessons learned in service contracting.

c. Make program and contracting officers aware of any recurring problems in the development of independent Government cost estimates, technical evaluations and price negotiation and implement an enforcement program to ensure that these problems do not reoccur.

Response: Concur. The Army Procurement Management Assistance Program (PMAP) provides consultant services for the Army to enhance the procurement process. The PMAP provides assistance and assessment of the effectiveness and efficiency of Army-wide procurement through outcome-based analysis, i.e., assessing actual achievement against stated goals. As part of this program, our Heads of Contracting Activities (HCAs) are to review contracting compliance with the FAR, DFARS, AFARS, Command Supplements and Army Policy. They also identify and communicate procurement best practices, lessons learned, and associated issues. Updates to policy that correct problems (revealed through audits, reports, or PMAP) are made through updates to policy letters, or through notices in our newsletters. Enforcement is undertaken through current internal controls. We believe that our existing assistance and assessment program accomplishes the goal of improving our effectiveness and efficiency without the establishment of a new enforcement program.

d. Develop and employ adequate management controls that ensure service contracts are appropriately awarded and administered.

Response: Concur. The OSD-approved Army Management and Oversight of Services (AMOAS) process and its strategic implementation is critical to ensuring that our service acquisitions are appropriately awarded and administered, are of the highest quality, and are in the best interest of the Army and DOD. We believe that the AMOAS and the aforementioned PMAP will continue to provide adequate management controls for Army service acquisitions.

We are confident that through the use of our AMOAS, PMAP, on-going training and leadership, the Army will address all valid issues you have pointed out. Thank you again for the opportunity to comment on this report.

The point of contact for this action is Mr. Robert Friedrich, SFCA-CP, (703) 681-6700, DSN 761-6700, e-mail: robert.friedrich@saalt.army.mil.



E. Ballard
Deputy Assistant Secretary of the Army
(Policy and Procurement)

Department of the Navy Comments



DEPARTMENT OF THE NAVY
OFFICE OF THE ASSISTANT SECRETARY
RESEARCH, DEVELOPMENT AND ACQUISITION
1300 NAVY PENTAGON
WASHINGTON DC 20355-1000

OCT - 7 2003

MEMORANDUM FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL,
PROGRAM DIRECTOR, CONTRACT MANAGEMENT
DIRECTORATE

Subj: DODIG DRAFT AUDIT REPORT ON CONTRACTS FOR PROFESSIONAL,
ADMINISTRATIVE, AND MANAGEMENT SUPPORT SERVICES (PROJECT
NO. D2002CF-0216)

Ref: (a) DoDIG Draft Audit Report dated August 11, 2003

Encl: (1) DoN COMMENTS ON SUBJECT DODIG DRAFT AUDIT REPORT

The enclosed comments are provided in response to
reference (a).


M. F. GAGGARD
Chief of Staff/Policy for
Deputy Assistant Secretary of the Navy
(Acquisition Management)

Copy to:
NAVIG

DEPARTMENT OF THE NAVY COMMENTS ON DODIG
DRAFT AUDIT REPORT ON CONTRACTS FOR PROFESSIONAL,
ADMINISTRATIVE, AND MANAGEMENT SUPPORT SERVICES
(PROJECT NO. D2002CF-0216), AUGUST 11, 2003

The following comments are in response to recommendation 2 of the draft audit report.

Recommendation 2. We recommend that the Acquisition Executives for the Army, Navy, Air Force and the Defense Microelectronics Activity:

- a. Place greater emphasis on defining requirements and the use of fixed-price contracts especially in situations where contracts are follow-on contracts.**

Concur in principle. We believe existing policy and guidance on defining requirements and use of fixed price contracts is adequate. While use of fixed price contracts, especially in follow-on situations, has advantages, there are often circumstances mitigating use of a fixed price contract. DoN contracting officers recognize the advantages of fixed price contracts, but make the type of contract decision based upon specific circumstances surrounding the instant requirement and in accordance with FAR Part 16.

- b. Establish and use centers of excellence in service contracting as required by section 821(c) of the National Defense Authorization Act for FY 2001 (Public Law 106-398).**

Concur. DoN Virtual Center of Excellence for Services Contracting will be discussed at the October meeting of the Naval Contracting Council. The Center of Excellence is scheduled to be fielded first quarter, FY 2004.

- c. Make program and contracting offices aware of recurring problems in the development of independent Government cost estimates, technical evaluations and price negotiation and implement an enforcement program to ensure that these problems do not reoccur.**

Partially Concur. We believe the DoN Virtual Center of Excellence will provide a good forum for sharing issues and lessons learned in the acquisition of services. In

Enclosure (1)

addition, the DoN Procurement Performance Management Assessment Program (PPMAP) provides contracting activities additional insight to the operation of its procurement function. PPMAP requires contracting activities to perform a continuous self-assessment through procurement performance-based measurements. The procurement organization is expected to use the results of this self-assessment to continuously evaluate the quality of its procurement processes and management systems and to know when corrective action is appropriate. For more information on the DoN PPMAP, see www.abm.rda.hq.navy.mil/abm98_4a.html.

We do not concur with establishing an enforcement program. Rather, we believe that communication between contracting activities and effective management assessment will continue to improve DoN Procurement processes.

d. Develop and employ adequate management controls that ensure service contracts are appropriately awarded and administered.

Concur in principle. We believe DoN has management controls in place that ensure appropriate award and administration of services contracts.

- The DoN Management and Oversight Process, implemented under Section 801(d) of the National Defense Authorization Act for FY200, Pub. L. 107-107, ensures that DoN services acquisitions are of the highest quality, support DoN objectives and are properly planned and administered to ensure intended results. You can see DoN MOPAS at <http://www.abm.rda.hq.navy.mil/policy2003.cfm>, scroll down to Acquisition of Services, March 10, 2003.

- PPMAP focuses on contracting activity leadership, strategic planning and management of key procurement processes, all key issues in the proper award and administration of service and supply contracts. Award and administration of services contracts is a special interest item for DoN PPMAPs.

Department of the Air Force Comments



Office Of The Assistant Secretary

DEPARTMENT OF THE AIR FORCE
WASHINGTON, DC

30 SEP 2003

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING
OFFICE OF THE INSPECTOR GENERAL
DEPARTMENT OF DEFENSE

FROM: SAF/AQX
1060 Air Force Pentagon
Washington, DC 20330-1060

SUBJECT: DoD(IG) Draft Report on Contracts for Professional, Administrative, and
Management Support Services (Project No. D2002CF-0216)

This is in reply to your memorandum requesting the Assistant Secretary of the Air Force (Financial Management and Comptroller) provide the AF comments on the subject report.

This report fails to address Section 801 of the FY 02 National Defense Authorization Act and the actions that the AF has taken and is taking to satisfy the mandates of this section: to provide oversight and management of services acquisitions. SAF/AQ established the Program Executive Office for Services (PEO/SV) to provide oversight and management of the acquisition of services over \$100M or 300 Full Time Equivalents (FTEs). In addition SAF/AQ delegated the oversight and management responsibilities for services acquisitions to the other PEOs for all services acquisitions in their portfolio. For acquisitions under \$100M or less than 300 FTEs the Heads of Contracting Activities (HCA) have the oversight and management responsibility. PEO/SV developed the Management and Oversight of the Acquisition of Services (MOASP) to outline how the Air Force proposes to gain insight into services acquisitions over \$100M or 300 Full Time Equivalents. SAF/AQC is in the process of having the AFFARS amended to incorporate the MOASP.

The legislation also mandates that the officials are designated by the department approve acquisitions that are not performance-based. The DAR Council is in the process of publishing an interim rule defining the roles and responsibilities of this official. SAF/AQC is in the process of having the AFFARS amended to identify the officials for Air Force. These officials have specific statutory obligations to review and approve all services acquisitions and ensure they are performance-based. Many of the issues identified in this DoD(IG) follow-up are being addressed in this policy and the subordinate commands implementing instructions.

During the past year, SAF/AQC and the AFPEO/SV have identified specific and general education and training requirements relative to services contracting. Both activities have instituted stopgap measures by developing internal training packages in source selection techniques, past performance evaluation, and developing performance objectives and metrics. The AF has also requested that the Defense Acquisition University allocate more resources to develop and add to its new training curriculum that address services contracting policy and procedures. We have also identified the need for the non-acquisition workforce to obtain access

to training to ensure functional personnel have the requisite skills to participate in acquisition planning, execution and post-award management.

We offer the following comments on the draft recommendations:

Recommendation 1a & 1c. No comment

Recommendation 1b. We concur with reservations that additional training is necessary in the area of Performance-Based Services Acquisition (PBSA). However, the report fails to address all that AF is doing to improve training.

SAF/AQC is in the process of revising AFI 63-124, PBSA that expands the application of PBSA throughout the life of the acquisition. We are also developing a PBSA guide that outlines the philosophy of PBSA, discusses the elements of PBSA and provides various approaches available for meeting the requirements of PBSA. There are specific chapters providing details in performance assessment and contract management. All services acquisitions over \$100K will require a performance plan that details how the contractor's performance will be assessed and how the acquisition team will manage the contract after award.

SAF/AQC and the PEO/SV held a Services Symposium in Jan of this year with industry, MAJCOM contracting representatives, and their customers to identify initiatives Air Force must implement to develop an effective services program. One of SAF/AQC Services Initiatives is to validate the numerous commercial PBSA courses, and have the acquisition team take a PBSA course to ensure members understand the requirements, during acquisition strategy development.

Recommendation 1d. Concur.

Recommendation 2a-d. Concur. However, we are aware of the problem(s) identified here and have already started addressing them. AFMC has developed a Pricing Analysis Methods (PAM) course and converted to a web-based course offered through AFIT. This course identifies issues related to pricing. These tools have been made available AF-wide. We also have placed special emphasis on pricing in the SAF/AQC Contract Assessment Program. The AF has also developed a team to define pricing issues. One of the recommendations is the need to develop performance and responsibilities training for technical personnel.

Please feel free to contact us if you have any additional questions. My POC is Mr. Michael Kratz, SAF/AQXD, (703) 588-7121.



RICHARD W. LOMBARDI, Col, USAF
Associate Deputy Assistant Secretary
(Acquisition Integration)
Assistant Secretary (Acquisition)

Defense Microelectronics Activity Comments



DEFENSE MICROELECTRONICS ACTIVITY

4234 54th STREET
MCCELLELLAN, CALIFORNIA 95652-2100

27 Aug 03

FROM: Defense Microelectronics Activity
4234 54th St.
McClellan CA 95652-2100

MEMORANDUM FOR DoD Inspector General Contract Management Directorate
(Terry L. McKinney)

SUBJECT: Defense Microelectronics Activity (DMEA) Response to DoD Inspector
General IG Project No. D2002CF-0216 (Contracts for Professional, Administrative, and
Management Support Services)

Thank you for the opportunity to respond to subject audit. Attached are the responses as requested in the DoD IG Draft Report on the Contracts for Professional, Administrative, and Management Support Services. If you have any questions concerning the response contact Kellie M. Valdez, Chief, Microelectronics Contracting Division at (916) 231-1523 or email Valdez@dmea.osd.mil.

A handwritten signature in black ink, appearing to read "Ted Glum".

TED GLUM
Director
Defense Microelectronics Activity

Attachment
Response to Recommendation

Response to Recommendation. Listed below are the recommendations of the DoD Inspector General Draft Proposed Project No. D2002CF-0216 dated August 11, 2003 and DMEA's responses to the recommendations as requested.

Recommendation 2 – We recommend that Acquisition Executives for the Army, Navy, Air Force, and the Defense Microelectronics Activity:

- a. Place greater emphasis on defining requirements and the use of fixed-price contracts especially in situations where contracts are follow-on contracts.
- b. Establish and use centers of excellence in service contracting as required by section 821(c) of the National Defense Authorization Act for FY2001 (Public Law 106-398).
- c. Make program and contracting offices aware of any recurring problems in the development of independent Government cost estimates, technical evaluations and price negotiation and implement an enforcement program to ensure that these problems do not reoccur.
- d. Develop and employ adequate management controls that ensure service contracts are appropriately awarded and administered.

DMEA response to 2.a. – DMEA concurs with the audit recommendation. As a part of acquisition planning DMEA contracting officials already review the requirement(s) and available history, if any, to ensure the appropriate pricing arrangement and contract type is used.

DMEA response to 2.b. – DMEA concurs with the audit recommendation. The management of DMEA will ensure that personnel are familiar with and encourage the use of the Army's centers of excellence. This information will be disseminated through management review meetings and included in the quarterly Contracting Information Bulletin (CIB).

DMEA response to 2.c. – DMEA concurs with this recommendation. DMEA reviewed their processes for developing Independent Government Cost Estimates (IGCE), writing technical evaluations and completing price negotiation memorandums. The DMEA Contracting Engineering Services Training has been updated and training was conducted in March. The training provided additional guidance that focused on these specific areas. This training is conducted approximately every 12–18 months, or sooner for new personnel. Additional reviews are being conducted to help ensure that accurate and complete technical evaluation and resulting price negotiation memorandums are accomplished.

DMEA response to 2.d. – DMEA nonconcurs with this finding. The contracts identified, in the report, are administered by either DCMA or ONR; the appropriate office is cited in the contract. DCMA or ONR provide the administration duties IAW the Federal Acquisition Regulation (FAR) Part 42. The Project Engineer stays closely involved with the project. This involvement includes, but is not limited to, attending Technical Interchange Meetings (TIMs), reviewing Monthly Status Reports (MSR) for accuracy and completeness, traveling to the contractor's facility for meetings, and working closely with both the assigned PCO and ACO. The PCO, ACO, and Project Engineer serve as a team in the oversight of their assigned contracts. The on-site surveillance and payment is accomplished by the cognizant ACO.

Team Members

The Contract Management Directorate, Office of the Deputy Inspector General for Auditing of the Department of Defense prepared this report. Personnel of the Office of the Inspector General of the Department of Defense who contributed to the report are listed below.

Robert K. West
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Sharon L. Carvalho