
January 17, 2007



Hold for Release
Expected 2:30 p.m.

Statement
of
Mr. Thomas F. Gimble
Acting Inspector General
Department of Defense

before the
Subcommittee on Readiness
Senate Committee on Armed Services
on
"Services and Inter-Agency Contracting"

Mr. Chairman and Members of the Subcommittee on Readiness:

Thank you for the opportunity to appear before the committee today to address our ongoing oversight work regarding interagency contracting.

Our recent efforts in interagency contracting began in FY 2004 with a compliance audit of DoD purchases made through the General Services Administration (GSA) in response to section 802 of the National Defense Authorization Act for FY 2005. Section 811 of the National Defense Authorization Act for FY 2006 expanded the scope of the compliance audits to include the DoD use of interagency contracting at the Department of Interior, the Department of the Treasury, and the National Aeronautics and Space Administration. Section 817 of the National Defense Authorization Act for FY 2007 further expanded our scope to include the National Institutes of Health and the Department of Veterans Affairs. Each of these audits has been an effort performed by the Inspectors General of DoD and the non-DoD agency being reviewed.

We have issued final reports of our joint audits at four agencies: GSA, the Department of the Interior, the Department of the Treasury, and the National Aeronautics and Space Administration. Collectively, these agencies awarded 54,022 contract actions valued at about \$5.4 billion for DoD during FY 2005. To conduct the audits, we reviewed 352 contract actions valued at about \$1.0 billion.

Audits of Interagency Contracting at GSA and the Department of the Interior

Today, I will talk specifically about contracting and funding problems found during the audits of interagency contracting at GSA and the Department of the Interior, the two largest agencies audited. We have completed two audits at GSA as required by the FY 2005 National Defense Authorization Act. We have also completed our first audit at the Department of the Interior and are working on the second year follow-up audit.

Overall, we found significant contracting and funding problems. We found a lack of market research by both DoD and non-DoD agencies. When a DoD organization initiated its requirement, it did not determine whether it was in DoD's best interest to make the purchase through a DoD contracting office or pay a 2 to 5 percent fee for assistance from a non-DoD agency. On the other hand, GSA and Interior did not always make sure the contracting vehicle or contractor used was the best for the purchase. Other contracting problems involved a lack of competition, determining fair and reasonable pricing, providing adequate contract surveillance, and establishing leases and construction projects without proper approvals. Regarding funding problems, we found that DoD activities used GSA and the Department of the Interior revolving funds as places to "park" or "bank" funds that were expiring. Subsequently, both GSA and Interior placed contracts for DoD customers using the expired funds, thereby circumventing DoD appropriations law. We determined that at GSA, about \$1 billion to \$2 billion in

expired funds remained in the “bank” at the end of our FY 2005 audit. At the Department of the Interior, we identified about \$400 million that we believed should have been returned to the Treasury as expired funds. Most of the contracting and funding problems were driven by three factors: the desire to hire a particular contractor, the desire to obligate expiring funds, and the inability of the DoD contracting workforce to timely respond to its customers.

Contracting Problems

The contracting problems stem from hurried buys with little or no planning, mostly due to DoD program managers attempting to quickly obligate funds about to expire. We found that DoD and non-DoD officials skipped basic planning and contracting fundamentals such as performing market surveys, competing acquisitions, determining price reasonableness, conducting surveillance on services received, and obtaining required approvals for construction and leasing contracts. We found some severe contracting problems. For example, the Department of the Interior awarded a contract worth \$100 million without proper approvals or competition to lease office space for the Counterintelligence Field Activity. Interior officials also awarded a contract to a computer software and construction firm to procure armor for Army vehicles going to Kuwait. We also found illogical purchases such as DoD program officials using non-DoD agencies who in turn made purchases using credit cards, Federal Supply Schedules, and even existing DoD contracts.

Of the 131 GSA purchases and 49 Department of the Interior purchases reviewed, we found only one instance where a DoD organization documented that using a non-DoD agency to award the contract was in the best interest of the Government. Program and contract officials conducted almost no market research on the other interagency purchases we reviewed. DoD used the Department of the Interior to purchase approximately \$592 million of goods and services from the Federal Supply Schedules. For that service, DoD paid the Department of the Interior more than \$23 million in surcharges for purchases that could have been routinely handled by junior DoD contracting personnel. DoD often paid surcharges for GSA and the Department of the Interior to purchase low-cost military equipment or commercial items that could have been obtained from existing DoD contracts. The Federal Acquisition Regulation specifies that it is the responsibility of the requiring activity to perform market research. We asked DoD personnel why they used a non-DoD agency instead of a DoD contracting office. DoD personnel stated that the non-DoD agency processed the purchases faster than DoD and they could generally get the contractor they wanted.

During our review of GSA FY 2005 purchases, we examined 14 contract actions to evaluate the adequacy of contracts awarded on a sole-source basis. We determined that 6 of the 14 actions did not comply with the Federal Acquisition Regulation because GSA did not adequately justify the use of sole-source contracts. Similarly, at the Department of the Interior, there was no competition for 27 of the 49 purchases reviewed. However, most of the Department of the

Interior purchases were exempt from Federal Acquisition Regulation competition requirements. The contracts were given to either small business 8(a) contractors that were owned by Native Americans or to contractors where only one bid was received. When competition was obtained, it was generally satisfied by obtaining a minimum of three bids by posting the solicitation on e-Buy.

During our joint effort, GSA auditors identified that 64 percent of the GSA orders and modifications reviewed lacked required documentation showing that the Government received fair and reasonable prices. At the Department of the Interior, we determined that contracts for services tended to have more problems with price reasonableness than contracts for products. Of the 49 purchases reviewed, 24 were for services and 25 were for products. For 20 of the 24 services purchases reviewed, contracting officers did not adequately document and support that prices paid were fair and reasonable. Of the 25 product purchases reviewed, contracting officers did not adequately document price reasonableness for 5 purchases.

Of the 131 GSA purchases reviewed, 117 did not have adequate surveillance plans that met Federal Acquisition Regulation requirements. Government surveillance was also not adequate for 23 of the 24 Department of the Interior services contracts reviewed. On almost all interagency purchases, it was unclear who had responsibility for surveillance. Furthermore, when DoD was responsible for surveillance, DoD officials were unable to demonstrate how they effectively monitored contractor performance. In some cases, we found non-DoD

contracting officers without security clearances awarding contracts with classified statements of work. We found a lack of quality assurance surveillance plans, designation letters establishing contracting officer representatives, and a general lack of contract oversight.

One of the potentially most serious problems was when DoD and Department of the Interior officials leased office space for the Counterintelligence Field Activity by using a service contract instead of following required procedures through GSA. When leasing costs surpass a cost threshold, DoD officials must contact GSA before leasing space to accommodate computer and telecommunications operations and secure or sensitive activities related to the national defense or security. The Administrator of General Services must determine whether leasing the space is necessary to meet requirements that cannot be met in public buildings. GSA then submits that determination to the Senate Committee on Environment and Public Works and the House Committee on Transportation and Infrastructure. Public Law also requires the Secretary of the applicable Military Department to notify the Senate Committee on Armed Services and the House Committee on Armed Services when certain cost thresholds are met on leases of real property. The 10-year, \$100 million lease for the Counterintelligence Field Activity was disguised as a service contract and exceeded all thresholds that require Congressional notification and approval. If DoD and Interior managers are allowed to purchase lease space via service contracts, congressional and senior DoD oversight will be lost, and other DoD

activities will be making “end runs” around GSA and Congressional approvals.

We are currently aware of two other major leases that similarly circumvented the process.

Funding Problems

Funding problems revolved around year end spending and attempts by DoD managers to obligate funds that are about to expire. We found numerous instances of DoD officials using interagency revolving funds to “park” or “bank” funds. We also found instances of officials using the wrong appropriation to fund contracts. Overall, we identified 107 potential Antideficiency Act violations at the four agencies reviewed. Of the 107 potential violations, 72 were identified in GSA and the Department of the Interior. The follow-on audit at the Department of the Interior has already identified at least an additional 250 potential violations, 189 of which occurred after officials were notified that continued use of expired funds was contrary to DoD business practices. Exacerbating these funding problems are accounting processes at non-DoD agencies. For example, non-DoD agencies sometimes accept expired funds for incremental portions of services contracts, or bill for advance payments. These processes make it difficult or impossible to maintain oversight and make corrective accounting entries.

Of the 72 potential Antideficiency Act violations at GSA and the Department of the Interior, 63 involved the bona fide needs rule, and 17 involved

using the wrong appropriation. There were instances where both problems occurred on the same purchase.

On 41 purchases reviewed at GSA and 22 purchases at the Department of the Interior, DoD funding authorities potentially violated the bona fide needs rule. That is, they used an annual appropriation to purchase goods or services that they needed in the following year rather than in the year of the appropriation. In many cases, the DoD funding authorities used annual operations and maintenance appropriations to fund the purchase of severable services to be received in the year following the year of the appropriation. For example, the U.S. Central Command Air Force sent \$18.5 million of funds that expired on September 30, 2005, to fund the support of a Network Operations Security Center from October 1, 2005, through September 30, 2006.

At the Department of the Interior, we found goods described as “commercial” in contract documentation that were ordered or delivered many months past the expiration date of the appropriation. For example, Department of the Interior contracting officials used FY 2002 operations and maintenance funds to pay for FY 2006 purchase orders. Those funds had been expired for 3 years.

On 16 GSA purchases and 1 Department of the Interior purchase, we found that the wrong appropriation was used; in some cases, fiscal policy was severely abused. For example, the first GSA audit found that the Program Manager, Defense Communications and Army Transmissions Systems sent \$44 million of operations and maintenance funds to GSA for the Army Materiel Command

Headquarters Relocation purchase. GSA used the funds to contract for the construction of two modular two-story office buildings totaling about 230,000 square feet at Fort Belvoir. The buildings serve as the headquarters of the Army Materiel Command and provide office space for about 1,400 civilian and military personnel. Although the Army contended that construction did not occur, no buildings existed at the site prior to the contract. Army officials stated that using operations and maintenance funds was correct because the contractor was providing a service: the use of the buildings. However, the procurement of these buildings was clearly a construction project. The Army should have used Army Military Construction funds, even though the approval of construction projects is a far lengthier process in DoD than in GSA.

Adding to the DoD funding control problems is the Department of the Interior use of “advance payments” for DoD purchases. Advance payments result in a series of internal control problems at DoD because this process generally removes the ability of DoD to account for funds transferred to the Department of the Interior. When DoD sends a funding document to another agency for a purchase of goods or services, DoD expects that agency to bill DoD as costs are invoiced and paid. However, using the “advance payments” method, the Department of the Interior collects the full amount of the funding document within 48 hours after receipt and acceptance of the document. Accordingly, DoD has paid for goods and services before they are even contracted for. This process makes it extremely hard for DoD to oversee and reconcile its funds at the

Department of the Interior. DoD generally relies on the Department of the Interior to furnish the amounts of unused balances of DoD funds.

Also adding to the funding problems, non-DoD agencies incrementally fund portions of severable services contracts. Public Law allows the funding of severable services contracts to cross fiscal years as long as the funds are obligated and work is started in the year of the appropriation and is for a period not to exceed 12 months. However, the law is not clear about the 12-month rule when incremental funds are used. For instance it is unclear whether it is proper to obligate FY 2006 funds in September 2006 for work to be performed in June of 2007 on a severable services contract that began in April of 2006.

As mentioned earlier, we have reported 72 potential Antideficiency Act violations at GSA and the Department of the Interior. We expect to report at least another 250 potential violations at the Department of the Interior due to the use of expired funds. In July 2005, we also reported 38 potential Antideficiency Act violations. DoD conducted preliminary reviews in a timely manner in accordance with DoD regulations for only 8 of those 38 potential violations. However, the preliminary reviews are now complete on the 38 GSA potential Antideficiency Act violations reported in July 2005. The reviews determined that 11 still require a formal investigation to determine whether an Antideficiency Act violation occurred. Ten have had corrective actions taken that removes the Antideficiency Act violation that had occurred (for example, replacing the initial appropriation used with another year's appropriation or another type of appropriation). In

17 cases, the preliminary review concluded that an Antideficiency Act violation did not occur. However, in our January 2, 2007, compendium report on potential Antideficiency Act violations, we recommended that the Under Secretary of Defense (Comptroller)/Chief Financial Officer reassess 12 of those 17 cases because the potential Antideficiency Act violations appeared egregious. Further, to our knowledge, none of the investigations held individuals responsible for the violations. Unless responsible individuals are held accountable, the problems will remain.

Causes

In FY 2004, when our interagency contracting audits began, DoD guidance on the use and funding of interagency contracting vehicles was unclear. We had previously cited the simultaneous growth of contracting for services by DoD and the reduction of acquisition personnel as a cause of contracting problems within DoD. That factor combined with DoD lack of market research and non-DoD agencies emphasizing that their funds could be used to legally extend an appropriation's period of availability ("banking of funds") created serious financial problems. Additionally, the marketing of procurement services by non-DoD agencies put pressure on their own contracting offices to offer streamlined acquisition methods that do not include such time-consuming requirements as competing acquisitions or certifying price reasonableness. This generally resulted in the contractor desired by the requiring DoD activity receiving the contract

award. In short, we believe most of the problems will be resolved if the option to “bank” funds and the ability to award to a preferred vendor are eliminated.

Furthermore, if DoD organizations perform adequate market research, many of the purchase requests sent to non-DoD agencies will remain within DoD.

Corrective Actions

DoD officials have taken many corrective actions as a result of our interagency contracting audits.

- On December 4, 2006, the Director of Defense Procurement and Acquisition signed a memorandum of agreement with the Chief Acquisition Officer of GSA. The memorandum states DoD and GSA share a single objective of providing the best value goods and services, in a timely manner, to support the warfighter. DoD and GSA agreed to work together on 22 basic contracting management controls. These include such controls as ensuring that sole-source justifications are adequate, that statements of work are complete, and that interagency agreements describe the work to be performed.
- GSA has worked with DoD to identify unused and expired DoD funds in GSA accounts. So far, GSA has returned over \$600 million to DoD, and it continues to review its accounts.
- The Department of the Interior has withdrawn numerous contracting officer warrants due to findings of the joint DoD and Department of

the Interior audits. It continues to revise interagency contracting procedures to include establishing a legal review procedure.

- On October 16, 2006, the DoD Acting Deputy Chief Financial Officer revised financial policy by issuing a memorandum, “Non-Economy Act Orders.” The memorandum implements many internal controls. For example, for Non-Economy Act orders in excess of the simplified acquisition threshold, the requesting official must provide evidence of market research and acquisition planning, and a statement of work that is specific, definite, and certain. The memorandum states that all Non-Economy Act orders greater than \$500,000 must be reviewed by a DoD-warranted contracting officer prior to sending the order to the funds certifier or issuing a funding document to a non-DoD organization. The memorandum also includes much-needed funding guidance. Specifically, it clarifies the DoD position on obligating funds for goods and severable services. However, it does not address incremental funds and how to provide adequate oversight over funds processed by Advance Payment.

Actions Needed

The problems reported are not new to the Government. We have reported on similar problems for many years, and material internal control weaknesses over

DoD contracting and funding processes continue to exist. We believe DoD must continue to make it a priority to correct these problems. Clarification of funding guidance is required. DoD should not provide “advance payments” when transacting interagency financial agreements. Incremental funding of services contracts with funds that are expiring needs to be clearly addressed. Further, formal investigations of all the potential Antideficiency Act violations we have reported need to be completed, accountable individuals need to be identified, and appropriate administrative actions need to be taken. The deliberate circumvention of Appropriation Law cannot be condoned.

Listing of DoDIG Reports with Interagency Contracting Issues

DoDIG Report No. D-2007-042, "Potential Antideficiency Act Violations on DoD Purchases Made Through Non-DoD Agencies," January 2, 2007

DoDIG Report No. D-2007-032, "FY 2005 DoD Purchases Made Through the Department of Treasury," December 8, 2006

DoDIG Report No. D-2007-023, "FY 2005 DoD Purchases Made Through the National Aeronautics and Space Administration," November 13, 2006

DoDIG Report No. D-2007-007, "FY 2005 DoD Purchases Made Through the General Services Administration," October 30, 2006

DoD IG Report No. D-2006-029, "Report of Potential Antideficiency Act Violations Identified During the Audit of the Acquisition of the Pacific Mobile Emergency Radio System," November 23, 2005

DoD IG Report No. D-2005-096, "DoD Purchases Made Through the General Services Administration," July 29, 2005

DoD IG Report No. D-2005-003, "DoD Antideficiency Act Reporting and Disciplinary Process," October 14, 2004

DoD IG Report No. D-2004-084, "Antideficiency Act Investigation of the Research, Development, Test and Evaluation, Defense-Wide Appropriation Account 97 FY 1989/1990 0400," May 28, 2004