



Office of Audits Office of Inspector General U.S. General Services Administration

DATE: September 19, 2016

TO: Thomas A. Sharpe, Jr.
Commissioner
Federal Acquisition Service (Q)

FROM: R. Nicholas Goco 
Assistant Inspector General for Auditing
Office of Audits (JA)

SUBJECT: Major Issues from Multiple Award Schedule Preaward Audits
Audit Memorandum Number A120050-6

This memorandum details issues identified during our Fiscal Year (FY) 2014 preaward audits. We have raised a number of these issues in three prior Major Issues memoranda.¹ This memorandum also highlights issues with schedule pricing, the Price Reductions clause, and overbillings that have not previously been raised in these memoranda.

For purposes of this memorandum, we have organized these issues under two broad categories:

- GSA's Multiple Award Schedules Program (Schedules Program) may not provide the lowest overall cost alternative to meet the government's needs; and
- Contractors are not in compliance with their schedule contract terms and conditions.

The pervasiveness of these issues indicates that additional management attention is needed to bring improvements to the Schedules Program – the largest interagency contracting vehicle in the federal government.

Background

Under the Schedules Program, FAS establishes long-term governmentwide contracts. Through these contracts, millions of commercial products and services are made available to customer agencies. In FY 2014, Schedules Program sales exceeded \$32 billion.

¹ Memoranda dated September 26, 2011; March 8, 2013; March 25, 2014; and March 13, 2015.

Our office conducts preaward audits to assist contracting officers in negotiating schedule contracts. These audits provide contracting officers with an evaluation of contractor-supplied CSP information and detail whether contractors are in compliance with specific terms and conditions of their contracts.

In FY 2014, we issued 42 preaward audits of contracts with estimated sales of over \$6.5 billion for their pending contract periods. As a result of these audits, we recommended price and discount adjustments that, if realized, would allow for over \$221 million in cost savings for the government and, ultimately, the taxpayer. We also informed contracting officers of numerous instances of contract non-compliance.

Results

GSA's Schedules Program may not provide the lowest overall cost alternative to meet the government's needs.

The intent of the Schedules Program is to leverage the government's buying power in an effort to provide customer agencies with competitive, market-based pricing. To achieve this, schedule contracts must comply with a number of statutory and regulatory requirements. For instance, the *Competition in Contracting Act of 1984* provides that GSA's schedule contracts and the orders placed against them meet competition requirements as long as they result in the lowest cost alternative in order to meet the government's needs. In addition, General Services Administration Acquisition Regulation (GSAR) 538.271, *MAS Contract Awards*, states that schedule prices must be fair and reasonable. To assist contracting officers in complying with this regulation, FAS issued Procurement Information Bulletin (PIB) 04-2, *Achieving Fair and Reasonable Prices in Multiple Award Schedule Negotiations*, outlining its goal for the Schedules Program "...to achieve the best possible prices and terms for both customers and taxpayers."

Customer agencies generally rely on schedule prices based on the presumption that GSA has complied with these Schedules Program requirements. However, if GSA is not meeting these requirements, the government may be overpaying for the products and services being purchased. Our FY 2014 preaward audits identified instances in which schedule prices did not reflect contractors' actual sales practices, schedule prices were not adequately monitored, and contractor-supplied data was not current, accurate, or complete. In addition, we found examples of contracting officers not leveraging the government's collective purchasing power and not fully maximizing identified cost savings.

Contractors' CSP disclosures are not consistently providing sufficient GSA and commercial sales information needed to obtain fair and reasonable pricing. CSP disclosures provide a link to the commercial marketplace by outlining a contractor's commercial sales practices for the contracting officer to evaluate and use as a basis to establish schedule pricing. In order to obtain a schedule contract, contractors are

required to submit current, accurate, and complete CSP disclosures with their offer. The information in these disclosures allows the contracting officer to determine if the proposed schedule prices are fair and reasonable and in line with the contractor's commercial sales practices. Without current, accurate, and complete CSP disclosures, the contracting officer's ability to provide customer agencies with market-based pricing, the foundation of the Schedules Program, is significantly impaired.

Of the audited contractors in FY 2014, 79 percent (33 out of 42) submitted CSP disclosures that were not current, accurate, and/or complete. If the contractors had provided all of the required information, contracting officers could have used that information to obtain potential cost savings of over \$405 million.

Further, when schedule sales account for the majority of a contractor's sales, schedule prices should be at least equal to or better than those granted to other customers. GSAR 538.270, *Evaluation of Multiple Award Schedule Offers*, establishes that the government will seek to obtain pricing equal to or better than the best pricing afforded to a contractor's other customers. If schedule sales account for the majority of a contractor's sales, GSA should leverage its purchasing power to receive pricing equal to or better than the contractor's other customers. In fact, FAS PIB 00-10, *Fair and Reasonable Prices and the MAS Pricing Policy*, states that the statutory justification for the Schedules Program is to take advantage of this purchasing power.

For 18 of the contracts we audited in FY 2014, Schedules Program users were the contractor's largest customer, based on sales volume. However, 39 percent of these contractors (7 out of 18) did not offer schedule pricing that was equal to or better than the contractor's best customer. Targeting the prices of these seven contractors' best customers could potentially save the government approximately \$79 million. This demonstrates the importance of maximizing the government's purchasing power to obtain better pricing and realize cost savings for the government and, ultimately, the taxpayer.

Schedule prices are being treated as ceiling prices. FAR 8.405, *Price Reductions*, allows customer agencies to seek discounts at the task order level. However, prices consistently granted below established schedule prices are an indicator that schedule prices are treated as ceiling prices. As a result, schedule prices may be too high. FAS internal guidance supports this assertion stating:

It is erroneous to allow prices higher based on the theory that agencies will negotiate better prices on individual orders.... Higher prices based on this logic undermines the credibility of the MAS Program. (PIB 00-10)

Additionally, high schedule prices increase the risk that customer agencies will overpay for products and services ordered through the Schedules Program, thereby wasting taxpayer dollars.

In FY 2014, 55 percent of our preaward audits (23 of 42) identified instances of contractors routinely granting lower prices to schedule customers than those offered on schedule. For one contract, schedule customers received average discounts of up to 19 percent higher than schedule discounts offered on the majority of its schedule sales. For another, the contractor stated that schedule prices do not reflect its best pricing and that schedule prices are viewed only as ceiling prices. The prevalence of this practice indicates that, in some cases, schedule pricing may not be providing customer agencies with the best price.

Contracting officers are not maximizing savings identified by preaward audits. As outlined above, current, accurate, and complete CSP disclosures are vital in order to establish fair and reasonable prices and save taxpayer dollars. In preaward audits, we obtain and analyze a contractor's sales transactions for a specified period of time (generally 1 year) to verify the CSP data. If we identify better pricing and/or terms and conditions than those disclosed by the contractor, we provide the information to the contracting officer as recommended cost savings.

Of the 42 preaward audits issued in FY 2014, contracting officers have exercised extension options for 24 of the subject contracts. For these audits, we identified and recommended cost savings totaling approximately \$221 million for the remaining option extension periods.² However, contracting officers only negotiated savings of \$93 million (43 percent).

In your response to our FY 2013 Major Issues memorandum dated June 26, 2015, you stated that "Commercial pricing...is based on quantity/volume commitments, risk, scope and/or other commercial terms and conditions. The comparison to Schedule prices...is not a valid comparison." We disagree. According to FAR 8.402, *Federal Supply Schedules, General*, the Schedules Program provides federal agencies with a simplified process for obtaining commercial supplies and services at prices associated with volume buying. Likewise, our preaward audits, in analyzing a contractor's CSP and sales data, consider volume and other terms and conditions when assessing the comparability of a contractor's commercial customers to its schedule customers. These comparisons are often included in preaward audit reports and provided to the contracting officers for their price evaluations and contract negotiations.

The recommended cost savings in our audit reports are based on significant data analysis that otherwise would not be available to contracting officers for negotiations. These analyses are provided as an aid to contracting officers in their decisions and to improve negotiation results in order to maximize cost savings for the government and taxpayers.

² All of the audited contract option periods were 5 years. However, in the event a contract was temporarily extended to complete the audit and/or conduct and complete negotiations, we reduced the applicable cost savings by that amount of time.

The Price Reductions clause protections were negated by ineffective basis of award customers. The Price Reductions clause provides a key price protection to the government by regulating price changes over the life of schedule contracts. Each contract establishes a customer or category of customers to serve as the basis for schedule prices. This relationship is required to be monitored and maintained; if prices granted to the basis of award customer decrease, the prices to the government are also required to decrease. This price protection is vital to ensuring the government maintains competitive, market-based pricing throughout the life of multi-year schedule contracts.

Despite the importance of the Price Reductions clause to the protection of taxpayer dollars, 43 percent of our FY 2014 audits (18 out of 42) identified an ineffective basis of award customer was established. We also highlighted this issue and its related negative impact on schedule prices in a July 2016 audit report issued on IT reseller contracts. In that report, we recommended that FAS implement controls to ensure that deviations to the Price Reductions clause do not diminish the price protections.³ When the relationship is ineffective, the government loses its price protection and may pay more than the contractor's commercial customers.

Contractors are not in compliance with their schedule contract terms and conditions.

The Schedules Program requires contractors to comply with terms and conditions incorporated into their contracts. However, our FY 2014 preaward audits identified contractors violating several contract terms and conditions including, but not limited to, labor qualifications in service contracts, the reporting of sales and computation of the Industrial Funding Fee (IFF), and customer billing requirements.

Contractors provide the government with unqualified labor. For service contracts awarded under the Schedules Program, minimum educational requirements and/or experience qualifications are established for employees to qualify for specific labor categories. In FY 2014, we audited 20 service contracts and found that 25 percent of contractors charged the government for labor that did not meet the minimum requirements of the contract. In one instance, the auditors found that 53 percent of the sampled employees failed to meet minimum labor requirements. When a contractor provides labor that fails to meet these contractual requirements, customer agencies do not receive the level of services they pay for and overpay for the labor that they receive.

Contractors have inadequate systems to accumulate and report schedule sales and are improperly computing IFF payments. Schedule contractors are required by their contracts to pay IFF of 0.75 percent for all schedule sales to fund GSA's program administration costs. Contractors should have an adequate system in place to ensure that these sales can be accumulated and reported accurately, as required by GSAR 552.238.74, *Industrial Funding Fee and Sales Reporting*.

³ *IT Reseller Contracts Present Significant Challenges for GSA's Schedules Program* (Report Number A120026/Q/6/P16003, July 22, 2016).

Of the preaward audits performed in FY 2014, 43 percent of the audited contractors (18 out of 42) did not have adequate systems in place to accumulate and report schedule sales. Over 83 percent of those contractors (15 out of 18) improperly computed IFF, resulting in approximately \$2.8 million of unpaid IFF. If a contractor's system is unable to identify and report on schedule sales accurately, its IFF computation will be inaccurate and GSA will not collect the correct IFF that is due.

Customer agencies are being overbilled for contract items. When contracts are awarded, schedule prices are established and agreed upon by the contracting officer and the contractor. These prices cannot be changed unless mutually agreed upon. However, in some cases, customer agencies are being overbilled. In 29 percent of FY 2014 preaward audits (12 out of 42), we found that contractors billed the government at higher prices than those established under their contracts. These overbillings totaled just under \$1 million.⁴ In such instances, customer agencies are paying more than the schedule prices.

Conclusion

The *GSA Multiple Award Schedules Program Desk Reference* states that cost savings through the Schedules Program are realized, in part, by “competitive, market-based pricing that leverages the buying power of the federal government.” As such, FAS should work to ensure that these cost savings are achieved under the Schedules Program and schedule prices provide the lowest cost alternative to meet the government's needs. In addition, FAS needs to ensure contractors comply with contract requirements to protect both FAS and its customer agencies. With FY 2014 schedule sales exceeding \$32 billion, it is imperative that FAS management take appropriate measures to address the issues identified in this memorandum. Improvements in these areas will strengthen the integrity and cost effectiveness of the Schedules Program, and protect the taxpayer.

If you have any questions regarding this audit memorandum, please contact Brian J. Gibson, Associate Deputy Assistant Inspector General for Auditing, at (202) 273-7278, or me at (202) 501-2322.

⁴ In one instance, the total amount of overbillings was not computed; therefore, this amount is conservative.

Memorandum Distribution

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