



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

Audit of GSA's Cost- Reimbursement Contracts

Report Number A120052/Q/A/P12004
March 30, 2012



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

REPORT ABSTRACT

OBJECTIVE

To determine if the cost-reimbursement contracts and task orders GSA entered into between March 17, 2011, and September 30, 2011, comply with the provisions of interim rule 76 Federal Register 14543.

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WHAT WE FOUND

We identified the following during our audit:

Finding 1 – The cost-reimbursement contracts and task orders GSA entered into between March 17, 2011, and September 30, 2011, do not fully comply with the provisions of interim rule 76 Federal Register 14543. This increases the likelihood that the risks characteristic of this type of contract will occur.

WHAT WE RECOMMEND

We recommend that the Commissioner of the Federal Acquisition Service:

1. Reaffirm internal guidance (i.e., Federal Acquisition Service Instructional Letter 2011-18) and develop additional internal policies to ensure that acquisition personnel understand how interim rule 76 Federal Register 14543 and related Federal Acquisition Regulation changes affect existing and future contracts and task orders.
2. Incorporate the requirements as a result of interim rule 76 Federal Register 14543 into existing acquisition plan templates.

MANAGEMENT COMMENTS

The Commissioner of the Federal Acquisition Service concurred with the audit report finding and recommendations. Management's written comments to the draft report are included in their entirety as Appendix B.

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

DATE: 3/30/2012

TO: Steven Kempf
Commissioner, Federal Acquisition Service (Q)

FROM: Michelle Westrup *Michelle Westrup*
Audit Manager, Acquisition Programs Audit Office (JA-A)

SUBJECT: Audit of GSA's Cost-Reimbursement Contracts
Report Number A120052/Q/A/P12004

This report presents the results of our audit of GSA's cost-reimbursement contracts. Our finding and recommendations are summarized in the Report Abstract. Instructions regarding the audit resolution process can be found in the email that transmitted this report.

Your written comments to the draft report are included in Appendix B of this report.

If you have any questions regarding this report, please contact me or any member of the audit team at the following:

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On behalf of the audit team, I would like to thank you and your staff for your assistance during this audit.

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Introduction

High risk contracts, such as cost-reimbursement contracts, provide no direct incentive for contractors to control costs. They are often used without appropriate justification or sufficient management and oversight. As a result, the risk to the taxpayer escalates.

Section 864 of the Duncan Hunter National Defense Authorization Act for Fiscal Year 2009 (the Act) effected revisions to the Federal Acquisition Regulation (FAR) strengthening the guidance regarding the use of cost-reimbursement contracts. These FAR revisions address: (1) when cost-reimbursement contracts are appropriate; (2) the type of findings an acquisition plan must have to support a decision to use cost-reimbursement contracts; and (3) the assessment of the workforce resources needed to award and administer cost-reimbursement contracts. The Act also requires that the Inspector General of each executive branch agency review the agency's use of cost-reimbursement contracts¹ for compliance with these regulations.

On March 16, 2011, the Department of Defense, GSA, and the National Aeronautics and Space Administration jointly issued interim rule 76 Federal Register 14543 to address section 864 of the Act. The interim rule provides regulatory guidance regarding the proper use and management of cost-reimbursement contracts. The interim rule aligns with the March 4, 2009 Presidential Memorandum on Government Contracting which directs agencies to reduce the use of high risk contracts.

On March 2, 2012, the Department of Defense, GSA, and the National Aeronautics and Space Administration adopted the interim rule as final with changes. The final rule changes are effective on April 2, 2012 and will be published in the FAR.

The objective of our audit was to determine if the cost-reimbursement contracts and task orders² GSA entered into between March 17, 2011, and September 30, 2011, comply with the provisions of interim rule 76 Federal Register 14543.

To accomplish this objective, we reviewed a sample representing 99 percent of the dollars obligated under cost-reimbursement type procurements entered into by GSA during the audit period. This sample consisted of ten cost-reimbursement task orders awarded by various offices within the Federal Acquisition Service (FAS).³

See Appendix A – Purpose, Scope, and Methodology for additional information.

¹ The Act applies to cost-reimbursement contracts or orders issued under contracts previously awarded. See Regulations on the Use of Cost-Reimbursement Contracts, Public Law 110-417, 122 Stat 4549 (2008).

² For the purposes of this report, the term task order is a generic term to include task and delivery orders.

³ As all orders reviewed were from within FAS, the audit recommendations are addressed to the FAS Commissioner.

Results

Finding 1 – The cost-reimbursement contracts and task orders GSA entered into between March 17, 2011, and September 30, 2011, do not fully comply with the provisions of interim rule 76 Federal Register 14543.

The cost-reimbursement contracts and task orders GSA entered into between March 17, 2011, and September 30, 2011, do not fully comply with the provisions of interim rule 76 Federal Register 14543. Specifically, GSA acquisition personnel did not consistently assure that: (1) acquisition plans were properly developed; (2) the designation of the contracting officer's representative was timely or distributed appropriately; and (3) contractors' accounting systems were adequate for tracking costs during the entire period of performance. As a result, the risks inherent with this type of contract (unnecessary costs and/or reduced quality of the goods and services) are more likely to occur and/or be mismanaged.

Acquisition Planning

The acquisition plans for nine of the ten task orders we reviewed, did not address at least one provision of Federal Acquisition Regulation (FAR) 16.103(d)(1) which stipulates the requirements for planning and documenting the planning of cost-reimbursement contracts.

Additional Risks and Risk Management. The acquisition plans for three task orders in our sample did not document the additional risks assumed by the Government as a result of using cost-reimbursable contracts as required by FAR 16.103(d)(1)(ii). In addition, four task orders did not state how the Government identified those risks, three task orders did not discuss the nature of the additional risks, and one task order did not discuss how the Government will manage and mitigate those risks. As a result, these task orders were not fully in compliance with FAR 16.103(d)(1)(ii)(A-C).

Assessment of Resources. The acquisition plans for two task orders did not provide an assessment regarding the adequacy of Government resources to properly plan for, award, and administer a cost-reimbursement procurement in accordance with FAR 16.103(d)(1)(iii) and FAR 16.103(d)(1)(iv)(C).

Plans to Minimize Future Use and Transition to Firm-Fixed-Price. For nine task orders, the acquisition plans did not document the actions planned to minimize the use of other than firm-fixed-price⁴ contracts on future acquisitions for the same requirement. Additionally, they did not include a documented plan to transition, to the maximum extent practicable, to a firm-fixed-price contract. As a result, these task orders did not comply with FAR 16.103(d)(1)(iv)(D).

⁴ By definition, other than firm-fixed-price contracts include cost-reimbursement contracts.

Rationale for Fee Provision. The acquisition plan for one task order did not discuss why a fee provision was included in accordance with FAR 16.103(d)(1)(v).

In reviewing the acquisition plans for the task orders in our sample, we noted that nine were prepared prior to the issuance of Federal Acquisition Service (FAS) Instructional Letter 2011-18. This FAS-specific document informed acquisition personnel of the interim changes to the FAR and provided guidance on how to adhere to the regulation's provisions. However, it was issued more than four months after the interim rule (and its related requirements) went into effect. Despite policies in place to distribute new regulations in a timely manner, acquisition personnel informed us that they were unaware of the interim rule. The provisions of FAR 16.103(d)(1) are intended to help ensure acquisition personnel fully consider all of their options when choosing to use something other than a firm-fixed price contract. Acquisition plans should demonstrate that a well-planned strategy is in place with a resource assessment to properly manage and mitigate the risks associated with cost-reimbursement contracts and task orders.

Contracting Officer's Representative Responsibilities

At least one of the FAR requirements regarding the designation of the contracting officer's representative (COR) was not adhered to in all ten task orders we reviewed.

The COR helps monitor the technical aspects of the contract and assists with contract administration. FAR 16.301-3(a)(4)(i) states that cost-reimbursement may only be used when the COR, in accordance with FAR 1.602-2, is designated prior to award of the contract or order. FAR 1.602-2(d)(6) requires that the designation be in writing and that it specify the COR's responsibilities, authorities and limitations. FAR 1.602-2(d)(6) states a copy of this written designation must be provided to the contractor.

Each task order in our sample contained a designation letter, signed by the contracting officer and the COR, spelling out the COR's responsibilities and authorities. However, in four instances, the COR was not officially designated prior to award as required by FAR 16.301-3(a)(4)(i). Three of these task orders were awarded before the effective date of FAS Instructional Letter 2011-18. In addition, as discussed in the previous section, multiple acquisition personnel stated that they were unaware of the interim rule when it went into effect.

In nine cases, acquisition personnel did not provide a copy of the designation letter to the contractor as required by FAR 1.602-2(d)(6). Acquisition personnel informed us that they do not normally provide a copy of the COR's designation letter to the contractor. While the contractor does receive a copy of the contract, which identifies the COR, the contract does not outline the exact authorities and limitations specified in FAR 1.602-2(d)(6)(i-v) as the written designation letter does.

The role of the COR is significant for cost-reimbursement contracts and task orders due to the additional inherent risks. Thus, the assignment of a COR and his or her respective responsibilities should be established prior to award as part of the proactive

planning required by FAR 16.301-3(a)(4)(i). The COR is an important resource for the contractor as well. Therefore, the official assignment of the COR, his or her responsibilities, limitations, and authority should be articulated to the contractor. This helps ensure that the contract and task orders are managed effectively.

Contractor's Accounting System

In two of the task orders reviewed, we found indications that the contractors' may not have had accounting systems that adequately tracked their costs during the entire period of performance as required by FAR 42.302(a)(12).

The adequacy of a contractor's accounting system impacts the quality and validity of the data the Government relies on for management oversight. This is especially important for cost-reimbursement contracts and task orders.

In one case, the price negotiation memorandum stated that other offerors had approved cost accounting systems; however, the awardee's system was classified as being in an "unaccessed" status pending completion of an audit. The amount obligated to this task at the time of award was \$89,413,000. With regard to the second task order, its base contract was awarded to a contractor that was later acquired by another company. While the original contractor's accounting system was determined acceptable for award of the base contract, acquisition personnel noted that they have not evaluated the current contractor's accounting system. In this case, the dollars obligated to award the task order, under the current contractor, totaled \$9,154,482. FAR does not require a reassessment of a contractor's accounting system at the task order level. However, these two cases indicate that the contractors' accounting systems may not have conformed to the requirements of FAR 42.302(a)(12) .

The Government must rely upon the quality and validity of the cost data maintained by contractor accounting systems in order to effectively manage contracts and task orders. For one of the task orders we reviewed, the contractor's cost accounting system had been determined adequate at the base contract level. However, the contracting officer maintained the acceptability of that system for the award of the task order as well. This continued assurance of the adequacy of the accounting system is essential for task orders in which the Government assumes greater risk, such as cost-reimbursement orders.

Recommendations

We recommend that the Commissioner of the Federal Acquisition Service:

1. Reaffirm internal guidance (i.e., Federal Acquisition Service Instructional Letter 2011-18) and develop additional internal policies to ensure that acquisition personnel understand how interim rule 76 Federal Register 14543 and related Federal Acquisition Regulation changes affect existing and future contracts and task orders.

2. Incorporate the requirements as a result of interim rule 76 Federal Register 14543 into existing acquisition plan templates.

Management Comments

The Commissioner of the Federal Acquisition Service concurred with the audit report finding and recommendations. Management's written comments to the draft report are included in their entirety as Appendix B.

Other Observation

Discrepancy in Acquisition Plan Approval Documentation

FAR 7.103(j) states that acquisition plans for other than firm-fixed-price contracts must be approved and signed by an acquisition official at least one level above the contracting officer. FAS uses an Acquisition Planning Wizard template to generate acquisition plans. For the purposes of acknowledging and approving the acquisition plan, the template contains data fields for the planning officials, including email addresses and dates. For plan approval within the Acquisition Planning Wizard, insertion of an email address and date serves as the electronic signature. In addition to these data fields, the template also contains approval information and an approval status. For one of the task orders sampled, the acquisition plan had the electronic signature (i.e., email address and date) of an acquisition official one level above the contracting officer as required. However, the acquisition plan still had an approval status of "pending." Based upon FAS internal policy, the acquisition plan contained an electronic signature and therefore, met FAR requirements in this capacity. However, from a documentation standpoint, the pending approval status brings the electronic signature of the approver into question. We suggest that FAS management revisit the Acquisition Planning Wizard to ensure consistency and minimize any discrepancies as far as approval status.

Conclusion

The cost-reimbursement task orders that GSA entered into between March 17, 2011, and September 30, 2011, do not fully comply with the provisions in interim rule 76 Federal Register 14543. Consequently, the risks associated with cost-reimbursement task orders may be mismanaged; resulting in unnecessary costs and a decrease in the quality of the products and services provided. We found that acquisition personnel did not consistently identify the risks and risk factors associated with cost-reimbursement task orders in the acquisition plan. Acquisition plans also did not regularly identify actions planned to minimize the use of other than firm-fixed price task orders in the future or actions planned for a transition to firm-fixed-price contracts to the maximum extent practicable. Additionally, acquisition personnel did not always designate a COR prior to award and did not provide a copy of the COR's written designation letter to the contractor. Furthermore, contracting officers may not have consistently ensured the continued adequacy of the contractor's accounting system. To properly plan for and manage cost-reimbursement contracts and task orders, GSA should ensure the provisions of interim rule 76 Federal Register 14543 are applied to existing and future cost-reimbursement contracts and task orders.

Appendix A – Purpose, Scope, and Methodology

Report Number A120052/Q/A/P12004

Purpose

The General Services Administration's (GSA) Office of Inspector General included this audit in its Fiscal Year (FY) 2012 Audit Plan as required by the Duncan Hunter National Defense Authorization Act for FY 2009 (the Act).

Scope

The audit's scope was limited to cost-reimbursement contracts and task orders entered into by GSA between March 17, 2011, and September 30, 2011.

Methodology

To accomplish our objectives, we:

- Reviewed section 864 of the Act and the interim rule 76 Federal Register 14543.
- Reviewed the Federal Acquisition Regulation (FAR) and applicable Federal Acquisition Service (FAS) guidance to ensure compliance with interim rule provisions.
- Reviewed Office of Management and Budget Memorandums regarding Government contracting and Contracting Officer Technical Representatives from March 2009 and November 2007, respectively.
- Reviewed a U.S. Government Accountability Office September 2009 report regarding spending under cost-reimbursement contracts and related controls.
- Obtained GSA's universe of cost-reimbursement contracts and task orders entered into during March 17, 2011, and September 30, 2011. This universe was comprised of 84 contracts and task orders with a total dollar value of \$137,458,784.
- Developed a risk-based judgmental sample of ten task orders with a total dollar value of \$135,724,844.
- Obtained the contract files for the sampled task orders from FAS's Assisted Acquisition Services Business Systems Portal and FAS acquisition personnel.
- Analyzed the contract files of the sampled task orders for compliance with interim rule 76 Federal Register 14543.
- Held discussions with FAS acquisition personnel regarding contract file documentation.
- Obtained input from GSA's Office of Governmentwide Policy regarding the subject FAR provisions.

Appendix A – Purpose, Scope, and Methodology (cont.)

Report Number A120052/Q/A/P12004

We conducted the audit between October 2011 and January 2012 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Internal Controls

Our audit was limited in scope; therefore, our evaluation of internal controls was limited to items discussed in the Results section of this report.

Appendix B – Management Comments

Report Number A120052/Q/A/P12004



GSA Federal Acquisition Service

March 21, 2011

MEMORANDUM FOR KENNETH L. CROMPTON

DEPUTY ASSISTANT INSPECTOR GENERAL FOR
ACQUISITION AUDITS (JA-A)

FROM:

For:
STEVEN J. KEMPF
COMMISSIONER
FEDERAL ACQUISITION SERVICE (Q)

SUBJECT:

GSA Draft Report, "Audit of GSA's Cost-Reimbursement
Contracts" Report #A120052

Thank you for the opportunity to provide comments to the above draft report. My staff has reviewed the draft audit report and we concur with your audit findings and recommendations. In addition, the AAS portfolio has already initiated actions to improve understanding and implementation of Interim Rule 7B within FEDSIM, which awarded the preponderance of cost-reimbursable contracts/task orders reviewed during the audit. AAS will leverage this experience and work towards implementing a similar level of understanding throughout the remainder of the portfolio. Actions already underway in FEDSIM include:

- Acquisition Planning – updates are underway to templates and instructions with a focus on the requirements of the Interim Rule for addressing the use of cost-reimbursable contracts.
- Contracting Officer's Representative responsibilities – the current process is being updated from dependence on manual action by individual Contracting Officers to use existing automated tools to track and ensure compliance with requirements for issuance of the COR designation and distribution to contractors.

Please call me at (703) 605-5400 if you have any questions. Your staff may contact Wayne Williams at (703) 605-2177 or wayne.williams@gsa.gov.

cc: Michelle Westrup, JA-F

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Appendix C – Report Distribution

Report Number A120052/Q/A/P12004

Associate Administrator for Office of Governmentwide Policy (M)

Deputy Chief Acquisition Officer/Senior Procurement Executive (MVD)

Commissioner, Federal Acquisition Service (Q)

Deputy Commissioner, Federal Acquisition Service (Q1)

FAS Chief of Staff (Q0A)

Acting Assistant Commissioner (QF)

Director, Center for FEDSIM (QF0B)

Assistant Commissioner (QT)

Acting Director, Office of Acquisition Operations (QTA)

Commissioner, Public Buildings Service (P)

Deputy Commissioner, Public Buildings Service (PG)

PBS Chief of Staff (PGD)

Division Director, GAO & IG Audit Response Division (H1C)

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Assistant IG for Auditing (JA)

Deputy Assistant IG for Investigations (JID)

Director, Audit Planning, Policy, and Operations Staff (JAO)