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Acronyms

CDME	Capital and Direct Medical Education
DCAA	Defense Contract Audit Agency
DoD IG	Department of Defense Inspector General
FAR	Federal Acquisition Regulation
J&A	Justification and Approval
PNM	Price Negotiation Memorandum



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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OCT 11 2006

MEMORANDUM FOR DIRECTOR, TRICARE MANAGEMENT ACTIVITY

SUBJECT: Review of Hotline Allegations Concerning the TRICARE Contract Award for the Audit of Capital and Direct Medical Education Costs
(Report No. D-2007-6-002)

We are providing this final report for review and comment. We performed this review based on a Defense Hotline complaint. We considered management comments in preparing this final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. TRICARE provided acceptable alternative action plans to Recommendations 1. through 5. and 7. In accepting the alternative action plans, we request specific information be provided to us on Recommendation 1. We revised Recommendation 6 in response to your comments. We request that you provide comments to revised Recommendation 6., and completion dates for all actions plans by November 5, 2006.

If possible, please send management comments in electronic format (Adobe Acrobat file only). 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.

We appreciate the courtesies extended to the staff. Questions on the review should be directed to Ms. Meredith Long-Morin at 703-604-8739 (meredith.morin@dodig.mil) or Mrs. Carolyn R. Davis at 703-604-8877 (carolyn.davis@dodig.mil). See Appendix C for the report distribution.

A handwritten signature in cursive script that reads "Patricia A. Brannin".

Patricia A. Brannin
Assistant Inspector General
for Audit Policy and Oversight

Office of the Inspector General of the Department of Defense

Report No. D-2007-6-002
(Project No. D2005-DIPOAI-0227.000)

October 11, 2006

Hotline Complaint Concerning the TRICARE Contract Award for the Audit of Capital and Direct Medical Education Costs

Executive Summary

Who Should Read this Report and Why? DoD acquisition officials responsible for follow-up of Defense Contract Audit Agency contract audit findings, Defense Contract Audit Agency management, the Under Secretary of Defense (Acquisition Technology and Logistics), and Director Defense Procurement and Acquisition Policy to whom DoD acquisition officials report should read this report. The report discusses key Federal Acquisition Regulation requirements for evaluating unsolicited proposals, and DoD Directive requirements for dispositioning contract audit findings.

Background. We conducted this review in response to a complaint that the DoD Hotline received. The Hotline complainant alleged that:

- TRICARE awarded a contract to Tichenor and Associates, LLP (an accounting firm) for the audit of Capital and Direct Medical Education costs that did not comply with the Federal Acquisition Regulation (FAR); and
- TRICARE management pressured the contracting officer and other TRICARE employees to award the contract knowing that it did not comply with the FAR.

We also reviewed TRICARE actions taken in response to contract audit reports to determine if it complied with DoD Directive 7640.2, "Policy for Follow-up on Contract Audit Reports," dated February 12, 1988.

Results. We substantiated the first allegation but were unable to substantiate the second. The Tichenor and Associates, LLP unsolicited proposal and resulting contract award did not comply with the FAR. Specifically, the results of our review disclosed that:

- the TRICARE contract file did not support the FAR 15.603(c)(1) requirements that the unsolicited proposal be unique or innovative;
- the unsolicited proposal did not include sufficient technical information in order for the Government to perform a comprehensive evaluation, as FAR 15.603(c)(4) and FAR 15.606-1(a)(4) requires;
- TRICARE commenced negotiations without a favorable technical evaluation as FAR 15.607(b)(1) requires; and

- TRICARE did not adequately justify issuing the Tichenor contract as a sole-source award under the authority of FAR 6.302.1.

In addition, we determined that the incentive fee terms did not properly consider all of the overpayments that the Defense Contract Audit Agency (DCAA) identified, resulting in Tichenor and Associates, LLP receiving additional fees of up to \$4.7 million. TRICARE also did not adequately explain its October 6, 2005 decision to extend the contract, considering that the contractor did not demonstrate it could identify larger Capital and Direct Medical Education overpayments than were identified by DCAA.

Although we could not substantiate the second allegation, the contracting officer did not follow established procedure by requesting approval for the contract prior to addressing the technical evaluator's concerns or preparing a Justification and Approval.

Section V, "Other Findings to be Reported," of this report discusses our review of TRICARE compliance with DoD Directive 7640.2. TRICARE actions taken on several contract audit reports did not comply with DoD Directive 7640.2. For example, TRICARE did not take timely action to recover Capital and Direct Medical Education payments identified by DCAA, which contributed to Tichenor receiving additional fees of up to \$4.7 million. TRICARE should also modify its performance appraisals of acquisition personnel to measure their performance in resolving and dispositioning contract audit reports as DoD Directive 7640.2 requires.

Management Comments and Department of Defense Inspector General (DoD IG)

Response. TRICARE believes that the Tichenor and Associates, LLP contract award complied with the FAR. However, in response to Recommendations 1. and 2., TRICARE stated that the contracting officer will re-evaluate the Tichenor contract to determine if terminating it for convenience is in the best interests of the Government. After completing the re-evaluation, we request that TRICARE provide us with a written justification that fully supports its decision.

In response to Recommendations 3. and 5., TRICARE stated it will review and modify its procedures for handling unsolicited proposals and dispositioning contract audit reports. For Recommendation 4., TRICARE will ensure that future evaluations of unsolicited proposals are adequately documented and comply with the FAR. For Recommendation 7., TRICARE stated that it will evaluate all contracting officers on their effectiveness in resolving and dispositioning contract audits.

Finally, we revised Recommendation 6. based on TRICARE's comments. We request that TRICARE provide comments in response to revised Recommendation 6., and completion dates for all planned corrective actions by November 5, 2006.

See the Findings section of the report for a discussion of management comments and the Management Comments section for a complete copy of TRICARE's comments to a draft of this report.

Table of Contents

Executive Summary	i
Background	1
Objective	1
Findings	
Allegation 1: Tichenor Proposal	2
Allegation 2: TRICARE Management	7
Other Issues to be Reported	9
Appendixes	
A. Scope and Methodology	15
B. Untimely Disposition of Contract Audits and Inadequate Rationale for Sustained Costs	16
C. Report Distribution	17
Management Comments	
Deputy Director TRICARE Management Activity	18

BACKGROUND

Capital and Direct Medical Education Costs. TRICARE authorizes reimbursement of certain Capital and Direct Medical Education (CDME) costs to eligible hospitals. Hospitals eligible for reimbursement of CDME costs include those that are subject to a diagnostic related group based payment system. TRICARE reimburses CDME costs if a hospital submits a request for reimbursement along with the associated Medicare cost report. Medicare cost reports are subject to adjustment based on desk review, audit, or appeals. Hospitals are required to submit an amended CDME payment request if the Medicare cost report is adjusted; however, many hospitals fail to submit an amended request, resulting in uncollected CDME overpayments due to TRICARE.

Defense Contract Audit Agency. The Defense Contract Audit Agency (DCAA) provides audit and financial advisory services to DoD Components, including TRICARE. In May 1999, DCAA alerted TRICARE to the possibility that significant CDME overpayments were not being recovered from hospitals. As agreed to by TRICARE, DCAA conducted 15 audits of CDME costs between February 2000 and November 2002 (see report listing in Appendix A). DCAA conducted the audits in three phases. Phase 1 audits covered hospitals that received CDME reimbursements and were subjected to a Medicare cost audit during 1992 through 1997. Phase 2 audits covered remaining hospitals that received CDME reimbursement during 1992 through 1997. Phase 3 audits covered hospitals that received Medicare cost report updates for 1996 and 1997 and a small number of hospitals for the period 1998 through 1999. The DCAA audits identified approximately \$24 million in CDME net overpayments to hospitals.

Tichenor and Associates, LLP. In January 2000, Tichenor and Associates, LLP (Tichenor), an accounting firm, submitted an unsolicited proposal to TRICARE for the identification of CDME overpayments. In October 2000, TRICARE rejected the January 2000 proposal because TRICARE concluded that the proposal was neither unique nor innovative as Federal Acquisition Regulation (FAR) Subpart 15.6, "Unsolicited Proposals," requires. Tichenor submitted several revised proposals to TRICARE throughout 2001. On November 1, 2002, TRICARE awarded Tichenor a 4-year contract to identify CDME overpayments to hospitals for the period 1992 through 1997, the same period already covered by DCAA. Under the terms of the contract, Tichenor receives a 25-percent incentive fee on CDME overpayments actually recovered by TRICARE in excess of overpayments identified in the DCAA Phase 1 audits. Tichenor receives a full 25-percent fee on all remaining CDME overpayments not identified in the DCAA Phase 1 audits, even if the same overpayments were already identified in the DCAA Phases 2 and 3 audits.

Review Objective. The primary objective was to determine the validity of the Defense Hotline allegations. Our objective also included an evaluation of compliance with DoD Directive 7640.2, "Policy for Follow-up on Contract Audit Report," dated February 12, 1988. See Appendix A for details of our scope and methodology.

FINDINGS

Allegation 1. The Tichenor proposal did not comply with certain FAR requirements for an unsolicited proposal. In addition, TRICARE awarded the contract to Tichenor without competition in noncompliance with the FAR.

The allegation was substantiated. The unsolicited proposal and resulting contract award did not comply with portions of the FAR. The Tichenor proposal did not include sufficient technical information, and TRICARE did not adequately support its conclusion that the proposal was unique and innovative. TRICARE also did not justify issuing the contract as a sole-source award because DCAA and other contractors may have been able to satisfy the agency's requirement. In addition, the incentive fee terms did not properly consider all overpayments previously identified by DCAA, resulting in additional inappropriate fees being paid to Tichenor of up to \$4.7 million.

Facts and Analysis:

FAR Unsolicited Proposal Requirements. FAR Subpart 15.6 sets forth policies and procedures concerning submission, receipt, evaluation, and acceptance or rejection of unsolicited proposals. According to FAR 15.603(c), a valid unsolicited proposal must—

- be innovative and unique;
- be independently originated and developed by the offeror;
- be prepared without Government supervision, endorsement, direction, or direct Government involvement;
- include sufficient detail to permit a determination that Government support could be worthwhile and the proposed work could benefit the agency's research and development or other mission responsibilities;
- not be an advance proposal for a known agency requirement that can be acquired by competitive methods; and
- not address a previously published agency requirement.

Furthermore, before the agency begins a comprehensive evaluation, FAR 15.606-1 requires that the agency perform an initial review of unsolicited proposals to determine compliance with these and other FAR unsolicited proposal criteria.

TRICARE Initial Review of Tichenor's Unsolicited Proposal. The TRICARE initial review of Tichenor's final unsolicited proposal dated October 2, 2001, did not

disclose any noncompliances with FAR Subpart 15.6. However, the TRICARE contract file did not include any documentation to support that determination. At a minimum, the initial review should have disclosed that the proposal did not comply with FAR 15.603(c) because it did not contain sufficient technical information. The proposal did not include any information about Tichenor's claim that it employs a unique database to collect and identify CDME overpayments. Tichenor's refusal to describe the database or provide access to it prevented TRICARE from determining if the proposal reflected unique methodologies or could benefit the Agency's mission responsibilities.

TRICARE Comprehensive Evaluation of Tichenor's Unsolicited Proposal.

Based on its favorable initial review, TRICARE initiated a comprehensive evaluation of the Tichenor proposal in accordance with FAR 15.606-2. The TRICARE Health Benefits Contract Evaluator performed the evaluation and reported the results to the contracting officer in a memorandum dated October 16, 2001. The evaluator took exception to several aspects of the Tichenor proposal based on the evaluation factors listed in FAR 15.606-2. For example, the evaluator commented that:

- the Tichenor proposal did not reflect any unique or innovative methodology;
- the Tichenor proposal did not demonstrate any significant technical accomplishments;
- the proposed approach may be a duplication of previous audits performed by DCAA;
- the proposed approach may result in inaccurate CDME overpayment calculations, a concern also raised by the TRICARE technical consultant, Kennell and Associates, in its memorandum dated January 19, 2001; and
- information used by Tichenor in calculating CDME overpayments is also available to the TRICARE managed care support contractors. According to the evaluator, the managed care support contractors should have been monitoring CDME overpayments as required by their contracts with TRICARE.

The evaluator recommended against accepting the Tichenor proposal unless these and other issues were resolved. The contracting officer notified Tichenor of the issues in a letter dated November 20, 2001. The technical evaluator reviewed the contractor's response dated December 6, 2001, and determined that the response did not adequately resolve the issues. Further, no evidence exists in the TRICARE contract file to suggest that the issues were later resolved before the contract was awarded to Tichenor in November 2002.

Authority for Waiving Full and Open Competition. There was no sufficient basis for waiving full and open competition. To accept an unsolicited proposal, FAR 15.607, "Criteria for acceptance and negotiation of an unsolicited proposal,"

requires that a Justification and Approval (J&A) be prepared based on one of the authorities for waiving full and open competition provided in FAR Subpart 6.3. FAR 6.303-2 requires that the J&A contain sufficient facts and rationale to justify the use of the specific authority cited. As the authority for waiving full and open competition, TRICARE cited FAR 6.302-1, entitled "Only one responsible source and no other supplies or services will satisfy agency requirements." However, the J&A does not contain any facts or rationale to justify the use of this authority. The J&A simply states ". . . the proposed contract will allow Tichenor to utilize their proprietary system to demonstrate a unique capability to perform this service at a level not otherwise currently available to the government." TRICARE had no basis for concluding that Tichenor possessed any unique capabilities for performing the service because Tichenor would not allow TRICARE to access its proprietary database.

The J&A also does not provide any facts or rationale for concluding that Tichenor was the only responsible source for this requirement. Prior to the Tichenor award, DCAA had already completed its review of CDME overpayments for the period 1992 through 1997 and was therefore a potential source for additional years. In addition, at least two other contractors had previously submitted unsolicited proposals to TRICARE for the identification of CDME overpayments, one in 1992 and one in 1997. TRICARE did not adequately explain why these contractors or DCAA were unable to satisfy the agency's CDME overpayment identification requirements.

Proof of Concept. Both the J&A and contract describe the Tichenor effort as a "Proof of Concept," whereby Tichenor would have the opportunity to prove its claim that it could identify larger overpayments in a more expeditious manner than DCAA. Once Tichenor provided its initial results of CDME overpayments, the contract required that TRICARE compare Tichenor's results to the DCAA Phase 1 results by hospital to determine whether Tichenor proved its concept.

In March 2003, 5 months after the Tichenor contract was awarded, TRICARE compared the overpayments Tichenor identified to those DCAA identified during its Phase 1 audits. On a hospital by hospital basis, DCAA identified higher recoveries nearly twice as often as Tichenor. Despite these results, the Tichenor contract remained in force. Furthermore, the contract was recently modified on October 6, 2005, to add the identification of 1998 through 2004 overpayments. In granting the modification, the agency cited Tichenor's unique capability to perform the identification services using its proprietary software. TRICARE did not adequately explain its decision to add the additional years to the contract considering the results of the comparison, which did not reflect larger overpayments than DCAA.

Tichenor Incentive Fee Terms. The Tichenor contract provides for an incentive fee equal to 25 percent of CDME overpayments recovered by TRICARE in excess of the DCAA Phase 1 audits. Tichenor receives a full 25-percent fee on all remaining CDME overpayments not identified in the DCAA Phase 1 audits, even if the same overpayments were identified in the DCAA Phases 2 and 3 audits. This is not consistent with the incentive fees terms originally described in the J&A, which considered all DCAA

overpayments. The J&A states, “The amount paid to Tichenor will not exceed 25% of the amount identified and collected in excess of what the DCAA audit identified during the period FY92 through FY97,” which would have included Phases 2 and 3. As a result of that change in incentive fee terms, we estimated that Tichenor will be paid up to \$4.7 million¹ in incentive fees for overpayments already identified by DCAA during Phases 2 and 3. We were not able to determine who authorized this change in incentive fee terms. The contracting officer and other TRICARE employees we interviewed stated that “someone” in TRICARE upper management had authorized the change, but they could not recall the person by name.

Management Comments and Department of Defense Inspector General Response to Finding (Allegation 1)

TRICARE Comment (FAR Unsolicited Proposal Requirements). TRICARE believes that the CDME recovery contract awarded to Tichenor complies with the FAR. TRICARE states that the contracting officer properly determined that Tichenor was the only responsible source in accordance with FAR Subpart 6.3, which TRICARE’s Chief of Special Contracts and the Office of General Counsel supported. TRICARE asserts that the Tichenor proposal was unique, innovative, and meritorious based on Tichenor’s ability to track amended Medicare cost reports, expedite the audit of Fiscal Years 1992 through 1997, make use of a proprietary database, and provide sufficient documentation to support the collection of all identified overpayments.

According to TRICARE, the contracting officer interpreted the Executive Director’s approval on January 15, 2002 to mean that a positive technical evaluation had been made. The contracting officer concluded that it was in the best interest to pursue the contract because Tichenor would receive no funds unless it could identify overpayments in excess of those identified by DCAA. TRICARE also said that senior management considered other factors within their purview in approving the contract.

DoD IG Response (FAR Unsolicited Proposal Requirements). The contract files we reviewed did not provide an adequate basis for determining that the Tichenor proposal was unique and innovative. The reason given in the contract files was the “proprietary database” which had not been reviewed by TRICARE. TRICARE provided no additional information in its response to support the uniqueness of the database. For example, we found no documentation of a description of the database or operating procedures that outlined any unique abilities or a comparison of how it differed from other sources.

TRICARE stated that the Tichenor methodology gave it a unique ability to track amended Medicare cost reports. However, there was no documentation in the contract files we reviewed that explained how Tichenor tracks the reports, why it benefits the Government, and how it differs from DCAA who can also track the reports.

¹ Our estimate of \$4.7 million in additional incentive fees was calculated by multiplying the 25-percent Tichenor incentive fee by the \$18.9 million identified in the DCAA Phases 2 and 3 audits.

TRICARE stated that the Tichenor proposal would result in expedited audits for FYs 1992 through 1997. TRICARE did not provide us with any analysis which demonstrated that Tichenor could provide audits quicker than others such as DCAA. There was also no evidence in the contract file to suggest that DCAA timeliness was a problem, or that TRICARE ever asked DCAA to provide the reports more quickly. It is unclear why timeliness was an issue because DCAA had already completed its audits of FYs 1992 through 1997 overpayments before the Tichenor contract was awarded.

TRICARE also stated that the Tichenor proposal would result in sufficient documentation to support the collection of all identified overpayments. We found no evidence in the contract files to support the contention that the Tichenor documentation was unique and innovative, or that the DCAA documentation was insufficient to support collection efforts.

Given that the Executive Director only gave approval to pursue negotiations, we do not believe it was appropriate for the contracting officer to assume the Executive Director was declaring an acceptable technical evaluation. As stated in our findings to Allegation 2, the contracting officer's description of the technical evaluator's concerns communicated to the Executive Director was not sufficient for the Executive Director to recognize any actual or potential violations with the FAR. Although the contracting officer stated in his correspondence that the outstanding technical issues could probably be resolved during the negotiation phase, there was no evidence in the contract file to suggest they were later resolved. While we agree that senior management can consider other factors in a decision, those other factors were not documented in the contract file.

TRICARE Comment (Proof of Concept). According to TRICARE, the unsolicited proposal involved an offer of proof of concept without any risk or cost to the Government should the effort not have succeeded in establishing the existence of a unique and innovative approach. In October 2002, DoD Inspector General (DoD IG) reviewed the proof of concept solicitation and had no objection to the auditing contract.

TRICARE states that the maximum additional fees paid to Tichenor for disregarding the DCAA Phase 2 and Phase 3 were actually \$3.8 million, not the \$4.7 million maximum that the DoD IG estimated. TRICARE also notes that it had conducted an "apples to apples" comparison in May 2006, which suggests that Tichenor outperformed DCAA by identifying \$6.4 million additional overpayments. Therefore, TRICARE states that the \$6.4 million in extra overpayments exceeds the \$3.8 million in additional fees paid to Tichenor.

DoD IG Response (Proof of Concept). In October 2002, we reviewed the proof of concept contract to ensure that it complied with applicable DoD audit policies. We did not review the proof of concept for compliance with the FAR. In addition, we believe that TRICARE took actions that were contrary to a "proof of concept." Specifically, TRICARE paid Tichenor incentive fees for work already performed by DCAA in Phase 2 and Phase 3, and issued an extension for additional years despite the March 2003

comparison results showing that the Tichenor methodology did not produce better results than DCAA. Therefore, TRICARE had no basis for concluding that the Tichenor methodology was unique or innovative.

We disagree that the May 2006 analysis demonstrates Tichenor's ability to identify more overpayments than DCAA. This after-the-fact comparison does not justify the TRICARE decision to either award the initial contract in November 2002 or extend the period of performance in October 2005. The May 2006 analysis is not an "apples to apples" comparison. Medicare Cost Reports are subject to continuous revisions and amendments based upon ongoing audits or the resolution of appeals. As a result, the DCAA overpayments identified in 2000 are not comparable to those Tichenor identified in 2003. TRICARE prevented DCAA from updating its results for more current Medicare cost information while TRICARE held negotiations with Tichenor, thus negating an "apples to apples" comparison. Thus far, the only "apples to apples" comparison was the March 2003 analysis which showed that DCAA had identified higher overpayments nearly twice as often as Tichenor. The May 2006 comparison also does not address the other claimed benefits of the Tichenor methodology, including the claim that Tichenor could provide faster and better documentation of overpayments.

Allegation 2. TRICARE management pressured the contracting officer and other TRICARE employees to award the Tichenor contract knowing that it violated the FAR.

We were unable to substantiate the allegation. There was high-level management interest in the proposal as a result of congressional inquiries made on behalf of Tichenor. Because of that interest, the contracting officer took the unusual step of requesting approval from the Executive Director of TRICARE in a memorandum dated January 14, 2002. However, the contracting officer's description of the technical evaluator's concerns in his January 14, 2002, memorandum was not sufficient for the Executive Director to recognize any actual or potential violations with the FAR. In addition, the contracting officer did not receive a favorable technical evaluation or prepare a J&A before requesting final approval from the Executive Director.

Facts and Analysis

TRICARE Top Management Involvement. Both before and during its review of the Tichenor proposal, TRICARE received several inquiries from members of Congress requesting that TRICARE consider the merits of the Tichenor proposal. As a result, TRICARE top management, including the Executive Director (second in command at TRICARE), closely monitored the status of the contracting officer's review of the Tichenor proposal. In its written responses to the congressional inquiries, TRICARE top management appropriately replied that TRICARE would perform a thorough review of the unsolicited proposal in accordance with the FAR and would advise the contractor of its outcome.

TRICARE Management Directive dated January 14, 2002. Three months after the comprehensive technical evaluation was performed, the contracting officer asked the Executive Director to decide whether to pursue a contract with Tichenor in a letter dated January 14, 2002. The Director of Acquisition Management and Support, who is subordinate to the Executive Director, usually approves unsolicited proposals. However, the contracting officer requested approval from the Executive Director because of the congressional interest and the Executive Director's prior involvement. In the letter, the contracting officer pointed out that the technical evaluator had several outstanding questions that needed to be resolved before a contract was issued, but he also commented that the outstanding technical questions could probably be worked out during the negotiation phase. The letter did not describe the outstanding questions and did not refer to them as potential noncompliances with the FAR or other regulations. Although the contracting officer did not explain the technical evaluator's concerns to the Executive Director, he did explain them to the Director of Acquisition Management and Support.

In response to the contracting officer's letter, the TRICARE Executive Director wrote, "I direct you to pursue a contract with Tichenor and Associates as it is in the organization's best interest." No explanation was given for concluding that the Tichenor contract was in the organization's best interest.

Requirements for Approving Unsolicited Proposals. TRICARE procedures indicate that final approval should be granted only after an unsolicited proposal is accepted and a J&A is prepared. TRICARE Acquisition Manual, Subpart 15.6, "Unsolicited Proposals," states in part:

"If the proposal is accepted, the project manager will prepare a justification addressing the evaluation factors contained in FAR 15.606-2. The responsible official shall review the justification and initiate additional agency coordination, if appropriate . . . If the Competition Advocate concurs with the opinion that the unsolicited proposal is unique and meets the definition in FAR 15.601, final approval shall be sought as required by FAR 15.607."

The contracting officer's request for the Executive Director's final approval on January 14, 2002, occurred before the contracting officer had resolved the technical evaluator's concerns and prepared a J&A. The J&A was not prepared until February 26, 2002.

Record of January 31, 2002, Meeting. In a record of a meeting on January 31, 2002, the contracting officer documented that the Executive Director directed him to pursue a contract with Tichenor and that a J&A had to be prepared and signed before negotiations could begin.

Memorandum for the File. In an undated Memorandum for the File, under TRICARE Tracking Number 2001-0001, the contracting officer documented that he reported the concerns raised by the technical evaluator to the acting director of Acquisition Management and Support. According to the memorandum, the Director of

Acquisition Management and Support responded that the proposal was worth pursuing regardless of the technical evaluator’s concerns.

Interview with Contracting Officer and Technical Evaluator. We interviewed both the contracting officer and the technical evaluator (the technical evaluator has since retired) as part of this review. Both employees said that management made clear to them that they wanted to pursue the contract with Tichenor. Although both employees at the time expressed concerns about the contract, the contracting officer said he decided to proceed with the contract based on management’s direction.

Other Issues To Be Reported

Contract Audit Follow-up. We also performed a review to determine whether actions TRICARE took in response to contract audit reports complied with DoD Directive 7640.2, “Policy for Follow-up on Contract Audit Reports,” dated February 12, 1988. The directive establishes DoD policies, responsibilities, reporting requirements, and follow-up procedures for reportable² contract audit reports. DoD Directive 7640.2 requires that Secretaries of the Military Departments and Directors of Defense agencies maintain adequate follow-up systems for the proper and timely resolution and disposition of contract audit reports. Contract audit reports should be resolved³ within 6 months and dispositioned⁴ within 12 months of report issuance. DoD Directive 7640.2 also requires that DoD Components submit semiannual status reports on reportable contract audits to the DoD IG for the 6-month periods ending March 31 and September 30 of each year. DoD IG summarizes the semiannual status reports for DoD Components, which is included in the Inspector General’s Semiannual Report to Congress, in accordance with the Inspector General Act of 1978, as amended.

Issue One: Untimely Disposition of DCAA Audit Reports. TRICARE contracting officials did not disposition 11 of the 16 audits we reviewed within 12 months of report issuance as DoD Directive 7640.2 requires. The results are summarized below and detailed in Appendix B.

	Number of Audits Reviewed	Timely Dispositioned	Untimely Dispositioned
CDME Audits	14	4	10
Other Audits	<u>2</u>	<u>1</u>	<u>1</u>
Total	16	5	11

²Reportable audits generally include all contract audits except those involving future or projected costs, such as audits of pre-award and forward pricing rate proposals.

³Resolution of an audit is achieved when the contracting officer determines a course of action, which is documented and approved in accordance with agency policy.

⁴ Generally, disposition of an audit is achieved when the contracting officer negotiates a settlement, the contracting officer issues a final decision pursuant to the Disputes Clause, or a court renders a final decision on appeal.

CDME Audits. The 10 CDME audits that were untimely dispositioned include one from Phase 1, which questioned \$437,000 and nine from Phases 2 and 3, which questioned \$18.9 million. The disposition dates for the audits exceeded the 12-month requirement by an average of 21 months, and the contract file did not include sufficient justification to warrant such a delay. While the audits were still open (not dispositioned), TRICARE explained in its semiannual report to Congress that “Disposition [is] pending analysis of recoupments demonstration contract with Tichenor and Associates.” The explanation does not justify the Agency’s decision to delay recovering the \$18.9 million in CDME overpayments reported in the DCAA Phases 2 and 3 audits, since the purpose of the “proof of concept” was to determine if Tichenor could identify larger overpayments than DCAA. Furthermore, 6 months before awarding the Tichenor contract, TRICARE, without explanation, discontinued its efforts to recover the CDME overpayments identified by DCAA. TRICARE should have continued its recovery efforts while the Tichenor proposal was under consideration. Had TRICARE acted promptly, the agency may have saved up to \$4.7 million in incentive fees paid to Tichenor (25-percent fee times \$18.9 million Phases 2 and 3 overpayments).

Other Audits. Of the two other audits we reviewed, one (DCAA Report No. 6171-2003L17900003) exceeded the 12-month disposition requirement by 1 month. However, the TRICARE contract file included sufficient documentation to justify the delay.

Issue Two: Inadequate Rationale for Disposition of Questioned Costs. In 15 of 16 cases, the contracting officer did not maintain adequate documentation to support disposition of questioned costs reported by DCAA (see listing by audit in Appendix B). TRICARE Acquisition Practice No. 15-05, Paragraph 5.4, requires that the contracting officer document the rationale for dispositioning the DCAA questioned costs. Properly documenting the contracting officer’s rationale helps ensure that the auditor’s findings are appropriately considered and the Government’s interests are fully protected.

DCAA CDME Overpayment Audits. For all 14 reportable CDME audits we reviewed, TRICARE did not maintain adequate documentation to support the questioned costs reported as sustained⁵ in the TRICARE semiannual report to Congress.

In 4 of 14 cases, TRICARE reported that a portion (averaging 27 percent) of the DCAA questioned costs was sustained. The TRICARE semiannual report to Congress dated September 30, 2001, TRICARE simply stated “sustained totals reflect adjustments for actions referred to DoJ [Department of Justice] and those past debt collection time limitations.” However, no documentation was in the TRICARE contract file that explained how the adjustments were determined, or why 73 percent of the questioned costs were not sustained.

In the remaining 10 cases, TRICARE reported that none of the questioned costs were sustained. All but one relate to the DCAA CDME audits performed in Phases 2

⁵ Sustained questioned costs represent the portion of costs questioned by the auditor that are upheld as a result of agreement by the contractor or final decision by the contracting officer.

and 3. TRICARE did not document why none of the questioned costs totaling \$19.3 million was sustained.

Other DCAA Audits. For one of two other audits we reviewed (DCAA Report No. 6171-2003L17900003), the sustained costs reported in the TRICARE semiannual report to Congress dated September 30, 2004, was not consistent with the contracting officer's disposition action described in the price negotiation memorandum (PNM). Although the TRICARE semiannual report to Congress reported that none of the \$9.8 million questioned costs were sustained, the PNM indicates that the contracting officer partially agreed with the DCAA audit report. We were not able to determine how much of the questioned costs were agreed to and sustained by the contracting officer because the PNM does not contain this information. Although we do not take exception to the negotiation results in this case, the contracting officer should have documented the sustained questioned cost amount in the PNM and accurately reported this amount in the TRICARE semiannual report to Congress.

Issue Three: Evaluations not Impacted for Contract Audit Follow-up. Paragraph 5.2.4 of DoD Directive 7640.2 specifies that the Directors of DoD agencies must "Ensure that performance appraisals of appropriate acquisition officials reflect their effectiveness in resolving and dispositioning audit findings and recommendations in a timely manner, while fully protecting the Government's interest." We reviewed performance plans and appraisals for three TRICARE employees, including one senior contract specialist and two price analysts, and determined that none had comments addressing the employee's ability to timely and effectively resolve and disposition contract audit findings and recommendations.

The TRICARE performance appraisals for acquisition personnel do not comply with DoD Directive 7640.2. The contract audit follow-up requirements specified in the directive should be included in all appropriate acquisition officials' performance appraisal to emphasize the importance of the DoD Directive 7640.2 requirements and to recognize those individuals who are effective in timely and appropriately resolving and dispositioning audit findings and recommendations.

Management Comments and DoD IG Response (Other Issues to be Reported)

TRICARE Comments. TRICARE maintains that the contract file had adequate rationale for dispositioning the questioned costs. TRICARE identified the primary reason for the delay was the review and evaluation process of the Tichenor unsolicited proposal. TRICARE contends that it was a better business practice to wait until they had a more reasonable expectation that, using Tichenor's concept, additional and more complete overpayments would be discovered before they attempted recoupment actions from the hospitals.

DoD IG Response. We disagree that the TRICARE delay of recovery actions was justified based on its review of the Tichenor proposal and its expectation of

additional and more complete overpayments. Considering the time value of money, we do not agree that it was a better business practice to suspend recovery of the DCAA identified overpayments pending receipt of the Tichenor identified overpayments. In addition, we are not aware of any circumstance that prevented TRICARE from promptly collecting the overpayments identified by DCAA, and later collecting any additional overpayments identified by Tichenor.

Recommendations, Management Comments, and DoD IG Response

1. We recommend that the TRICARE contracting officer for the Tichenor contract initiate a termination for convenience on the portion of the contract covering identification of 1998 through 2004 Capital and Direct Medical Education overpayments.

TRICARE Comments. The TRICARE contracting officer will consider the DoD IG concerns and reevaluate the pros and cons of available options before determining whether terminating the Tichenor contract for convenience is in the best interest of the Government. TRICARE believes that millions of dollars remain to be collected in Capital and Direct Medical Education overpayments. Tichenor represents only one of several methods for documenting overpayments of uncollected medical funds.

DoD IG Response. We request that TRICARE provide us with a completion date for re-evaluating available options. In addition to addressing our concerns, we request that TRICARE provide us with a written justification which fully supports its determination. The justification should include data and analysis which demonstrates that the use of Tichenor has resulted in benefits to the Government which cannot be obtained from other sources.

2. We recommend that the TRICARE contracting officer for the Tichenor contract satisfy the requirement for identifying 1998 through 2004 Capital and Direct Medical Education overpayments by either:

- a. Requesting that the Defense Contract Audit Agency perform the work or
- b. Issuing the requirement under a solicitation that provides for full and open competition.

TRICARE Comments. TRICARE acknowledges that Tichenor is only one of the sources available to provide the service. TRICARE states that if the TRICARE contracting officer determines that it is in the best interests of the government to terminate the Tichenor contract for convenience, appropriate action will be initiated.

DoD IG Response. Given the response to Recommendation 1, the TRICARE comments are generally responsive.

3. We recommend that the TRICARE Director of Acquisition Management and Support implement the controls necessary to ensure that future unsolicited proposals received by the agency are processed and documented in accordance with Federal Acquisition Regulation Subpart 15.6.

TRICARE Comments. TRICARE will conduct a thorough review of current policies and procedures regarding the handling of unsolicited proposals.

DoD IG Response. The TRICARE response meets the intent of our recommendation. We request that TRICARE provide a date for completing the review and providing the results to the DoD IG.

4. Before requesting final approval of an unsolicited proposal, we recommend that contracting officers be required to sign a statement affirming that the requirements for accepting and negotiating an unsolicited proposal have been met, including the receipt of a favorable technical evaluation and the preparation of a Justification and Approval.

TRICARE Comments. As part of its review of current policies and procedures, TRICARE will ensure the contracting officer's evaluation of unsolicited proposals will be formally documented and included in the file. Further, TRICARE will ensure all requirements for accepting and negotiating an unsolicited proposal are met and to use such documentation to support the contracting officer's preparation and certification of a J&A.

DoD IG Response. The TRICARE response meets the intent of our recommendation. We request that TRICARE provide us with a completion date for reviewing its policies and procedures and identify the quality assurance process it will implement for complying with the FAR unsolicited proposal requirements.

5. We recommend that the Director of Acquisition Management and Support revise TRICARE Acquisition Practice No. 15-05, entitled "Contract Audit Follow-up," to require that contracting officers document the justification for exceeding either the 6-month requirement for resolution or 12-month requirement for disposition established by DoD Directive 7640.2.

TRICARE Comments. TRICARE understands the DoD IG concerns regarding the disposition of audits and believes its contracting officers are aware of the responsibilities to resolve and disposition audits in accordance with DoD Directive 7640.2. TRICARE is modifying its procedures to clarify the DoD Directive 7640.2 requirements.

DoD IG Response. The TRICARE response meets the intent of our recommendation. We request that TRICARE provide us with a completion date for modifying its procedures and providing the results to the DoD IG. In addition, we request that TRICARE identify the quality assurance process it will implement for timely

resolving and dispositioning contract audits, and for justifying those instances when the contracting officer must exceed the DoD Directive 7640.2 timeframes.

6. We recommend that the TRICARE Director of Acquisition Management and Support implement appropriate controls for ensuring compliance with TRICARE Acquisition Practice No. 15-05, Paragraph 5.4, which requires that the contracting officer document the rationale for dispositioning the Defense Contract Audit Agency questioned costs. At a minimum, we recommend that TRICARE implement a process to test the adequacy of documentation supporting the disposition of contract audit reports before the contracting officer reports them as dispositioned in the TRICARE semiannual report to Congress.

TRICARE Comments. TRICARE stated that the contracting officer adequately identified and documented the contract file with rationale for dispositioning the audit reports. Further, TRICARE believes that a requirement for supervisory review of a contracting officer's disposition decision is contrary to FAR 1.602-2 and would subrogate the contracting officer's independence.

DoD IG Response. The TRICARE response suggests there is no need for checks and balances of contracting officer work performance. OMB Circular A-50 and DoD Directive 7640.2 require management oversight of the contract audit follow-up function. For example, OMB Circular A-50 requires that agency management officials designate a top management official who will oversee audit follow-up, including resolution and corrective action. Where management officials disagree with an audit recommendation, the matter must be resolved by the follow-up official. Each agency must promptly resolve and implement audit findings and recommendations and provide for a complete record of actions taken. Therefore, we do not believe that supervisory review of contract audit follow-up actions would subrogate the contracting officer's independence. However, based on the concerns expressed by TRICARE, we modified our recommendation and request that comments on the revised recommendation be provided by November 5, 2006.

7. In accordance with Paragraph 5.2.4 of DoD Directive 7640.2, we recommend that the Deputy Chief of TRICARE Acquisitions revise the performance appraisals of appropriate acquisition officials to measure their performance in resolving and dispositioning contract audit reports.

TRICARE Comments. TRICARE claims that listing every responsibility in a performance standard is not feasible. All contracting officers and pricing personnel have been instructed on the importance of audit follow-up and documentation requirements. However, TRICARE will evaluate all contracting officers on their effectiveness in timely resolving and dispositioning reportable audit findings.

DoD IG Response. The response meets the intent of our recommendation. However, we are concerned that without a specific reference in the performance plans, contracting officers, managers and supervisors will not comply with the requirements of DoD Directive 7640.2.

Appendix A. Scope and Methodology

We evaluated records maintained by TRICARE, Aurora, Colorado to determine the validity of the allegations. We also interviewed current and former TRICARE managers and employees at Aurora and the Chief of Health Plan Operations at the Falls Church, Virginia headquarters. Specifically, we

- determined the applicable standards, public law, DoD regulations, directives, and instructions;
- reviewed the contract files related to the Tichenor & Associates contract award, prepared in both hard copy and electronic format;
- interviewed the TRICARE staff and managers and DCAA employees having direct involvement with the Tichenor contract award and the Contract Audit Follow-up system;
- obtained supporting documentation from the DCAA Financial Liaison Auditor assigned to the TRICARE Aurora, Colorado facility; and
- reviewed mathematical calculations prepared by TRICARE Aurora in support of the Tichenor contract award.

We also evaluated the actions taken by TRICARE to timely and effectively disposition 16 reportable DCAA audit reports, including 14 dispositioned DCAA audits of CDME overpayments and 2 other dispositioned DCAA audits. (See report listing in Appendix B.)

We performed the review from June 2005 through June 2006.

Appendix B. Untimely Disposition of Contract Audits and Inadequate Rationale for Sustained Costs

	DCAA Report Number	Report Date	DCAA Questioned Cost	Disposition Date	Exceeds 12-Month Disposition Requirement By	Reported as Sustained	Rational For Sustained Costs on File?
CDME Audits:							
Phase 1	6311-2000L17900006	11/29/2000	\$ 1,028,872	7/27/2001	--	\$ 224,043	No
Phase 1	6311-2000L17900007	1/12/2001	1,180,796	8/27/2001	--	350,962	No
Phase 1	6311-2000L17900005	6/5/2001	1,435,463	6/05/2001	--	337,198	No
Phase 1	6311-2000L17900003	1/8/2001	436,672	9/30/2004	32 months	0	No
Phase 1	6311-2000L17900004	12/21/2000	<u>1,204,710</u>	8/06/2001	--	<u>398,155</u>	No
Phase 1 Total			\$ 5,286,513			\$1,310,358	
Phase 2	6311-2001L17900006	6/14/2001	\$ 4,914,983	9/30/2004	27 months	\$ 0	No
Phase 2	6311-2001L17900009	6/20/2001	2,212,611	9/30/2004	27 months	0	No
Phase 2	6311-2001L17900004	6/12/2001	6,148,700	9/30/2004	27 months	0	No
Phase 2	6311-2001L17900005	6/20/2001	283,133	9/30/2004	27 months	0	No
Phase 2	6311-2001L17900007	6/20/2001	<u>3,094,015</u>	9/30/2004	27 months	<u>0</u>	No
Phase 2 Total			\$16,653,442			\$ 0	
Phase 3	6171-2002A17900005	9/24/2002	\$ 343,311	9/30/2004	12 months	0	No
Phase 3	6171-2002A17900003	10/21/2002	386,421	9/30/2004	11 months	0	No
Phase 3	6171-2002A17900004	9/30/2002	886,417	9/30/2004	12 months	0	No
Phase 3	6171-2002L17900003	9/25/2002	20,010	-----Not Reportable Under DoD Directive 7640.2-----			
Phase 3	6171-2002A17900001	9/27/2002	<u>594,062</u>	9/30/2004	12 months	<u>\$ 0</u>	No
Phase 3 Total			\$ 2,230,221			0	
Total CDME Audits			\$24,170,176			\$ 0	
Other Audits:							
N/A	1621-2003T17900008	7/22/2003	256,649	6/24/2004	--	\$ 256,649	Yes
N/A	6171-2003L17900003	4/11/2003	9,833,263	5/14/2004	1 month	0	No

Appendix C. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition, Technology, and Logistics
 Director, Defense Procurement and Acquisition Policy
Under Secretary of Defense for Personnel and Readiness

Other Defense Organizations

Director, TRICARE Management Activity
 Acting Chief of Healthcare Plan Operations
 Director, Acquisition Management and Support Division
Director, Defense Contract Audit Agency
 Branch Manager, Defense Contract Audit Agency Chesapeake Bay Branch Office
 Financial Liaison Auditor, TRICARE Management Activity (Contracts), Aurora

Department of the Army

Auditor General, Department of the Army

Department of the Navy

Chief, Office of Naval Research
Audit Liaison, Assistant Secretary of the Navy
 Financial Management and Comptroller
Naval Inspector General

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)

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 Homeland Security and 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
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

Deputy Director TRICARE Management Activity Comments



TRICARE
MANAGEMENT
ACTIVITY

OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE
HEALTH AFFAIRS
SKYLINE FIVE, SUITE 810, 5111 LEESBURG PIKE
FALLS CHURCH, VIRGINIA 22041-3206

JUN 30 2006

MEMORANDUM FOR PATRICIA A. BRANNIN, ASSISTANT INSPECTOR
GENERAL AUDIT POLICY AND OVERSIGHT

SUBJECT: TRICARE Management Activity Response to Draft of a Proposed Report entitled, "Review of Allegations Concerning the TRICARE Contract Award for the Audit of Capital and Direct Medical Education Costs (Project NO. D2005-DIPOAI-0227.000)," dated March 23, 2006

The TRICARE Management Activity (TMA) response to your draft report is attached. The draft report that reflects your findings as a result of your review initiated by a DoD Hotline alleging the award of a contract to Tichenor and Associates, LLP, (Tichenor) did not comply with the Federal Acquisition Regulation (FAR) and senior TRICARE Management Activity (TMA) management pressured the contracting officer and other TMA employees, to award the contract knowing that it did not comply with the FAR. Your draft report indicates you believe one of these allegations can be substantiated and identifies your concerns with the TMA contract with Tichenor.

Regarding the award of the subject contract, we respectfully submit that reasonable people may reach different conclusions based on a review of the files and facts available to the decision makers at the time of the contract action. Your report does not find any indication of improper intent or bad faith on the part of government personnel; rather, your report appears to be based on disagreements with business judgments exercised by TMA management and the adequacy of supporting documentation of actions based on those judgments. Our response is intended to reflect TMA's perspective on the business judgments leading to the contract action in reasonable compliance with the FAR.

The second allegation was that TMA management pressured the contracting officer and other TMA employees to award the contract knowing that it did not comply with the FAR. Since your draft report states you are unable to substantiate the second allegation, our response does not address any of your comments on this allegation and focuses on the first allegation of a non-compliant contract.

My staff remains available to discuss any aspect of the attached response, including any supporting data and analysis. My point of contact is Mr. John Meeker,

Deputy Director TRICARE Management Activity Comments

Director, Acquisition Management and Support. Mr. Meeker can be reached at (303) 676-3991, or by e-mail at john.meeker@tma.osd.mil.



Elder Granger
Major General, MC, USA
Deputy Director

Attachment:
As stated

Deputy Director TRICARE Management Activity Comments

TRICARE Management Activity (TMA) Response to Draft of a Proposed Report entitled, "Review of Allegations Concerning the TRICARE Contract Award for the Audit of Capital and Direct Medical Education Costs (Project NO. D2005-DIPOAI-0227.000)," dated March 23, 2006

TMA fully cooperated with your representatives, Meredith Long-Morin and Mark Dixon, when they were in the TMA Aurora office, July 11–21, 2005, performing the review. Your representatives had complete access to the files involving the Tichenor unsolicited proposal and resultant contract, and interviewed several key personnel knowledgeable of the action. At the time of the exit interview, we did not receive any indication that significant concerns existed, or that the continued contractual relationship with Tichenor should be suspended. Therefore, as a result of actions initiated prior to April 2005, a modification to the contract with Tichenor was executed on October 6, 2005, to complete the identification of Capital and Direct Medical Education (CDME) overpayments occurring during Fiscal Years 1998–2004.

On May 5, 2006, along with a draft of our response, we sent several files related to the Defense Contract Audit Agency (DCAA) Phase I, II, and III audits, as well as Tichenor's audit, directly to Ms. Meredith Long-Morin and Mr. Mark Dixon. These files provided detailed information for the data exclusions/analysis that we performed to support the findings that Tichenor had done a better job at identifying overpayments of CDME funds than did DCAA. On May 8, 2006, we sent a copy of the complete, (unabridged) Tichenor audit to further assist the Office of the Assistant Inspector General (OAIG) in their analysis of the data. We believe this information will support our analysis of and response to the issues addressed in your draft report.

FAR Unsolicited Proposal Requirements:

We do not believe the facts support your findings that award of the CDME audit contract to Tichenor did not comply with the FAR. Although the proposed draft report asserts certain conclusions resulting from the review of the contracting actions involving the Tichenor contract, the specific facts on which those conclusions are drawn are not clear. In our opinion, the following information shows compliance with applicable provisions of FAR Subpart 15.6 (Unsolicited Proposals):

- In accordance with FAR Subpart 15.604 (Agency Points of Contact), the contractor is authorized contact with agency personnel before preparing an unsolicited proposal.
 - The record shows that Tichenor had contacted the TMA to discuss the content of his unsolicited proposal. This contact was compliant with the FAR.

Deputy Director TRICARE Management Activity Comments

- In accordance with FAR Subpart 15.606 (Agency Procedures), the agency “shall establish procedures for controlling the receipt, evaluation, and timely disposition of unsolicited proposals consistent with the requirements of this subpart.”
 - These procedures have been established and can be found in the TRICARE Acquisition Manual (TAM) at part 15.6.
- In accordance with FAR Subpart 15.606-1 (Receipt and initial review), an initial review shall be performed.
 - The agency contact point had the initial review performed and made a determination on October 4, 2001, that a comprehensive evaluation should proceed.
 - A technical evaluator was assigned on October 5, 2001, and the comprehensive evaluation was completed on October 16, 2001.
 - This evaluator did not recommend acceptance of the proposal until noted issues were resolved.
 - Senior Management was knowledgeable of the proposal contents and considered other factors within their purview concluding that adequate information was provided by Tichenor, thereby satisfying the requirement for a favorable evaluation and contract award.
- FAR 15.606-2 states that in a comprehensive evaluation of an unsolicited proposal, evaluators shall consider ... “1) Unique, innovative and meritorious methods, approaches or concepts demonstrated in the proposal”.
 - TMA reimburses CDME costs if a hospital submits a request for reimbursement along with the associated Medicare cost report. Medicare cost reports are subject to adjustment based on desk review, audit, or appeals.
 - Hospitals are required to submit an amended CDME payment request if the Medicare cost report is adjusted; however, many hospitals fail to submit an amended request, resulting in uncollected CDME overpayments due to TMA.
 - Tichenor was keeping track of the amended Medicare cost reports which hospitals fail to submit and this was determined to be an innovative, unique, and meritorious approach.

Deputy Director TRICARE Management Activity Comments

Final Report
Ref.

- The amended reports are required to be submitted to Medicare under the Department of Health and Human Services; however, there is no legal requirement that the hospitals submit amended reports to TMA.
- This was seen as unique, innovative, and beneficial. Tichenor also had the qualifications, capability, experience, and facilities to perform the contract proposed as required by FAR Part 15.606-2.
- As part of your conclusion, the question was raised of whether the Tichenor proposal included sufficient technical information in order for the government to perform a comprehensive evaluation based on the unavailability of the Tichenor proprietary database.
 - The contracting officer determined that an actual review of the proprietary database was not necessary. The unique and innovative ideas and concepts as presented by the unsolicited proposal were that Tichenor could, within an expedited timeframe, conduct the audit of Fiscal Years 1992–1997 hospital regarding overpayments using his proprietary database and provide sufficient documentation to the government to support collection of all identified overpayments.
 - Such an audit would either validate the DCAA audits of the same hospitals or, as presented by Tichenor, prove that significantly more overpayments could be identified and collected with the proprietary database and software.
 - Under the proposal, Tichenor would receive no funding to perform any analyses and, in fact, would only be paid if TMA was able to recover overpayments over and above any identified overpayments for the same hospital resulting from Phase I audits performed by DCAA.
 - Therefore, the unsolicited proposal involved an offer of proof of concept without any risk or cost to the government should the effort not succeed in establishing the existence of a unique and innovative approach.
- The contracting officer submitted a letter to the Executive Director of TMA on January 14, 2002, which outlined the contracting officer's observations.
 - It was the contracting officer's interpretation of the response by the Executive Director, dated January 15, 2002, that a positive technical evaluation had been made. The contracting officer concluded, after discussions concerning the structure of the contract (i.e., Tichenor would receive no funds unless he proved by using his method that he could identify CDME overpayments in

clarified

Deputy Director TRICARE Management Activity Comments

excess of those identified by DCAA), that it was in the best interest of the Government to pursue the contract.

- In accordance with FAR 15.607(b) (4), a synopsis was issued through Federal Business Opportunities (FEDBIZOPS) of the organizations' intent to negotiate a sole source contract with Tichenor and Associates, LLP, of Louisville, Ky., in response to an unsolicited proposal.
 - No responses were received as a result of this notice.
- Additionally, regarding the concern that services may have been available from other sources, FAR 15.608 states that the government "*shall not use any data, concept, idea, or other part of an unsolicited proposal as the basis, or part of the basis, for a solicitation or in negotiations with any other firm unless the offeror is notified of and agrees to the intended use. However, this prohibition does not preclude using any data, concept, or idea in the proposal that also is available from another source without restriction.*"
 - We properly determined that Tichenor was the only responsible source for the work proposed in its unsolicited proposal.
- In accordance with FAR 15.607 (b), the contracting officer commenced negotiations on a sole source basis after the execution of a Justification and Approval (J&A).
 - This J&A was drafted in compliance with FAR 6.3 and was certified and supported by the technical evaluator and the Contracting Officer, supported by the Chief of Special Contracts and Operations Office and found legally sufficient by the Office of General Counsel.
 - This J&A was also approved by the Director of Acquisition Management and Support.
- Negotiations commenced with oversight by the Director of Acquisition Management and Support. The points of concern raised by the initial technical evaluator were discussed and the terms and conditions of the contract were negotiated.
- Additionally, on October 7, 2002, we forwarded to the OAIG (Audit Policy and Oversight) a copy of the proposed proof of concept solicitation and advised it was based on an unsolicited proposal from Tichenor and Associates "that was evaluated and accepted by the Contracting Officer and subject to a Justification and Approval."

Deputy Director TRICARE Management Activity Comments

Final Report
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Final
Report Ref.

- On October 16, 2002, TMA received a voice mail message from Mr. Wayne Berry from the office of the OAIG advising that he had completed his review and that there were no objections to the auditing contract.
- We regret the absence of documentation in the file formally recording the Contracting Officer's evaluation; however, the file does contain a J&A noting the Contracting Officer's determination that the unsolicited proposal qualified under FAR 15.603.
- The contract was executed on November 2, 2002.

Proof of Concept:

On page 5, fourth paragraph (Proof of Concept), the OIG asserts that "In March 2003, 5 months after the Tichenor contract was awarded, TRICARE compared the overpayments identified by Tichenor to those identified by DCAA during its Phase I audits. On a hospital by hospital basis, DCAA identified higher recoveries nearly twice as often as Tichenor."

- The OIG's statement is based on our very limited, preliminary analysis of only the Phase I audit data matches.
 - For a complete "Proof of Concept" analysis, we compared Tichenor's audit findings for CYs 1992-1997, to the combined DCAA Phase I, II, and III audit findings, minus the data exclusions required by the contract: audit findings tied to a Department of Justice qui tam, CHAMPUS Reform Initiative network hospitals, the six-year statute of limitations for underpayments, and findings of overpayment amounts of less than \$250.
 - This provided an "apples-to-apples" data comparison for all hospitals in the United States that received CDME payments from TMA covered by both the Tichenor and DCAA audits.
 - The final result of this comparison showed that Tichenor had identified a total of \$28.9 million (M) in net overpayments compared to DCAA's total of \$18.7M in net overpayments.
 - Tichenor identified \$10.2M more in net overpayments, nearly 55 percent more, than did DCAA. This clearly demonstrates that by using its proprietary database, Tichenor is able to identify more CDME overpayments than DCAA.

Note:
TRICARE
revised the
\$10.2
million to
\$6.4 million.

revised

Deputy Director TRICARE Management Activity Comments

- In fact, even after deducting the IG-questioned fee of \$3.81M from the \$10.2M of additional overpayments identified by Tichenor, the government could recover \$6.4M more than would have been possible through DCAA alone.

Tichenor Incentive Fee Terms:

In the March 23, 2006, draft report you state:

“In addition to the FAR noncompliances, we determined that the incentive fee terms did not properly consider all overpayments already identified by the Defense Contract Audit Agency (DCAA), resulting in Tichenor and Associates, LLP receiving additional fees of up to \$4.7 million. We also determined that TRICARE did not adequately explain its recent decision to extend the contract considering that the contractor did not demonstrate that it could identify larger Capital and Direct Medical Education cost overpayments than were identified by DCAA.”

- Your estimate of Tichenor receiving additional fees of up to \$4.7M is overstated because it is derived by multiplying \$18,883,663 (the sum of the DCAA Phase II and III total audit findings) by 25 percent (Tichenor’s fee for collections).
 - However, this entire amount is not eligible for the Tichenor fee. (See data exclusions in the Proof of Concept discussion above.)
 - In addition, since the DCAA Phase III audit pertains to a much broader time period, 1996–1999, all data for 1998 and 1999 are excluded because only the records for 1996–1997 data are covered by the contract.
 - When all these excluded records are removed from the DCAA Phase II and III audit findings, their combined value is reduced to \$15,332,730.
 - Therefore, the maximum potential amount of additional fees to be paid to Tichenor is reduced to \$3.8M (25 percent of \$15,332,730.)

Extension of the Tichenor Contract for 1998 – 2004:

In October 2005, the Tichenor contract was modified to allow an evaluation of the extent of CDME overpayments for 1998–2004. In November 2005, a stop work order was put in place. Using the base period audit findings as a guide, TMA estimates that the amount of overpayments for this period would range from \$30M–\$40M. At the current

¹ The IG proposed draft report identifies “additional fees of up to \$4.7 million.” TMA has adjusted this amount to \$3.8M to account for exclusions identified in this section, and calculated in the **Tichenor Incentive Fee Terms** section of this memorandum.

Deputy Director TRICARE Management Activity Comments

rate of 25 percent, the Tichenor fee would be in the range of \$7.5M–\$10M. This would leave approximately \$22.5M–\$30M returned to the TMA general fund.

Based on the highly successful recovery experienced in the base period of the Tichenor contract, there is every reason to believe that the contract extension covering 1998–2004 would be equally successful in recovering millions of overpaid CDME dollars.

Contract Audit Follow Up (CAFU):

The DoD IG identified that 11 of 16 audits reviewed were not dispositioned within 12 months of audit report issuance as required by DoD Directive 7640.2. Ten of the 11 audit reports identified were related to CAP/DME. The DoD IG also stated “the contract file did not include sufficient justification to warrant such a delay.” The report further stated that TRICARE explained in its semiannual report to Congress that Disposition [is] pending analysis of a recoupment demonstration contract with Tichenor and Associates. The DoD IG goes on to state that “[t]his explanation does not justify the agency’s failure to take prompt action in recovering the \$18.9 million in CDME overpayments reported in the DCAA Phases (sic) 2 and 3 audits.”

- The primary reason for the delay was the review and evaluation process of the Tichenor unsolicited proposal. We believed that it was a better business practice to wait until we had a more reasonable expectation that, using Tichenor’s concept, additional and more complete overpayments would be discovered before we attempted recoupment actions from the hospitals.
 - Each and every audit file, as provided to the DoD IG, was documented to identify the reason for the delay.
 - Every CAP/DME audit file stated, “[t]he entire series of CAP/DME audits are considered closed in the CAFU log. The findings of the DCAA audit reports were superseded by the award of a demonstration contract to Tichenor and Associates. The demonstration contract identified total dollar amounts which exceeded the amount originally identified by DCAA. Recoupment of the questioned costs are (sic) in process.”
 - In its semiannual report for the period ending September 30, 2004, TRICARE identified for the audit reports in question, “[t]he findings of these DCAA Audit reports were superseded by the award of a demonstration contract to Tichenor and Associates.

Deputy Director TRICARE Management Activity Comments

- The demonstration contract identified total dollar amounts which exceeded the amount originally identified by DCAA. Recoupment of these costs is currently in process.”
- The audit files were documented as to the reasons for the delay and the outcome resulted in recouping more overpayments than identified by DCAA. We believe this provides an adequate rationale for disposition of questioned costs.

COMMENTS ON DRAFT REPORT RECOMMENDATIONS

Your proposed draft report contains the following recommendations:

1. “We recommend that the TRICARE Contracting Officer for the Tichenor contract initiate a termination for convenience on the portion of the contract covering the identification of 1998 through 2004 Capital and Direct Medical Education overpayments.”

We believe millions of dollars remain to be collected in overpaid CDME funds. Tichenor is one method for documenting and making these collections. Consistent with the FAR termination clause, the TMA Contracting Officer will consider the concerns of the DoD IG and re-evaluate the pros and cons of available options before determining whether termination of the Tichenor contract for convenience is in the best interests of the government.

2. “We recommend that the TRICARE Contracting Officer for the Tichenor contract satisfy the requirement of identifying 1998 through 2004 Capital and Direct Medical Education overpayments by either:
 - a. requesting the Defense Contract Audit Agency to perform the work or
 - b. issuing the requirement under a solicitation which provides for full and open competition.”

If the TMA Contracting Officer determines that it is in the best interests of the government to terminate the Tichenor contract for convenience, appropriate action will be initiated to satisfy the requirement for audit services to identify and support recovery of the remaining overpaid CDME funds.

3. “We recommend that the TRICARE Director of Acquisition Management and Support implement the controls necessary to ensure that future unsolicited proposals received by the agency are processed and documented in accordance with Federal Acquisition Regulation Subpart 15.6.”

Deputy Director TRICARE Management Activity Comments

It is TMA's practice that all policies and procedures are reviewed on a periodic basis in order to ensure compliance with law and regulation, and we believed we had the necessary controls in place to ensure full compliance with such laws and regulations. However, given the concerns of the DoD IG, we will conduct a thorough review of current policies and procedures regarding the handling of unsolicited proposals to identify and implement any necessary improvements in the processing and documentation in accordance with FAR Subpart 15.6.

4. "Before requesting final approval of an unsolicited proposal, we recommend that Contracting Officers be required to sign a statement affirming that the requirements for accepting and negotiating an unsolicited proposal have been met, including the receipt of a favorable technical evaluation and the preparation of a proper Justification and Approval."

As part of the review of current policies and procedures, TMA will ensure that the contracting officer's evaluation of unsolicited proposals will be formally documented and included in the contract file. We will ensure all requirements for accepting and negotiating an unsolicited proposal are met. Such documentation will be used to support the contracting officer's preparation and certification of a J&A document.

5. "We recommend that the Director of Acquisition Management and Support revise TRICARE Acquisition Practice No. 15-05, entitled "Contract Audit Follow-up," to require Contracting Officers to document the justification for exceeding either the 6-month requirement for resolution or 12-month requirement for disposition established by DoD Directive 7640.2."

We understand your concerns regarding the disposition of audits, and believe all of our contracting officers are aware of their responsibilities to resolve and properly dispose reportable audits in accordance with DoD Directive 7640.2. In fact, prior to our knowledge of the "hotline" complaint and the subsequent DoD IG audit, we had already identified and prioritized the contract audit follow-up process as an opportunity to clarify DoDD 7640.2 requirements. We have clarified existing policies and are pending issuance upon receipt of written comment and questions from the contracting workforce.

6. "We recommend that the TRICARE Director of Acquisition Management and Support implement appropriate controls for ensuring compliance with TRICARE Acquisition Practice No. 15-05, Paragraph 5.4, which requires that the Contracting Officer document the rationale for dispositioning the Defense Contract Audit Agency questioned costs. At a minimum, we recommend that the Contracting Officer's supervisor review and approve documentation supporting the Contracting Officer's disposition of contract audit reports before the Contracting Officer reports them as dispositioned in the TRICARE semiannual

Revised Recommendation 6. based on TRICARE comments

revised

Deputy Director TRICARE Management Activity Comments

report to Congress.”

We agree that contracting officers must document their rationale for the dispositioning of DCAA questioned costs. Our contracting officers did adequately identify and document the file with the rationale for dispositioning each of the identified audit reports. We believe the recommendation that the contracting officers’ supervisors “review and approve documentation supporting the Contracting Officer’s disposition of contract audit reports before the Contracting Officer reports them as dispositioned...,” would be contrary to the FAR. We believe contracting officers should be free to seek advice from whatever sources are necessary to render a decision. In accordance with FAR 1.602-2 (Responsibilities), “[c]ontracting officers are responsible for ensuring performance of all necessary actions for effective contracting, ensuring compliance with the terms of the contract, and safeguarding the interests of the United States in its contractual relationships.” Contracting officers are to be given “wide latitude to exercise business judgment.” Any approval at any level above the contracting officer, unless specifically required by the FAR, could be contrary to the FAR and would subrogate the contracting officer’s authority to act independently within the meaning of FAR language, and as designated by his or her unlimited warrant to perform the duties of a contracting officer.

7. “In accordance with Paragraph 5.2.4 of DoD Directive 7640.2, we recommend that the Deputy Chief of TRICARE Acquisitions revise the performance standards of appropriate acquisition officials to measure their performance in resolving and dispositioning contract audit reports.”

clarified

All contracting officers and pricing personnel have been instructed on the importance of audit follow-up and documentation requirements. We have and will ensure that all personnel responsible for audit activity are made aware of requirements for disposition and will consider their success or failure in this regard when assessing performance. Contracting officers have wide and varied responsibilities, and it is not feasible to list every requirement and responsibility in a performance standard; however, during performance evaluations, all TMA contracting officers will be evaluated on their responsibilities for effectiveness, to include timely resolution and disposition of reportable audit findings.

CONCLUSION

We understand the concerns expressed in the draft report. We believe we have proceeded in compliance with regulation and acquisition policy, and that our actions were in the best interest of the Government in awarding the contract and the extension to Tichenor. Their unique and innovative approach outperformed DCAA by over \$10M. In our view, we exercised appropriate management discretion when determining term and fee structure for the initial Tichenor contract and its subsequent extension.

Deputy Director TRICARE Management Activity Comments

COORDINATION
TRICARE Management Activity Response to a Proposed Report Entitled
“Review of Allegations Concerning the TRICARE Contract Award for the Audit of
Capital and Direct Medical Education Costs
DOCS Open #s 105734 & 105736

Deputy Chief, TAD	Concur 4/21/06
Chief, OGC	Concur 4/23/06
Chief, HPO	Concur 5/16/06
CoS, TMA	_____
CoS, HA	_____



Inspector General Department of Defense

