U.S. Department of Agriculture

Office of Inspector General
Administration and Finance Division

Audit Report

Review of the Farm Service Agency's Control Over Contracting for the Disposal of Surplus Tobacco

Improved Policies and Procedures are Needed to Monitor Contracting Activities

Report No. 03099-03-Hq
August 2004

UNITED STATES DEPARTMENT OF AGRICULTURE
OFFICE OF INSPECTOR GENERAL
Washington, D.C. 20250-2316

DATE:

REPLY TO
ATTN OF: 03099-3-HQ

SUBJECT: The Farm Service Agency's Management and Control Over Contracting for the Disposal of Surplus Tobacco

TO: James R. Little
Administrator
Farm Service Agency

ATTN: T. Mike McCann
Director
Operations Review and Analysis Staff

Attached is the final report presenting the results of our review of the Farm Service Agency's control over contracting for the disposal of surplus tobacco. Our review covered the procedures employed in the acquisition planning, solicitation, award, monitoring, and termination of a contract with Biomass Group, LLC. for the disposal of 121,448 tons of surplus tobacco. Although Farm Service Agency (FSA) officials informed us that they relied on the guidance contained in the Federal Acquisition Regulation (FAR), the level of diligence exhibited was not sufficient for us to conclude that FSA adequately applied the FAR guidance to the subject contract to safeguard the interests of the Government. Our review disclosed significant weaknesses in administering the award process for the contract with Biomass with regard to ensuring that the best method of disposal of the tobacco was employed, and in determining that Biomass was a responsible contractor for this procurement.

In accordance with Departmental Regulation 1720-1, please furnish a reply within 60 days describing the corrective actions taken or planned and the timeframes for implementation. Please note that the regulation requires a management decision be reached on all findings and recommendations within 6 months of report issuance.

We appreciate the cooperation and courtesies extended to us during our review.

/s/

ROBERT W. YOUNG
Assistant Inspector General
for Audit

Executive Summary

Review of the Farm Service Agency's Management and Control over Contracting for the Disposal of Surplus Tobacco (Audit Report No. 03099-03-Hq)

Results in Brief

Based on a Congressional request, we performed a review of the Farm Service Agency's (FSA) contracting procedures for the acquisition planning, solicitation, awarding, monitoring, and termination of a contract with Biomass Group, Limited Liability Corporation (LLC) (here-in-after referred to as Biomass) for the disposal of 121,448 tons of surplus tobacco. Our audit disclosed that the level of diligence exhibited was not sufficient for us to conclude that FSA adequately applied the Federal Acquisition Regulation (FAR) guidance to the subject contract to safeguard the interests of the Government.

Our review disclosed significant weaknesses in administering the award process for the contract with Biomass to ensure that the best method of disposal of the tobacco was employed, and that Biomass was a responsible contractor for this procurement. This occurred because FSA had not prescribed or enforced adequate procedures and management controls. As a result, the Government was unnecessarily exposed to potential losses as the contractor was unable to perform in accordance with the terms and conditions of the contract, and other measures had to be taken to complete the disposal of the tobacco.

FSA did not demonstrate that it had performed a competent assessment of Biomass' ability to perform the work required to successfully complete the contract. The Statement of Work associated with the contract required that "Total destruction must be completed no later than 18 months after contract award", and that "Total destruction of the tobacco/cardboard shall only be through burning for energy recovery." In our opinion, this should have required that (1) Biomass had a functioning facility within a sufficient time frame to complete the scope of work, and (2) in order to convert the tobacco to energy, Biomass would have to be able to market the electricity it produced, otherwise there would have been no energy benefit from the process. At the time of the award, Biomass' certification as a competitive retail electric service provider had already expired, and on March 6, 2003, after receiving the award, Biomass allowed the Certification to be cancelled. Therefore, Biomass would have been unable to market any electricity it generated.

Biomass' financial ability to perform under the terms and conditions of the contract had not been determined. FSA was unable to show that Biomass had a satisfactory record of past performance and business integrity and ethics. Biomass submitted a bid that was less than one-fourth the amount of the next lowest bidder determined by the Contracting Officer's Technical

Representative (COTR) to be technically capable, and even though Biomass had no operational bio-mass processing facility, FSA deemed the bid to be reasonable. Further, Biomass did not have the necessary Ohio-EPA permit to legally perform under the contract. FSA ultimately cancelled the contract for "convenience" after the State of Ohio Environmental Protection Agency intervened and issued a determination that Biomass' Installation Permit did not authorize it to store and burn tobacco. Prior to this action, FSA had shipped over 10 thousand tons of tobacco and cardboard containers to Biomass and paid Biomass over $180 thousand. FSA, however, ultimately paid to dispose of the tobacco not shipped to Biomass by burial in landfills. Biomass paid to dispose of the tobacco it had received in the same manner. The final cost of the disposal was nearly $1 million less than the estimated cost of the contract with Biomass.

Recommendations In Brief

We recommended that FSA formally prescribe an effective documented planning process for researching options necessary to meet individual procurement requirements prior to the solicitation of bids. We also recommended that FSA establish formal guidelines and requirements for the conduct of past performance and pre-award reviews. These reviews need to be sufficiently specific to ensure that a prospective contract award recipient demonstrates either satisfactory prior performance of a scope of work similar to the prospective contract, or that it has the legal, technical, and financial capability to timely complete the contract.

We further recommended that FSA establish internal controls, such as review criteria, for contracting officers responsible for determining whether completed pre-award or past performance reviews of prospective contractors have been competently performed, and whether the conclusions and recommendations of the reviewer are adequately supported.

Agency Responses

FSA responded that the selected disposal methodology on this procurement was chosen based on the information ascertained using acceptable, but not necessarily documented, research techniques. FSA further stated that they believe adequate controls are in place using the existing personnel and acquisition regulations. They stated that the FAR and Department of Agriculture Acquisition Regulation provide formal guidance on the conduct of pre-award and past performance reviews, and that formal, detailed, written guidelines can't be implemented to address every unique aspect of the acquisition or other technical processes. FSA contended that any guideline written to address pre-award reviews would be obsolete by the next time one might possibly be required. In this particular acquisition, FSA stated that no formal pre-award survey was required, as sufficient information had been obtained to determine the contractor was responsible.

OIG Position

The results of this contract provide convincing evidence in our view that FSA's planning process was inadequate in its content and application to safeguard USDA's interests. The contract files lacked documentation to support the efforts of the COTR in determining how best to dispose of the tobacco. The files lacked any support for how the determination was made, what analysis was used to ensure that it provided the best value to the government, or even that the untried method of tobacco disposal would be effective.

Actions necessary to accept the agencies' management decisions are provided in the recommendation sections of the report. The agencies' written response is included as Exhibit B.

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Background and Objectives

Background

Section 844 of the Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriation Act (Public Law 106-387, enacted on October 28, 2000) as amended by Section 101 of the Consolidated Appropriations Act (Public Law 106-554, enacted on December 21, 2000) provided that a producer owned cooperative marketing association may fully settle a loan made for the 1999 crop of burley, flue cured, and cigar binder tobaccos by forfeiting to the Commodity Credit Corporation (CCC) the tobacco crop covered by the loan regardless of the condition of the tobacco. The 1999 burley tobacco crop loans were made to the Burley Tobacco Growers Cooperative Association in Lexington, Kentucky, and to the Burley Stabilization Corporation in Knoxville, Tennessee. The 1999 crop of flue-cured tobacco loans were made to the Flue-Cured Stabilization Corporation in Raleigh, North Carolina. The cigar binder tobacco loans were made to the Northern Wisconsin Cooperative Tobacco Pool, Inc. in Viroqua, Wisconsin. CCC called the loans and acquired title to the 1999 tobacco crop effective on May 1, 2001. The Contracting Officer's Technical Representative (COTR), who was a Farm Service Agency (FSA) tobacco division specialist, stated that this was a break from past practice wherein the tobacco associations, rather than CCC, took possession and disposed of the tobacco. The COTR also stated that this was a far larger quantity than had ever been disposed of before. The Office of Inspector General (OIG) was informed that a drought in Kentucky and flooding in several southeastern States had reduced the quality of the tobacco, harming its market value and precipitating the acquisition of the tobacco by CCC through forfeiture in return for settling outstanding loans. A total of 121,448 tons of tobacco was forfeited to CCC. This consisted of 80,802 tons of burley, 40,555 tons of flue-cured, and 91 tons of cigar binder tobacco. Because of the forfeiture program, CCC was forced to store the tobacco until it could be disposed of in a manner in which there was no possibility that it could be recovered and illegally resold in the U. S. market.

On February 5, 2002, the Under Secretary for the Farm and Foreign Agricultural Service approved two options to dispose of the tobacco. The first option was to offer the CCC owned tobacco inventory for sale at U.S. list prices for export use only, as the statute provided that "any tobacco forfeited may not be sold for use in the United States." On April 11, 2002, CCC offered the CCC-owned tobacco inventory for sale, but no bids were received. The second option allowed CCC to destroy the entire CCC-owned 1999 crop of burley, flue-cured, and cigar binder tobacco. The process used by FSA to determine how to dispose of the tobacco was not documented. Although there was no documented requirement that any particular disposal process be selected, FSA decided to destroy the tobacco through burning to produce energy. Through interview, we determined that FSA selected this method by making undocumented phone calls to several types of vendors and, through an

undocumented analysis, determined burning to produce energy to be the best approach. In November 2002, FSA (on CCC's behalf) issued a solicitation to various bio-mass companies to destroy the tobacco by burning for conversion into energy. Seven bio-mass energy companies and one trading company responded to the solicitation. After completing a technical evaluation of all companies, Biomass was selected to receive the contract award based on its low bid of $19.25 per ton of tobacco to be destroyed. The contract was awarded on January 30, 2003. The estimated cost of this contract to the Government was $2,337,874 to Biomass for the destruction of the tobacco plus $2,789,330 in freight cost to deliver the tobacco to Biomass' South Point, Ohio facility, for a total cost of $5,127,204.

From March 11-14, 2003, in response to complaints received from citizens and local governmental officials, the State of Ohio Environmental Protection Agency (Ohio-EPA) conducted an inspection of Biomass' South-Point, Ohio site. Both the contractor and Ohio-EPA officials alerted FSA to Ohio-EPA's concerns about the storage and disposal of tobacco at the Biomass Group facility. At this point, because Biomass had no operational facility, none of the 10,181 tons of tobacco it had received had been destroyed. (We have attached photographs, provided by Ohio-EPA, to this report as Exhibit A. The photographs show piles of tobacco and stacks of unopened cardboard tobacco containers stored in the open at the Biomass site. The photographs, taken on March 12, 2003, July 9, 2003, and July 12, 2004, also show a facility overgrown with weeds that has no apparent construction or renovation activity in progress.) The Ohio–EPA inspector reported that Biomass was in violation of Chapter 3734.03 of the Ohio Revised Code (ORC) and Chapters 3745-27-05(C) and 3745-37-01(A) of the Ohio Administrative Code as Biomass did not have a license or permit for the transfer or disposal of solid waste. [1] FSA suspended shipments of tobacco to Biomass and amended the contract on March 25, 2003 to incorporate a stop work order effective March 14, 2003. The stop work order directed that "The contractor and all subcontractors shall cease performance on all remaining work under this contract and is directed to minimize costs associated with this effort effective immediately. The stop work order will remain in effect until the issue with the Ohio Environmental Protection Agency concerning proceeding as a 'waste to energy' program or a 'solid waste' program is resolved. This action shall remain in place until further notice." On March 27, 2003, Biomass Group, LLC was formally notified by the OHIO-EPA by certified mail that it was in violation of its permit by receiving and storing a solid waste in the form of tobacco and cardboard tobacco containers.

On April 29, 2003, FSA requested the Office of General Counsel (OGC) to conduct a review of a proposed termination for cause for the contract with

[1] ORC Section 3734.03 states: "No person shall dispose of solid wastes by open dumping or open burning." OAC Rule 3745-27-05 states: "No person shall conduct, permit, or allow open dumping." OAC Rule 3745-37-01 states: "No person shall conduct solid waste operation without a valid license."

Biomass. On May 19, 2003, OGC recommended that FSA first issue a cure notice (instructing Biomass as to what it must do to correct current deficiencies in its performance under the FSA contract) to Biomass, and failing effective cure, terminate the contract for cause based on Biomass' failure to comply with the contract's terms and conditions. FSA issued the cure notice to Biomass on May 22, 2003, but then terminated the contract not for cause, as recommended by OGC, but for the convenience of the Government effective June 12, 2003 in accordance with FAR 52.212-4. When asked why the OGC recommendation was not followed, FSA responded that terminating for convenience was the better approach, as the contractor had agreed to dispose of the tobacco it had received at no additional cost to the government, and terminating for convenience would avoid the potential cost and time required to work through contractor appeals which would likely follow a termination for cause.

Termination for convenience, rather than for cause, however, impedes the Government's ability to seek damages for a contractor's nonperformance. FAR 52.212-4 (l) states: "The Government reserves the right to terminate this Contract, or any part hereof for its sole convenience. In the event of such termination, the contractor shall immediately stop all work hereunder and shall immediately cause any and all of its suppliers and subcontractors to cease work. Subject to the terms of this contract, the contractor shall be paid a percentage of the contract price reflecting the percentage of work performed prior to the notice of termination, plus reasonable charges the contractor can demonstrate to the satisfaction of the Government using its standard record keeping system, have resulted from the termination. The Contractor shall not be required to comply with the cost accounting standards for contract cost principles for this purpose. **This paragraph does not give the Government any right to audit the Contractor's records (emphasis added).** The Contractor shall not be paid for any work performed or costs incurred which reasonably could have been avoided."

On May 30, 2003, Ohio-EPA issued its "Director's Final Findings and Orders", which required that all tobacco be removed from the Biomass site within 60 days of the date of the order (July 29, 2003).

Ultimately, the tobacco was disposed of in several landfills under existing servicing agreements between the CCC and several Tobacco Associations. The final cost of disposing of the portion of the tobacco not delivered to Biomass was $3,565,059. If the transportation cost of $384,718 and $181,585 payment to Biomass for the tobacco it received is included, then the total cost of the tobacco disposal equals $4,131,362, or $995,842 less than the anticipated cost of the original award to Biomass.

The COTR reported that, as of December 19, 2003, the entire CCC inventory of tobacco had been crushed and mixed with other wastes (to make it unusable) and buried in landfills.

Objectives

The objectives of our review were to determine whether the award, monitoring, and disposition of the contract with Biomass by FSA were in compliance with applicable laws and regulations, and specifically, that due diligence was performed to protect the Government's interests.

Findings and Recommendations

Section 1. Management Oversight and Control

Finding 1 **FSA's Award Planning and Past Performance Review Methodology Lacked Adequate Management Control and Procedural Guidance**

Selection Process for Tobacco Disposal Methodology Was Not Documented

The method selected by FSA to dispose of the tobacco was not the most economically sound and the research employed in making the selection was not supported by documentary evidence. We attributed this condition to an overall lack of management control to ensure that due diligence was applied in the contracting process for this contract. This lack of control was evidenced by an absence of documentation to support the actions taken and determinations made, and by an absence of detailed written procedures and controls necessary to properly govern this activity. The disposal method selected (burning to produce electricity) was more costly than the alternative ultimately employed (disposal in landfills) and its viability for tobacco had not been established.

Although the need to dispose of such a large quantity of tobacco was a precedent-setting event, (The COTR stated that in his 14 years of experience, CCC had never taken possession nor had to dispose of surplus tobacco.) FSA should have had procedures in place to ensure that it was prepared to address any unique contracting needs that might arise. This apparently was not the case. When FSA was charged with obtaining a vendor to dispose of the tobacco, it had neither the experience nor sufficient documented procedures in place to provide guidance on how to determine the most appropriate way to carry out this new contracting requirement. FSA had no procedures in place to guide its personnel in determining what documentation was needed to support the research and analysis performed, the conclusions reached, and the review and final selection of the most cost effective and efficient methodology to employ to dispose of the surplus tobacco. Internal controls over the methodology of the selection process, such as supervisory or second party reviews, were not in evidence, and as a result, the decision to burn the tobacco to produce energy, which committed Government resources, went unchallenged**.** When we asked in interview as to how the decision was made to dispose of the tobacco by burning to produce electricity, the COTR informed us that he made a few telephone calls (none of which were documented) to inquire about disposal options, and ultimately spoke with an individual (whose name and title could not be recalled) who had experienced success in disposing of soybeans through conversion to energy. Even though the COTR stated that he had no prior experience with the burning–to-produce energy process, and was unaware of it ever being used for tobacco, it was recommended as the disposal method to be employed. We asked if there was

documentation of any analysis performed of alternatives to support the selection of this method, and were told that it was not a formal documented process.

The fact that it cost the Government nearly $1 million less to dispose of the excess tobacco in landfills (after the contract with Biomass was terminated) versus the original decision to burn the tobacco to produce energy points out that better planning was needed for this award. The contract with Biomass Group, LLC, if successfully completed, was projected to cost a total of $5,127,204 ($2,337,874 to Biomass and $2,789,330 for transportation paid by USDA). **The potential negative impact of the inadequate planning for this contract award is punctuated by the fact that had Biomass not bid on the contract, and had it then been awarded to the next lowest technically capable bidder, if funded, that award would have cost USDA $14,168,512. This would have been $10,037,150 more than the $4,131,362 cost ultimately incurred by disposing of the tobacco in landfills.**

We concluded that the seemingly arbitrary manner in which the disposal method was selected did not constitute due diligence. Further, we do not believe that the Contracting Officer, in failing to ensure that a competent documented planning process was employed to determine the best manner to dispose of the surplus tobacco, complied with the spirit of the FAR. Part 1.602-2 of the FAR places responsibility on the Contracting Officers for the 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.

Past Performance/Pre-Award Review Methodology Lacks Sufficient Guidance and Controls

FSA selected a contractor to dispose of the surplus tobacco who was incapable of performing under the terms and conditions of the contract. This was due to the absence of necessary prescribed guidance and supervisory review criteria over the past performance/pre-award review process. As a result, the Government was put at risk. FSA had not prescribed specific minimum procedures to be performed in order to (1) perform a competent past-performance assessment or determine that a pre-award review was necessary, and (2) assess the review results to determine that the contractor was responsible. This resulted in the conduct of an inadequate review, and produced an incorrect determination that Biomass was responsible.

The FAR does not provide specific guidance on when past performance and pre-award reviews are required, or on how they should be conducted, but it does provide minimum requirements in order for a contractor to be deemed responsible. Applicable FAR guidance is quoted below.

FAR 9.103 "Policy." states: "(a) Purchases shall be made from, and contracts shall be awarded to, responsible prospective contractors only. (b) No purchase or award shall be made unless the contracting officer makes an affirmative determination of responsibility. . . (c) The award of a contract to a supplier based on the lowest evaluated price alone can be false economy if there is subsequent default, late deliveries, or other unsatisfactory performance resulting in additional contractual or administrative costs…**A prospective contractor must affirmatively demonstrate its responsibility** (emphasis added) . . ."

FAR 9.104-1 "General Standards." states: "To be determined responsible, a prospective contractor must-

(a) Have adequate financial resources to perform the contract, or the ability to obtain them. . . (See 9.104-3(a).
(b) Be able to comply with the required or proposed delivery or performance schedule. . .
(c) Have a satisfactory performance record. . . A prospective contractor shall not be determined responsible or nonresponsible solely on the basis of a lack of relevant performance history. (FAR 15.305(a)(2)(iv) states: "In the case of an offeror without a record of relevant past performance or for whom information on past performance is not available, the offeror may not be evaluated favorably or unfavorably on past performance).
(d) Have a satisfactory record of integrity and business ethics.
(e) Have the necessary organization, experience, accounting and operations controls, and technical skills, or the ability to obtain them. . . (See 9.104-3(a)).
(f) Have the necessary production, construction, and technical equipment and facilities or the ability to obtain them. . . (See 9.104-3(a)).
(g) Be otherwise qualified and eligible to receive an award under applicable laws and regulations."

FAR 9.104-3 "Application of Standards" states:

(a) Ability to obtain resources. Except to the extent that a prospective contractor has sufficient resources or proposes to perform the contract by subcontracting, the contracting officer share require acceptable evidence of the prospective contractor's ability to obtain required resources. . . Acceptable evidence normally consists of a commitment or explicit arrangement, that will be in existence at the time of the contract award, to rent, purchase, or otherwise acquire the needed facilities, equipment, other resources, or personnel.

FAR 9.105-1 "Obtaining information." states:

(a) "**Before making a determination of responsibility, the contracting officer shall possess or obtain information sufficient to be satisfied that a prospective contractor currently meets the applicable standards in 9.104" (**emphasis added).
(b) "(1) Generally, the contracting officer shall obtain information regarding the responsibility of prospective contractors, including requesting pre-award surveys when necessary (see 9.106), promptly after a bid opening or receipt of offers. (2) Preaward surveys shall be managed and conducted by the surveying activity. (3) Information on financial resources and performance capability shall be obtained or updated on as current a basis as is feasible up to the date of the award."

FAR 9.106-1 states: "A pre-award survey is normally required only when the information on hand or readily available to the contracting officer, including information from commercial sources, is not sufficient to make a determination regarding responsibility."

FAR 15.302 describes the source selection objective – "The objective of source selection is to select the proposal that represents the best value. Similarly, FAR 15.303 establishes source selection responsibilities and notes that:

(a) Agency heads are responsible for source selection. The contracting officer is designated as the source selection authority, unless the agency head appoints another individual . . .
(b) The source selection authority shall (1) Establish an evaluation team, tailored for the particular acquisition, that includes appropriate contracting, legal, logistics, technical, and other expertise to ensure a comprehensive evaluation of offers; (2) Approve the source selection strategy or acquisition plan, if applicable, before solicitation release; (3) Ensure consistency among the solicitation requirement, notices to offerors, proposal preparation instructions, evaluation factors and subfactors, solicitation provisions or contract clauses, and data requirements; (4) Ensure that proposals are evaluated based solely on the factors and subfactors contained in the solicitation. . .; (5) Consider the recommendations of advisory boards or panels (if any); and (6) Select the source or sources whose proposal is the best value to the Government."

Inadequate Review of Proposed Contractor Prior to Award

FSA initially determined that it did not need to conduct a past performance review because it reasoned that the Environmental Protection Agency (EPA) must have done so in order for any of the bidders on this contract to be

considered biomass companies.[2] A memo in the contract file signed by the COTR and the contracting officer on November 26, 2002 states: "As per FAR 15.304 (C) (3) (iv) past performance will not need to be evaluated. (FAR 15.304 (C) (3) (iv) states: "Past performance need not be evaluated if the contracting officer documents the reason past performance is not an appropriate evaluation factor for the acquisition.") This determination is made as Environment [sic] Protection Agency (EPA) must certify Bio-Mass [sic] companies that destroy waste. **Tobacco is considered a solid waste** (emphasis added) that can only be processed for destruction by a bio-Mass [sic] Company. Since the companies capable of this requirement have already been screened for compliance by EPA, this will not be an additional requirement that USDA will address."

We noted that the contract files did not contain any evidence obtained directly from the national EPA, nor did it cite EPA regulations that supported the conclusions that the national EPA's actions were sufficient in lieu of performing a pre-award review. Subsequently, FSA reversed itself on this determination and performed a past performance review and a site visit to Biomass' South Point, Ohio facility, in January 2003 (the contract files did not explain why the reconsideration was made). A later document, "Recommendation for Award, Destruction of Tobacco, Solicitation No. FSA-R-003-04DC, Contract No. 53-3151-3-0004" states "A past performance check was made by the Tobacco and Peanut Division (TPD) [performed by the COTR] on the recommended contractor, Biomass Group, LLC. Biomass Group LLC [sic] has received an Air Permit from the Ohio Environmental Protection Agency. [We noted, however, that the permit, was an installation permit only, and did not authorize the storage and burning of tobacco, as was ultimately determined by Ohio-EPA.] **Bio-mass material can only be processed for destruction by a bio-mass company** (emphasis added)**.** [We noted that in the early stages of the award, FSA used the words solid waste and bio-mass interchangeably to describe the tobacco as evidenced in this document and the document describing the EPA requirements above.] The TPD [COTR] also contacted two other sources familiar with the offeror's performance. [We noted, however, that these individuals were advisors to Biomass, and, lacking an arms length association with Biomass, their statements of assurance did not evidence an appearance of independence]. Based on the information received by the TPD [COTR] and the site survey, the recommended offeror has a satisfactory record of past performance."

The above recommendation for award concluded that the offeror had a satisfactory record of past performance, even though FSA had no documented evidence to show that Biomass or its President had ever successfully operated a bio-mass to energy conversion facility, or could in the future. In our opinion, the conclusion was not adequately supported.

[2] The COTR had stated that biomass companies were selected because a contact (whose name could not be recalled) had indicated that a contract for disposal of soybeans through conversion to energy by a biomass company had been successful.

Criteria for Determining the Capability of Proposed Contractor Were Not Followed

"Factors" included by FSA in the contracting file as necessary support for a determination of technical competence were not followed. An undated memo from the COTR to the Contracting Specialist described the "factors" to be applied in determining the "Capability of vendors to receive the solicitation to provide 100 % total destruction of the 1999 crop (sic.) Government owned tobacco inventory" as the following:

- "The amount of material that can be burned in a day.
- Can they provide the amount of security I need.
- Are their permits in place to burn waste?
- Their capability to destroy tobacco in 18 months."

In OIG's opinion based the requirements of FAR 9.104-1, quoted above, and on FSA's own "factors", the COTR's on-site review at the Biomass facility in South Point, Ohio did not provide the information needed to make a supportable determination that Biomass was a responsible contractor. In interviews with the COTR and Contracting Officer in December 2003 and January 2004, we were informed that the COTR met with the president of Biomass and two of his advisors in January 2003. The COTR provided the Contracting Officer with a memorandum describing his site visit, and concluding that Biomass was responsible to carry out the contract. The FSA Contracting Officer, upon review of the information provided by the COTR, agreed with this determination (In interview, he stated that he relied on the COTRs' expertise with tobacco in making his determination) and recommended that the contract be awarded to Biomass.

The COTR stated that at the time he toured the facility there was no evidence of any construction in progress. He described the site as containing a large building housing seven boilers and several smaller outbuildings. The only activity noted by the COTR was some cleanup of trash and brush. The conclusion of the COTR in a January 10, 2003 memo, nonetheless, states: **"It appears that this company is more than capable of complying with our solicitation."** (emphasis added). The memo did not explain how a contractor that had not even started construction on its conversion of an old non-operational ethanol processing plant to an energy conversion plant for biomass could be assessed on the amount of material that could be burned in a day, or the capability to destroy all of the tobacco within 18 months of the date of the contract award, as is required by the contract's statement of work. Current information and photographs of the Bio-Mass South Point, Ohio facility, obtained from Ohio-EPA officials, shows that Biomass Group has not begun construction of the modifications necessary to become a functioning bio-mass plant as of July 2004. Further, publicly available information,

obtained from the website of the Ohio Public Utilities Commission (Case No. 00-2337-EL-CRS) and confirmed by telephone conversation, shows that Biomass' Certificate as a Competitive Retail Electric Service Provider (Certificate No. 01-046 (1)) expired on January 1, 2003, and has not been renewed to the current date. Thus, even if Biomass had possessed an operational facility on the date of the contract award, January 30, 2003, it would not have had the legal authority to market the electricity it would have generated.

When asked what information lead the COTR to conclude that Biomass would be able to perform under the contract, the COTR replied that he relied upon the character and experience of Biomass' President as supported by statements provided by two of his advisors. The advisors consisted of a member of a Kentucky based financial services organization and a representative of a consulting service specializing in energy production and distribution. The COTR stated that inquiries were not made as to what specific business or personal relationships the two individuals or their firms may have had with Biomass or its President. The COTR stated that the individuals were only referred to as advisors to Biomass. This infers, nonetheless, that some compensated business arrangement might have existed, and if that were the case, would taint the reliability of any support they might have offered regarding Biomass and its president. When asked whether independent verification of Biomass' financial and technical ability to perform had been sought, the COTR replied that except for an inconclusive Dun and Bradstreet (D&B) report, the answer was no. FAR 9.103 provides a "Contractor Qualifications Policy" for Contracting Officers, which states: "(a) Purchases shall be made from and contracts shall be awarded to, responsible prospective contractors only", and "(b) **No purchase or award shall be made unless the contracting officer makes an affirmative determination of responsibility. In the absence of information clearly indicating that the prospective contractor is responsible, the contracting officer shall make a determination of non-responsibility** (emphasis added)." We do not believe that a physical inspection of a nonfunctioning facility and interviews with individuals who may not have been independent of the bidder support the conclusion reached by FSA that Biomass Group was responsible.

Proposed Contractor's Financial Ability to Perform

Biomass' financial ability to perform under the terms and conditions of the contract as required by FAR 9.104-1 were not determined. FAR 9.104-1(a) states: To be determined responsible, a prospective contractor must have adequate financial resources to perform the contract, or the ability to obtain them. FAR 9.104-3(a) "Ability to obtain resources." states: "Except to the extent that a prospective contractor has sufficient resources or proposes to perform the contract by subcontracting, the contracting officer shall require acceptable evidence of the prospective contractor's ability to obtain required resources . . . . Acceptable evidence normally consists of a commitment or

explicit arrangement that will be in existence at the time of contract award to rent, purchase, or otherwise acquire the needed facilities, equipment, or other resources or personnel . . .."

An April 2, 2003 letter from Biomass' attorney to Ohio-EPA stated that Biomass had expended in excess of $13 million in developing the South Point, Ohio plant, and that final construction and development costs were expected to exceed $108 million. With such a substantial sum necessary to renovate the facility to be able to perform under the FSA contract, and having evidenced no construction activity at the site, due diligence and the FAR dictate that in order to determine Biomass' capability to perform, a review of documents such as construction agreements, timetables, and independently supportable evidence of financial ability would be advisable. This was not done, nor were such documents requested per the COTR.

Three sources of information, detailed below, relating to financial capability were addressed in the contract files and in FSA's responses to OIG's questions. However, none of these sources provided competent evidence, in our judgment, individually or in the aggregate, of Biomass' ability to perform.

The COTR stated that in evaluating Biomass' financial standing, FSA obtained a D&B report. We reviewed the copy of the D&B report that was in the contract file. We noted that the report, dated January 17, 2003, stated: "The DS indicator assigned to this business means that the limited information currently in the D&B file does not allow us to classify it within our rating systems. [3] We are providing this information in the interest of speed. Because management may have not been interviewed, this information should not be considered a statement of existing facts. We are currently investigating further, and an updated report will be sent to you shortly." FSA contracting personnel were unable to verify whether they received the noted update to the D&B report, and it was not available in the contract file. Thus, this report did not provide any useful information for assessing Biomass' financial standing. A November 25, 2003 response from the Chief, FSA Audits, Investigations, and State and County Review Branch, to questions submitted by OIG stated that FSA determined that Biomass was not on the "List of Parties Excluded from Federal Procurement and Non-procurement Programs." This check was not documented in the contract files, except by a brief notation that it had been performed and Biomass was not on the list. Further, this check only indicates that Biomass has not been determined as non-responsible on some other Federal procurement. It should not be viewed as a positive affirmation that Biomass is a responsible contractor.

Another FSA response noted: "It was also stated by Biomass that the Biomass group has a net worth of over 100 million dollars." This information, based on statements by Biomass' president per the COTR,

[3] The DS indicator is used to assign a credit worthiness rating to an entity being assessed by D&B.

provided no assurance, in our view, of Biomass' financial condition as it was not supported by any independently reliable source such as audited financial statements, tax records, or confirmations from financial institutions.

We reviewed Biomass' December 1, 2000 Application for Certification as Retail Generation Provider. This was the most recent information we could obtain on Biomass' financial status, and is available on the internet as stated above. In this document we noted that Biomass Group, LLC might consist only of one individual, its president. The COTR and Contracting officer were unable to provide a list of the names of the members of Biomass Group, and the above document, on page No.1, states that **the current President of Biomass purchased the interest of all of the other members on August 9, 2000, and is the sole member** (emphasis added).

The document also states in Section 2.01 "The member [president of Biomass] has contributed $100 to the capital of the Company in exchange for a 100 percent interest in the Company. It further states in Section 2.02 "The Member shall not have any personal liability for the liabilities or obligations of the Company except to the extent of its capital contribution set forth in Section 2.01 and the Member shall not be required to make any additional capital contributions to the Company." Under Exhibit C-6 of the document "Credit Rating" Biomass's president has attested to "None" (emphasis added). Thus, if indeed Biomass had only one member, and that member did not have any requirement to personally ensure that Biomass was adequately funded, it became even more critical to gain assurance that Biomass had sufficient financing to construct the needed facilities to become operational.

We also noted that the document contains an unaudited balance sheet for Biomass as of September 30, 2000. The balance sheet presented Biomass' net worth at that date as $36,475,000. However, $35,000,000 of this amount was listed as the value of the plant and equipment, and $5,000,000 was the value of its power purchase agreement permits. These figures are estimates and it is unknown whether the plant and equipment (last operated as and ethanol processing plant in 1995) could be sold or used as security for financing for the value stated. Additionally, as Biomass had no certification as a competitive retail electric service provider, the $5,000,000 related to this asset is also questionable. Thus, if liquidated, it is possible that Biomass could have no real net worth. As this information is dated and unaudited, Biomass's current financial standing is unknown. However, the above information was, and is currently, available on the internet, and it should have been considered by FSA in making a determination as to the responsibility of this contractor, and should have reinforced the need to adhere to the FAR and obtain reliable information as to Biomass' financial capability.

Biomass' Technical Ability to Perform Was Not Determined

FSA did not demonstrate that they had performed a competent assessment of Biomass' ability to perform the work required to successfully complete the contract. The contract's statement of work required that "Total destruction must be completed no later than 18 months after contract award", and that "Total destruction of the tobacco/cardboard shall only be through burning for energy recovery." In OIG's opinion, this should have required that (1) Biomass had a functioning facility within a sufficient time frame to complete the scope of work, and (2) in order to convert the tobacco to energy, Biomass would have to be able to market the electricity it produced, otherwise there would have been no energy benefit from the process. We already noted above that at the time of the award, Biomass' certification as a competitive retail electric service provider had expired, and on March 6, 2003, after receiving the award, Biomass allowed the certification to be cancelled. Although we cannot estimate how long it would have taken for Biomass to reapply and be recertified, this did not bode well for the success of a company that had just signed a contract to burn tobacco to produce energy. It is inexplicable in our view why a company which signed a contract to produce electricity from burning tobacco in January, the same month it was notified that it's certification had expired, would not have taken immediate action to avoid having its certification cancelled in March. This is particularly curious, in that Biomass had represented in its financial statements that $5,000,000 of its net worth was from the value of its power purchase agreement permits.

Additionally, evaluation "factors" FSA placed within the contract file include "The amount of material that can be burned in a day, and "Their capability to destroy tobacco in 18 months."

FAR 9.104-1"General Standards." states: "To be determined responsible, a prospective contractor must: (b) be able to comply with the required or proposed delivery or performance schedule. . . (e) have the necessary organization, experience, accounting and operations controls, and technical skills, or the ability to obtain them. . . (f) have the necessary production, construction, and technical equipment and facilities or the ability to obtain them. . ."

It is difficult to understand, after ascertaining during the site visit that the plant was not operational and that there was no evidence of construction either planned (from viewing contract documents or plans for construction or construction schedules) or in process, how FSA determined that Biomass would have its plant operating and could complete the burning of the tobacco to produce energy within 18 months of the date of the award.

Other than the verbal assurances provided to the COTR by the president of Biomass, and his technical advisors, FSA has indicated that it relied on the president's past experience in operating a power plant that had employed 50

people since 1997. FSA states that it obtained this assurance from the Dun and Bradstreet Report. We reviewed the report and noted that the report states that its information "SHOULD NOT BE TAKEN AS A STATEMENT OF FACTS," and that the record in the report was created at the request of the Biomass president. Therefore, we do not have any assurance as to its reliability. The report tells us, in the "Public Filings" section, that Biomass Group made a Corporate or Business filing on November 11, 1997. The data in the report also contains a warning "The information in the "Payments" and "Public Filings" and other sections when present, may not relate to this business due to possible changes in ownership, control, or legal status since the data was collected." As the specific source of the data was not known and there was no assurance as to its accuracy, and Dun and Bradstreet had warned that it might not be accurate, in our opinion, it provided no reliable information on Biomass's business history. Further, there was no assurance as to whether (1) the referenced power plant was a biomass to energy conversion plant, (2) it was currently in operation, and (3) was being operated successfully.

Further, OIG obtained information indicating that the referenced power plant may not exist, or if it ever existed, has ceased operations. By referencing the application submitted by Biomass, and it's only member of record at the time, its president, to the Ohio Public Utilities Commission, we note the following statements attested to by the Biomass President. On page No. 1 of the document we note that under Section 1.01, "Formation", it states: "On November 4, 1997, [proper name redacted] [The Biomass president] as Organizer, duly executed and filed Articles of Organization with the Kentucky Secretary of State forming a member managed limited liability company. . ." On page 7 of the application document in Exhibit B-1 Biomass' president attested **"Biomass' Ohio site is the first and only generating facility for the Company. Biomass is not licensed or certificated in any other jurisdiction** (emphasis added)**."** On page 8 of the application document in Exhibit B-2 under "Experience in providing service: Biomass' president attests: **"As a start up operation, Biomass Group, LLC has no experience in either electric generation, nor in electric services sales. Biomass owns the current coal fired generator, which is not operable at this time, and the land and road/potential barge site** (emphasis added)**.** Biomass has contracted with consultants who are addressing the conversion requirements and has begun the environmental permitting process necessary to obtain the required permits to install and permits to operate a biomass fired generation station."

The application document quoted from above, was filed with the State of Ohio on November 29, 2000, and the attestation accompanying the filing by Biomass' president stated in part: "The applicant herein, attests under penalty of false statement that all statements made in the application for certification are true and complete, and that it will amend its application while the application is pending if any substantial changes occur regarding the

information provided in the application." The now cancelled certificate as a competitive retail electric service provider was approved on January 1, 2001 without out amendment of any of the above quoted information.

Telephone calls to the States of Ohio and Kentucky Public Utilities Commissions and their respective Environmental Protection Agencies failed to unearth any record of Biomass having ever operated a power plant or obtaining an Air Permit, other than for the nonfunctional South Point, Ohio facility.

With regard to FAR 9.104-1(e), described above: During the site visit, the COTR met with and obtained references for the president of Biomass from two individuals described as advisors. One individual acted as a financial advisor, and the other was a technical advisor on power plants. In so far as Biomass continues these associations, they could provide technical expertise, however, the COTR obtained no specific information as to precisely what level of assistance they were providing now and what was contemplated in the future.

Based on the above, we conclude that the work performed and documented by the FSA contracting personnel does not meet the requirements of FAR 9.104-1(b), or its own evaluation factors, necessary to determine this contractor responsible.

Satisfactory Past Performance and Business Integrity Records Were Not Determined

FSA was unable to show that Biomass had a satisfactory record of past performance and business integrity and ethics.

FAR 9.104-1(c) states: "To be determined responsible, a prospective contractor must have a satisfactory performance record. . . A prospective contractor shall not be determined responsible or nonresponsible solely on the basis of a lack of relevant performance history. (FAR 15.305(a)(2)(iv) states: "In the case of an offeror without a record of relevant past performance or for whom information on past performance is not available, the offeror may not be evaluated favorably or unfavorably on past performance)."

As discussed above, the check FSA made of the D&B report was inconclusive, and the check of the "List of Parties Excluded from Federal Procurement and Non-procurement Programs" only indicated that Biomass had not been determined as non-responsible on some other Federal procurement. As FSA had no record of any contracting experience with Biomass, and the company's prior experience as a power producer, if any, is questionable, no assurance was available to use past performance as an indicator of Biomass' potential to be a responsible contractor.

FAR 9.104-1(d) states: "To be determined responsible, a prospective contractor must have a satisfactory record of integrity and business ethics. FSA has not provided any significant information useful in determining the status of Biomass' business integrity and ethics. References were provided by two of Biomass' advisors, but as the advisors were working with Biomass, and may have been compensated or had other business inducements that may have impaired their ability to provide completely impartial assessments their opinions do not carry the same level of assurance as would be obtained from individuals independent to Biomass. Therefore, we believe these references provided insufficient assurance upon which to base an assessment of responsibility.

Biomass' Unreasonably Low Bid Was Accepted Without Question

Biomass submitted a bid that was less than one-fourth the amount of the next lowest bidder determined by the COTR to be technically capable, and even though Biomass had no operational bio-mass processing facility, FSA deemed the bid to be reasonable. In a January 15, 2003 technical evaluation, the very low cost of Biomass' bid for disposal of the tobacco, as compared to the next lowest bidder ($19.25 per ton versus $85.00 per ton) was explained by the contracting officer as follows**:** The explanation FSA provided to justify Biomass' low bid states:

"Tobacco is not normally a product to be used as bio-mass waste to burn for energy recovery. The bio-mass energy companies are dealing with a new waste product to convert to energy. Because we are dealing with tobacco as a waste, some of the companies are going to be more conservative. The main reasons for such a price spread are that some of the offerors already have the infrastructure in place to receive and store this tobacco without any additional construction just for this project. Other offerors would have to build unloading ramps, add conveyor belts to deliver the product to the boilers, upgrade their systems to burn this product and hire new personnel. *[OIG Note: Photos of the Biomass South Point, Ohio facility, as well as information from Ohio EPA officials, and the interview discussion with the COTR, confirm that Biomass had no facilities such as these. Tobacco was simply dumped on the ground or stored in buildings, and no personnel other than the president of Biomass and his advisors were observed at the plant.]* Another factor could be profit motivated. Bio-mass energy companies make most of their money from selling the electricity they produce to utility companies. These companies normally have contracts with lumber companies, tree companies and municipalities to dispose of their waste thorough "Waste to Energy" programs. One of the offerors, Biomass Group, LLC deals primarily with lumber and tree companies to dispose of their sawdust from these companies for $8 per ton. Tobacco waste puts out about the same BTU's per pound as wood waste. The high amount of chlorine in tobacco is a problem to these companies. Chlorine is highly corrosive and has to be filtered from the tobacco when it is burned. Sodium Bicarbonate is used

to filter this from the tobacco and is very expensive. After off-setting (sic) the additional cost to destroy this tobacco with their (sic) ['bid offer' was apparently intended] Biomass group would see this as free fuel instead of having to pay $8 per ton. It will provide them with 10% of their fuel for the year."

OIG reviewed this explanation and noted that (1) Biomass had none of the stated facilities and upgrades, in place or under construction, that might allow them to operate within a contract based on a bid of less than one fourth that of the next technically acceptable bidder; (2) No ready labor force was observed, and therefore it was uncertain whether Biomass would have had to procure and train workers; (3) The COTR and Contracting Officer indicated that they had no support for the fuel cost reduction benefits claimed of 10 percent to Biomass. Without this information, we do not believe the explanation provided by the Contracting Officer for the price spread can be relied upon for decision-making, and it should have been questioned by reviewing officials.

Based on the above, we concluded that the technical evaluation not only fails to adequately explain away the substantial difference between the Biomass bid and those of other technically acceptable bidders, but it is also inconsistent with the facts at hand. We saw no evidence in the contract files that this explanation was questioned, or a better explanation offered.

Biomass Lacked Legal Authority to Perform

Biomass did not have the necessary Ohio-EPA permit to legally perform under the contract. One of the criteria listed above for evaluating potential contractors to destroy the tobacco was: "Are their [meaning the contractor's] permits in place to burn waste?" The COTR determined after reviewing Biomass' air permit that they did have the necessary approval to burn the tobacco. This determination was incorrect, and Biomass' lack of the appropriate permit became the reason why a stop work order effective March 14, 2003 was issued by FSA to Biomass on this contract. (This may have been fortunate, as had Biomass been allowed to receive the entire 121,448 tons of tobacco under the contract, and been unable to complete its destruction, USDA would have incurred the cost of transporting the tobacco a second time in order to assure that it was destroyed in an EPA approved manner, and would have had to seek recovery from Biomass of the 50 percent of the contract amount it was to receive upon delivery of the tobacco at its facility.) FSA contracting personnel apparently did not understand (1) The type of waste (solid vs. bio-mass) that tobacco was classified as by Ohio EPA, (2) which EPA (national or State) had authority over the Biomass site, and (3) what authorities and permissions were conveyed by Biomass' Ohio-EPA permit.

In a memo to FSA's Acquisition Management Branch on the subject of the "Past Performance Evaluation and Air Permit to Install and Operate" [undated] the COTR stated: "I have a complete copy of the Air Permit (181 pages) [the permit is actually 220 pages in length] on file from Ohio Environmental Protection Agency [Ohio-EPA] that allows them to convert waste into waste [sic.] [We presume 'energy' was intended]. It really does not mater [sic] what is burned as long as they stay within their emission levels that are released into the air. These emission levels are monitored not only by the company but also by Ohio EPA."

There are several problems with this statement: (1) It is difficult to understand how a non-operational facility can monitor emission levels when there are none; (2) When we asked for access to the EPA permit purported to be on file, we were told that all that was copied and was available was a few pages, and; (3) The Ohio-EPA issued permit limited what may be burned to wood chips and sawdust and is an installation permit, not an operating permit. A February 8, 2002 press release by Ohio EPA stated "This permit allows Biomass to modify seven boilers to burn wood-based fuel to generate electrical power." The permit, issued on February 7, 2002 is a "Final Permit to Install…" The permit, Signed by the Director, Ohio EPA further states: "Issuance of this permit does not constitute expressed or implied approval or agreement that, if constructed or modified in accordance with the plans included in the application, the above described emission unit(s) of environmental pollutants will operate in compliance with applicable State and Federal laws and regulation, and **does not constitute expressed or implied assurance that if constructed or modified in accordance with those plans and specifications the above described emissions unit(s) of pollutants will be granted the necessary permits to operate** (air) or NPDES permits as applicable [emphasis added]."

Part 10 (b) on page 6 of the permit did allow the install permit holder to temporarily operate for a period of up to one year. The operator was required to apply for the operating permit within 30 days after commencing operation. This clause, however, provided for testing the facility, and was accompanied by strict testing requirements that specified how the plant was to be operated, including what fuels may be burned, in what quantities and mixtures (The Permit to Install, No. 07-00493 issued on February 7, 2002, stateed, on page No. 21, **"During the test period, the fuel to be burned is to be 32 percent Mills Pride waste wood and 68 percent sawmill wood waste"** (emphasis added), and on page No. 39 stated: "Operational Restrictions 1. These boilers will burn a mixed wood waste fuel consisting of a mixture of Mill's Pride wood waste and sawmill waste... After the first 12 calendar months of operation, compliance with the annual combined Mill's Pride wood waste fuel use limitation shall be based upon a rolling 12 months summation of the fuel." During the first year of operation, the maximum amount of fuel to be burned was set at 291,998 tons in the mixture described above. There was no allowance for any other fuel source, such as tobacco, in the permit.). Ohio-

EPA officials have stated that, in their opinion, there is no way that someone who has read the permit should be able to construe that the plant is permitted to burn tobacco, and especially not in the quantities required to carry out the tobacco disposal contract. The operating portion of the installation permit is designed strictly to allow the owner of the facility to complete testing and ensure that the newly constructed plant meets design specifications and requirements.

On March 27, 2003, Biomass received formal notification from Ohio-EPA that its permit did not authorize it to store and process tobacco, as Ohio-EPA considered this to be a solid waste. An April 18, 2003 letter to Biomass' attorney, further clarified Ohio-EPA's position by stating that no additional waste materials may be accepted at the South Point location until Biomass applied for and obtained all applicable permits and licenses and the facility had been adequately prepared for operation. On May 30, 2003 Ohio-EPA ordered Biomass to remove and properly dispose of 10,181 tons of illegally stored tobacco at the company's 80-acre site in South Point by July 29, 2003. A November 17, 2003 letter from Ohio-EPA to Biomass confirmed that all waste tobacco had been removed from the Biomass facility for proper disposal at the time of its October 28, 2003 review.

Training

The COTR informed us via interview that he had been trained in performing on-site pre-award reviews (although FSA has stated that they do not consider the Biomass site-visit as part of a pre-award review) at some time in the past, but had never actually conducted one prior to this contract. He stated that he had received classroom training only, and added that in retrospect, there were some things he probably should have considered and done differently. In our opinion, additional training, and possibly the assistance of a technical expert in the waste to energy conversion field would have improved the results of FSA's pre-award review.

The need for additional training for the COTR was also evidenced in the contract file in that we noted that the COTR exceeded his authority by informing the contractor, on January 31, 2003, one day after the contract award to Biomass, that "The tobacco and containers [received by the contractor] will be considered 100% totally destroyed once the tobacco and containers have been run the (sic) tub grinder and mixed in with wood dust. Biomass Group would be paid the full amount of (sic) solicitation based upon tons processed per month." This response by the COTR directly to the contractor would have changed the contract's statement of work and modified the contract. The statement of work requires that payment to the contractor of only 50 percent per ton be made upon on receipt of the tobacco, and that the tobacco must be burned to produce energy before the remaining 50 percent is paid. Such a contract modification is not permitted by the "Assignment of Contracting Officer's Agreement." This was apparently (as evidenced by

documentation in the contract file) not noticed and corrected until April 2, 2003 when Biomass submitted invoices for 100% payment based on the tobacco it had received, as though it had been destroyed. This mistake points out the need for either better training or closer supervision of the COTR by the FSA Contracting Officer.

The lack of effective internal FSA procedures regarding the steps to employ in conducting a review, and the necessary elements of information to be collected in order to meet the general standards expressed in FAR 9.104-1 lead to the above deficiencies in the pre-award review of Biomass.

Recommendation No. 1

Establish an effective acquisition planning process that documents the research applied and analysis used to determine the methodology to be followed to obtain needed goods and/or services in a manner that provides the best value for the Government. Establish controls to ensure that personnel assigned to this task have the necessary knowledge and experience to make appropriate selections.

Agency Response. *(Due to the detailed nature of the agency response, and the need to clearly address each topic therein, we have segmented the agency response and OIG's position by major topic below.)* FSA responded by stating that a documented planning process for acquisition prior to the solicitation of bids or offers is in place and was adhered to in the conduct of the Biomass procurement. An acquisition strategy plan was determined, as evidenced in the contract file. The acquisition plan was completed and approved in accordance with procedures established by the FAR, the AGAR, and FSA procurement policy memorandum (PPM) 94-4.

OIG Position. Based on the results in evidence with regard to this contract, FSA's planning process was inadequate in its content and application to safeguard USDA's interests. The contract files contained no information in support of the efforts of the COTR in determining how best to dispose of the tobacco. The documents relating to this issue contained in the contract file all appear to have been generated after the COTR had formulated his decision to burn the tobacco to produce energy. We found no discussion or documents that present alternate means of disposal, or assess their merits. Further, our interviews with the COTR and Contracting Officer indicate that such notes or documents were not prepared. The acquisition strategy referred to in the response dates from a point in the process wherein the means of destroying the tobacco has already been determined. We were also informed that the decision to burn the tobacco to produce energy was not mandated by CCC, nor influenced by any USDA Bio-Energy Initiative.

FSA's current PPM 95-02 is to "establish thresholds requiring higher level approvals on specific contracting actions." The PPM states: "A careful review of a contract action can ensure: the action is – in the best interests of the government, - (and) reviewed by the highest level of contracting competence and experience available, commensurate with the value/importance of the procurement. . ." FSA needs to ensure that the detailed work leading up to and supporting the decision as to what methodology is to be employed in responding to a procurement need is documented and maintained so that it is available for subsequent review. This is necessary to apply lessons learned and to identify steps in the process that were inadequately performed so that corrective actions can be applied.

Agency Response. FSA responded that technical personnel are tasked with defining their requirements, including determining the most effective methodology, based on their subject matter expertise, market analysis, and the information available to them at the time. Price is not the only factor to be considered in any acquisition and sometimes is not the primary driver of the ultimate purchase decision. The source selection process itself is geared to "best value" which doesn't necessarily mean lowest price. In fact, in order to further other social or economic goals, the Government often considers price as a less important factor. For example, the socio-economic goals for small business specifically allow a price differential to be paid in order to further the use of small and disadvantaged businesses and the purchase of environmentally correct materials, often at a higher than market price, is encouraged and in some instances, required.

OIG Position. In reviewing the contract files, OIG saw no discussion of socio-economic reasons for awarding this contract. In point of fact, FSA's own Procurement Plan for this solicitation states "Award will be made to the Lowest Price technically acceptable."

Under "Evaluation Factors", this document states "Award will be made to the vendor that provides the most advantageous proposal to the Government, lowest price technically acceptable. . . .The total cost of Government transportation of the tobacco to the vendor, along with the unit cost per ton will determine price (sic) that is most advantageous to the Government." The Contracting Officer approved this document on November 26, 2002. No mention was made of socioeconomic issues as having any impact on this valuation. As the source solicitation document noted that only what were described as large businesses responded, the small and disadvantaged business reference did not apply to this contract.

Agency Response. FSA responded that the selected disposal methodology on this procurement was chosen based on the information ascertained using acceptable research techniques, i.e. consultation with experts such as the Environmental Protection Agency (EPA) Headquarters and other agricultural commodity experts. While written documentation of

this research isn't necessarily in evidence, there is also no substantiation leading one to believe that adequate investigation did not in fact occur. As evidenced by individual state (sic) EPAs, there is controversy within the environmental community, among technical experts, as to the proper classification of this "waste." It was therefore, logical to assume EPA Headquarters would be the ultimate experts in this field and their opinion was the driving force behind the selected disposal method. It is unreasonable to expect those outside a technical area to question the expertise and capability of assigned personnel and adequate controls are in place using the existing personnel and acquisition regulations.

OIG Position. OIG's reviews are conducted to meet the standards set by The General Accountability Office (GAO). Government Auditing Standards promulgated by GAO require the gathering of competent evidential support, and non-recorded oral discussions and suppositions of what must have been done do not constitute competent evidential support for FSA's actions. GAO's Standards for Internal Control in the Federal Government require that significant transactions and events be clearly documented, and that all documentation and records be properly managed and maintained in order for agency management to support the rational decision-making processes employed in the utilization of federal funds entrusted to its stewardship. Our review did not disclose any documentation of the research techniques employed on this award, and therefore we can garner no insight as to their acceptability.

We saw no evidence of consultations with EPA prior to the award, other than a document that argues that an undefined EPA certification requirement for Bio-Mass companies that destroy waste vacates the need for past-performance justification. This same document states that tobacco is considered a solid waste, which is in agreement with the Ohio-EPA position. Ohio-EPA officials stated that they have had an EPA approved environmental management plan in effect since the mid-1970s, and that as a fully delegated State, any contact with EPA Headquarters by a USDA agency should have resulted in the agency being informed that the State was responsible for solid waste versus bio-mass determinations. Further, the permit reviewed by the COTR for this contract was issued by Ohio-EPA, not EPA Headquarters; therefore, OIG does not agree that it would be logical for FSA to presume that EPA Headquarters was the driving force behind the selected disposal method.

FSA states: "It is unreasonable to expect those outside a technical area to question the expertise and capability of assigned personnel (sic) and adequate controls are in place using the existing personnel and acquisition regulations." OIG does not accept that the actions of anyone involved in the utilization and expenditure of taxpayer funds is beyond questioning. As auditors, such questions are a routine and necessary part of the conduct of our reviews. We believe the results of this procurement are sufficient to show that, at least in

this case, controls in place at FSA were not adequate to protect the Government's interests.

Recommendation No. 2

Establish formal, written guidelines and requirements for the conduct of past performance and pre-award reviews. The guidelines should ensure that prospective contractors have demonstrated either satisfactory prior performance of the scope of work of a prospective contract, or can demonstrate that they have the legal, technical, and financial capability to timely complete the contract.

Agency Response. FSA responded that the FAR and AGAR provide formal guidance on the conduct of pre-award and past performance reviews. Pre-award reviews are rare and only performed when determined necessary by a Contracting Officer. Formal, detailed, written guidelines can't be implemented to address every unique aspect of the acquisition or other technical processes. That's why the law, regulations, and the FAR are subject to interpretation and allow for the judgment of the technical experts. Any guideline written to address pre-award reviews would be obsolete by the next time one might possibly be required. Also, much of a pre-award review, by its nature, is specific to the company and/or industry involved so any guidance provided would be generic in nature and already covered by the FAR.

OIG Position. The guidance in the FAR and AGAR are broad and general in nature, and thus do not provide the level of guidance needed by the COTR and Contracting Officer in the conduct of the past performance assessment and the site survey. This was demonstrated by the problems encountered in the review of Biomass, as is demonstrated in the Finding above. Formal detailed guidelines may not be able to address every unique aspect of an acquisition or technical process, but the significant aspects of the information needed to properly assess a contractor's responsibility can certainly be addressed for every procurement. In OIG's opinion, the resources required to create such guidance are much less than those that would be expended in sending COTRs out to perform site surveys without adequate guidance, as in this case, where the survey failed to disclose important information that was readily available and could have prevented the awarding of this contract to a contractor who was unable to perform. We disagree that the guidance would be obsolete by the time of the next review; as such guidance should be continually modified to keep it current and relevant.

Agency Response. FSA responded "As stated in the findings, FAR 9.106-1 states that pre-award reviews are only required when information *on hand* or *readily available*, including information from commercial sources, isn't sufficient to determine responsibility. In this particular acquisition, no formal pre-award survey was required, nor performed. The findings

presented clearly show a failure to differentiate between pre-award survey and past-performance."

FSA states that the information on hand and readily available was sufficient to determine responsibility. They maintain that (1) The Dun & Bradstreet report had no adverse information, i.e. debts, late payments, and specifically showed the company's status as a corporation doing business since 1997 with 50 or more employees. (2) The List of Parties Excluded from Federal Procurement and Nonprocurement Programs was reviewed, as stated in the findings and documented in the contract file as a positive affirmation in the award recommendation. (3) Additionally, a site visit was performed by the COTR and positive statements regarding the firm's viability were received from two separate knowledgeable parties, as well as the contractor itself. FAR 9.105-1 specifically states that in making a determination of responsibility the Contracting Officer must consider relevant past performance information, using sources such as, the prospective contractor, suppliers, subcontractors and customers of the prospective contractor.

FSA notes that FAR 9.103 states that an affirmative determination of responsibility is required and that in the absence of information, clearly indicating that the contractor is responsible, then the Contracting Officer must determine the contractor as nonresponsible. They contend that there was no absence of information, and that there was adequate positive information to determine the contractor responsible. They also maintain that the adverse information cited in OIG's audit findings was all obtained after the fact.

OIG Position. We strongly disagree with FSA's conclusion that for this particular acquisition, no formal pre-award survey was required because they had sufficient information on hand to determine that the contractor was responsible. As pointed-out in the Finding above, none of the information FSA had collected and documented was sufficient to provide an affirmative determination that Biomass was responsible. FSA lacked information as to: (1) the contractor's past experience and success in operating a Biomass facility, (2) the contractor's financial ability to complete the construction necessary to operate the proposed Biomass plant, (3) the likelihood that the plant would be operational in time to complete the contract, and (4) Biomass' legal ability to complete the contract.

Additional information was available to show that Biomass was not responsible, but FSA did not attempt to collect this information, and apparently was unaware that it existed. FSA had so little information regarding Biomass Group's ability to successfully complete the contract, that a pre-award review, as described in FAR 9.105-1, should have been performed.

In its response, FSA points to the Dun and Bradstreet report as a basis for concluding that Biomass has apparently been successfully operating a power plant since 1997 with over 50 employees. OIG disagrees with this assessment, as the evidence we assembled and presented in the Finding above, which was publicly available at the time FSA was preparing to award the contract, supports the conclusion that Biomass Group, LLC is comprised of one individual who has never operated a power plant.

FSA also responded that they reviewed The List of Parties Excluded from Federal Procurement and Nonprocurement Programs, and that they view this as a positive affirmation for judging Biomass to be responsible. OIG strongly disagrees, as the fact that Biomass was not excluded from Federal Procurement merely indicates that no Federal entity has had a supported cause for excluding Biomass. This may simply be the result of Biomass having never been awarded a Federal contract, because Biomass' plant had never been in operation since the inception of the company.

FSA also points out in its response that a site visit was performed by the COTR and positive statements regarding the firm's viability were received from two separate knowledgeable parties, as well as the contractor itself. Again, as we discussed at length in this report, the two individuals from whom statements were received regarding the firm and its president were described by the COTR as advisors to Biomass. Statements from such sources must be discounted, as they are not independent of the contractor, and therefore, their responses are likely to engender a bias in favor of the contractor. We also noted that neither statement spoke to Biomass' viability, one commented only on Biomass' president's capability, and the other merely confirmed that an association existed between an energy advisory firm and Biomass.

FSA's response also maintains that all of the adverse information presented in the report's findings is "after the fact information" unavailable to the contracting officials at the time the contract was awarded. We don't accept the admonition that the adverse information cited in the findings was all obtained after the date of the award of the contract. Had FSA acted to conduct a thorough pre-award review, the information disclosed in this report's Findings would have been available. For example, had FSA exercised sufficient due diligence in reviewing the Ohio-EPA Air permit, information showing that the contractor was not authorized to accept or burn tobacco, and was therefore not responsible, was readily obtainable, and should have been acted upon. Similarly, the information quoted in the Finding from the Biomass president's attestation to the Ohio Public Utilities Commission that Biomass had never operated a power plant prior to the Ohio site was also readily available over the internet.

Recommendation No. 3

Establish internal controls, such as review criteria, for contracting officers responsible for determining whether completed pre-award or past performance reviews have been competently performed, and whether the conclusions and recommendations of the reviewer are adequately supported.

Agency Response. FSA responded: "Established FSA policy PPM 95-2 already requires that pre-award reviews of both solicitations and awards be completed. The Contracting Officer, the head of the Special Projects Section, and an established review committee consisting of the head of the Policy and Oversight Section and the Branch head are tasked with review of these actions. As evidenced in the contract file, reviews were completed for both issuance of the solicitation and the award of the resultant contract. The review comments in the contract file address the incorrect statements in the findings concerning the "pre-award review" requirement and it's (sic) subsequent reversal as well as the statements that Biomass's (sic) "unreasonably low bid" was accepted without question."

"The established review policy and procedures in place review all aspects of both solicitations and awards, not just pre-award review or past performance, to ensure compliance with all procurement rules and regulations as well as the soundness of all decisions. Based on the information readily available at the time, in accordance with the FAR, business judgement (sic), and in consideration of the needs of the Agency, the contract was properly reviewed and awarded."

OIG Position. Although PPM 95-2 requires that pre-award review of both solicitations and awards be completed, it does not present adequate criteria to ensure that the reviews are sufficiently detailed and comprehensive to safeguard USDA's funds devoted to contracts. A thorough review, prior to the issuance of the solicitation, should have shown that the most cost effective method to dispose of the tobacco was not selected. Further, a properly conducted review of the past performance of the contractor, combined with an adequate set of criteria for the site-survey and supervisory review by the Contracting Officer, should have found Biomass to be nonresponsible as disclosed in the Finding above.

FSA expressed concern over OIG's Finding that the Biomass Bid was accepted without question. We understand that FSA maintains that the bid was subjected to review. We noted that the Contracting Officer apparently reviewed the COTR's memo of January 10, 2003, containing the explanation of the price spread, as the Contracting Officer prepared a memo to the file, using similar wording, on January 15, 2003. However, we saw no concern expressed in the contract files over the unsupported and illogical nature of the explanation offered as to why Biomass can bid to complete the contract for less than one fourth the cost the other technically acceptable bidders. The Finding above discusses this issue in detail.

FSA states that based on the information available at the time, the contract was properly reviewed and awarded. OIG disagrees, as much of the information available at the time of the award was not considered by FSA in determining whether the method of disposal of the tobacco was in the best interest of the Government and whether the contractor was responsible. The information that OIG collected and discussed in the Finding relating to the responsibility of the contractor was available prior to the date the award was signed. It was either not requested by FSA, or in some cases, such as with the Ohio-EPA permit, the information was reviewed, but not understood. The ultimate inability of the contractor to perform, and the fact that the ultimate disposal of the tobacco in landfills was nearly $1 million less costly that the contract with Biomass, supports our position that FSA's review processes need to be strengthened.

Recommendation No. 4

Ensure that personnel conducting pre-award or past performance reviews have sufficient training and technical expertise to perform the review and render a competent supported determination. Where necessary, engage the services of technical experts to support those staff personnel conducting the review.

Agency Response. FSA responded that controls are established to ensure that personnel assigned have the required technical ability. The assigned personnel met or exceeded all required experience, education, and training requirements of USDA DR 5001.1. FSA stated that both technical and acquisition personnel have the training required by the USDA. The pace of acquisition rarely allows the time for training on specific topical areas when needed, i.e., just-in-time. As stated in the findings, the COTR had received training on pre-award surveys. As previously stated in this response, pre-award surveys are rarely done; the decision to conduct a pre-award survey is made after receipt and evaluation of proposals, immediately before an award. The acquisition process would have to be cancelled due to the unreasonable time frame necessary for receipt of training. Congressional time constraints in this particular acquisition didn't allow for any significant schedule slippage and putting the acquisition process on hold while someone sets up and attends training would be unacceptable.

The services of technical experts are utilized to support staff personnel in many areas. There still has to be a sufficient level of internal expertise to not only determine the adequacy of the expertise being hired but to monitor performance and make the final decision on the adequacy of their work. Also, as is the case with many things, there are often conflicting, and perfectly valid, expert opinions. Environmental issues in particular are an area of significant differing opinions on technical issues. So, while hiring an expert may seem an easy solution, it doesn't resolve the basic problem as one can literally hire an expert to support any position.

OIG Position. DR 5001-1 "Acquisition Workforce Training, Delegation, and Tracking System" is a broad regulation, with a purpose of ensuring that procedures are in place to ensure that USDA's acquisition workforce is provided with training to achieve career level competencies and a path for effective career development. It does not equip contracting personnel with the specific skills needed for this procurement, such as the ability to review a proposed contractor's construction plans and make an assessment as to whether the proposed contractor can achieve time frames for performance of a contract, provide guidance on how to interpret financial statements, read and comprehend EPA Air permits, or adequately respond to unanticipated issues that might arise in the conduct of a site survey. Such knowledge, needed to determine a contractor's responsibility, may require the assistance of hired technical experts or the accompaniment of other more experienced contracting personnel. In this case, although personnel assigned may have taken all of the courses required by the DR 5001-1, their performance demonstrated that additional competency is required; particularly with regard to understanding what information is necessary to render an affirmative judgment that a contractor is responsible, and to identify when a pre-award survey is needed.

FSA maintains that to correct the problems identified above, the acquisition process would have to be cancelled due to the unreasonable time frame necessary for receipt of training. They add that Congressional time constraints in this particular acquisition didn't allow for any significant schedule slippage and putting the acquisition process on hold while someone sets up and attends training would be unacceptable. CCC acquired title to the tobacco on May 1, 2001, yet this contract was not awarded until nearly 21 months later, on January 30, 2003. Therefore, it doesn't appear that time was of the essence in awarding this contract. FSA appears to be taking the position that because of insufficient time and resources, some mistakes in the award of contracts, such as with Biomass, should be expected, and apparently tolerated. OIG does not agree that lack of time and resources presents a reasonable excuse for failing to properly carry out a contracting officer's fiduciary responsibilities. If such conditions exist, they should be brought to agency management's attention so that they may be addressed, rather than placing Government resources at risk and accepting diminished performance as endemic to the contracting process.

We also disagree with FSA's contention that the practice of hiring experts is basically flawed because "one can literally hire an expert to support any position." An expert in biomass plant construction and operation for example could have been hired by FSA to assist the COTR in the Biomass site review to assess key elements, such as the practicality of the site for the construction of the plant or whether Biomass Group had competent effective plans for the construction of the plant, and whether the construction could be accomplished quickly enough to meet the conditions of the contract statement

of work. In so long as Biomass was not paying the expert's fee and had no personal or professional relationships with the expert, the expert's opinion, accompanied by supporting documentation and analysis could be reasonably relied upon in making a decision to award the contract.

We based our conclusion that additional training was needed on the apparent conduct of the pre-award survey, and the resultant determination by the COTR and the Contracting Officer that the contractor was "more than capable" of performing the contract. The errors and omissions that we noted in the conduct of the site review and subsequent review of the site report by the Contracting Officer are detailed in the Finding above. We buttress our position through comments made by the COTR in interview that the individual had received classroom training on pre-award site reviews, but never actually conducted one. We also question the level of training and due diligence evidenced through the Contracting Officer's review of the COTR's site report. The reviewer did not question the lack of key information in the report, or the COTR's unsupported positive affirmation of the ability of the contractor to perform.

Recommendation No. 5

Take appropriate administrative action against the individuals who were responsible for the award and administration of this contract.

Agency Response. FSA responded that if by this statement the OIG is recommending adverse action, we strongly disagree. The OIG has not demonstrated that the actions taken were in violation of any law, regulations or required procedure. Actions taken were timely and done in the best interests of the Government. The actions taken in responding to each adverse event protected the best interest of the Government and demonstrated a professionalism that should be lauded not punished.

OIG Position. We believe that the information contained in this report clearly identifies obvious and egregious errors and omissions in the conduct of this award that placed $5 million in Government funds at unnecessary risk. These mistakes were allowed to occur because actions taken to determine the most appropriate method to use to destroy the tobacco were not documented and therefore, there exists no evidence as to whether management was presented with a supportable analysis of the alternative methods that may be employed and the costs, risks and benefits of each, and because due diligence in the performance of contracting responsibilities as required by FAR 1.606-2 was not applied. The Contracting Officer reached an unsupported conclusion that Biomass Group, LLC. (which now appears to consist of one individual who has no record of operating a biomass facility and has no existing operational facility) was affirmatively responsible to carryout the tobacco destruction contract. By failing to ensure and document that a competent and thorough review was performed prior to making the award of the contract to Biomass Group, and by accepting incomplete and unsubstantiated information

as support of past performance, and current ability to perform, the contracting personnel placed USDA funds in jeopardy and failed to adequately carry out their fiduciary responsibility to the Department. Such inattention to the proper exercise of responsibility merits corrective administrative actions.

Scope and Methodology

The audit was conducted at the FSA Contracting Office in Washington, DC. Our audit consisted of a review of the contracting process undertaken by FSA to accomplish the disposal of surplus FY 1999 tobacco. As such, we examined the actions taken with regard to the research and decision process employed to determine how to dispose of the excess tobacco, the solicitation of bids by potential contractors, technical review of the bid packages received, past performance and on-site review at the Biomass South Point, Ohio facility, to determine whether the proposed contractor was responsible, award of the contract to Biomass, monitoring of Biomass' activities under the contract, contract termination, and the ultimate disposal of 1999 crop year surplus tobacco.

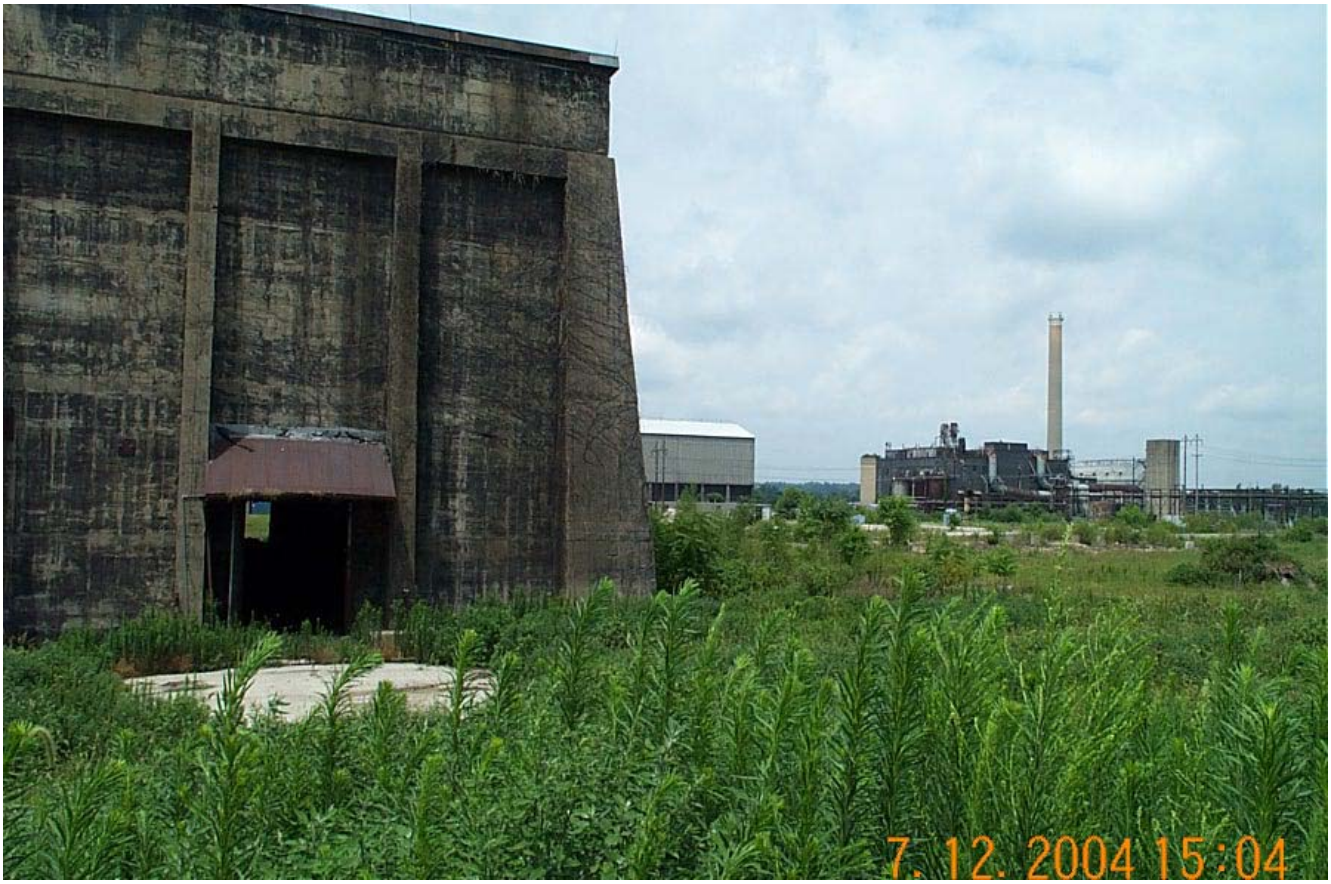
We reviewed activities that took place over the period of May 1, 2001 through December 19, 2003. We interviewed FSA officials, spoke over the telephone and corresponded by e-mail with Biomass' president and officials with the Ohio-EPA and relied on official opinions and decisions issued by Ohio-EPA. We also obtained information by telephone and e-mail from the Kentucky and Ohio State Utilities Commissions, and Kentucky State EPA. We reviewed written documentation including all of the available files on this specific contract in the possession of FSA, documents from the Ohio-EPA, and information from other sources such as financial reporting services and the local South Point, Ohio news services. Our audit fieldwork was initially performed between November 13, 2003 and February 27, 2004; additional audit evidence was compiled between May 13, 2004 and July 21, 2004, subsequent to the exit conference, to address concerns that were raised at that time.

Exhibit A

Photographs of the Biomass Group's South Point, Ohio Facility

The following photographs were provided by the Ohio State Environmental Protection Agency. They show piles of rotting tobacco and cardboard boxes containing tobacco stored in the open at the Biomass Group, LLC South Point, Ohio site. The photographs also show that the plant is not operating and overgrown with weeds, and that no construction activity is in evidence as of July 12, 2004.

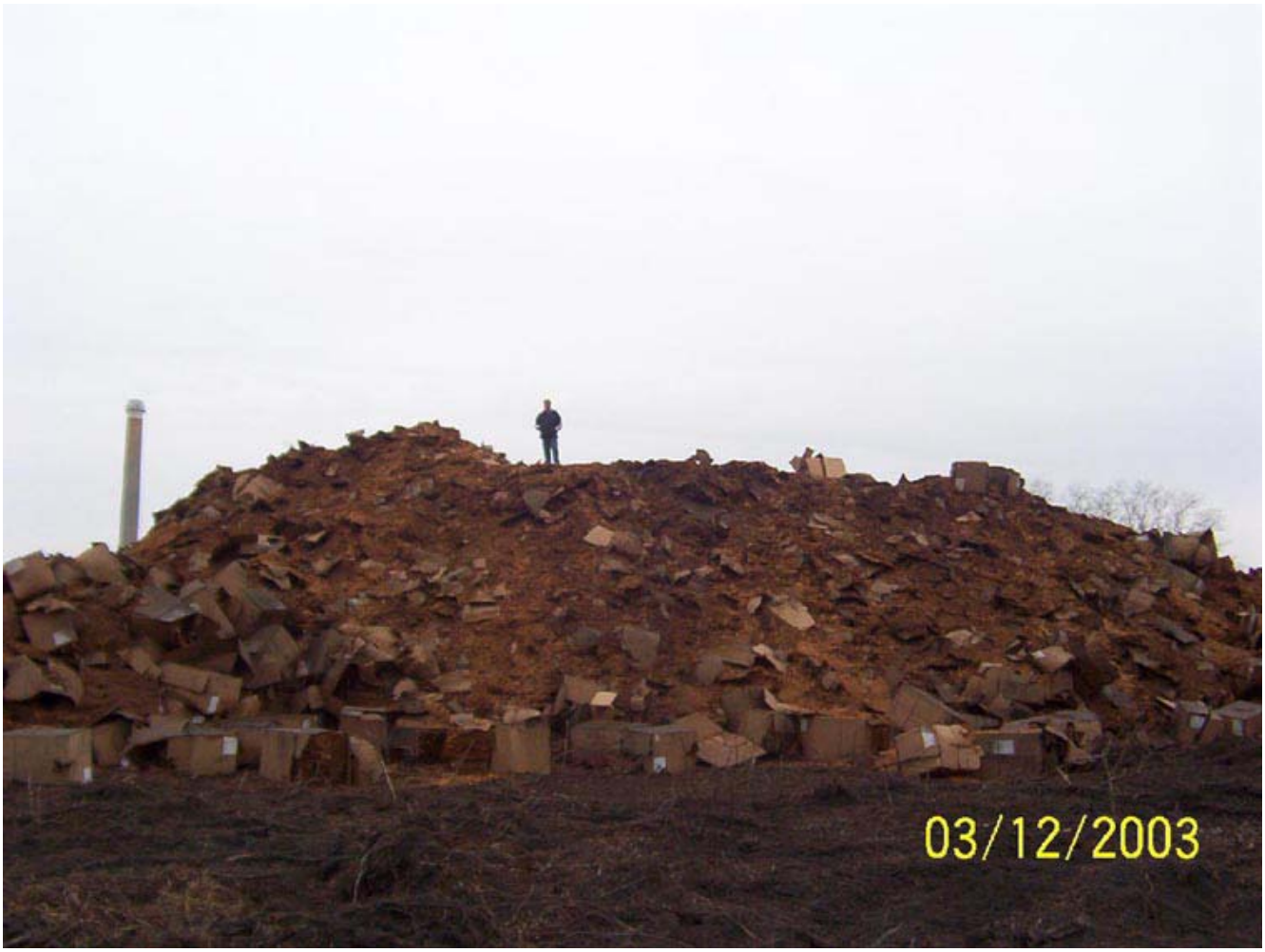
July 12, 2004, photograph of the inoperative boiler at the Biomass South Point, Ohio facility.



July 12, 2004 photograph of the Biomass bunker, overgrown with weeds, where tobacco was once stored, with the boiler plant shown in the prior page in the background. We note that there appears to be no sign of activity and that there was no smoke coming from the boiler stack.

July 9, 2003 photograph of the Biomass bunker site. The brown substance in the background is stored tobacco, with broken cardboard containers to the left of the photograph

March 12, 2003 photograph of the receiving depot at the Biomass South Point, Ohio facility, with cardboard containers of tobacco stored in the open.



March 12, 2003 photograph of a pile of decaying tobacco stored in the open on a fly ash pond at the Biomass South Point, Ohio site. The tobacco was smothering vegetation planted on the fly ash pond as part of an EPA Superfund effort to clean up the contaminated site.

March 12, 2003 close-up photograph of the pile of tobacco stored on the fly ash pond at the Biomass site.

Exhibit B

Response From the Farm Service Agency

USDA

United States Department of Agriculture

Farm and Foreign Agricultural Service

Farm Service Agency

1400 Independence Ave, SW
Stop 0560
Washington, DC
20250-0560

JUL 6 2004

USDA - OIG

TO: Philip Sharp, Chief
Audit, Investigations, and State and County Review Branch

FROM: John W. Williams
Deputy Administrator for
Management

SUBJECT: Response to Draft Audit, "The Farm Service Agency's Management and Control Over Contracting for the Disposal of Surplus Tobacco"

Attached is the Management Services Division/Acquisition Management Branch (AMB) response to the subject audit.

If you have any questions, please contact Raymond Suehr, Branch Chief, AMB at (202) 690-0723.

Attachment

ROUTE TO:	INIT.	ACTION
IG		
DIG		
Ex. Asst.		
ID		
Counsel		
AIG/Audit		
AIG/Inv.		
AIG/PDRM		
AIG/P&SP		
File		

MENTS:

IG-HQ-2004-866

USDA

United States Department of Agriculture

Farm and Foreign Agricultural Services

Farm Service Agency

1400 Independence Ave, SW
Stop 0567
Washington, DC 20250-0567

TO: Robert W. Young
Assistant Inspector General
for Audit

FROM: James R. Little
Administrator

SUBJECT: Response to Draft Audit, "The Farm Service Agency's Management and Control Over Contracting for the Disposal of Surplus Tobacco"

Attached is the Farm Service Agency (FSA), Acquisition Management Branch (AMB) response to the subject audit.

If you have any questions, please contact Raymond Suehr, Branch Chief, AMB at (202) 690-0723.

Attachment

cc: OIG, Rm. 117-W
OA, Rm. 3086-S
Sandra Garland
AMB Reader File
Author

FSA/MSD/AMB/POS/Scott Cook/dll/ext. 720-7349/C:\...\Blue Jacket Documents\
Response to Draft Audit (BJ 009, 04)/AMB-04-009
Revised by Ray Suehr/FSA/MSD/AMB/dll/ext. 690-0723/06-24-04/AMB-04-009
Revised by Thomas Hofeller/OA/dll/ext. 690-0153/06-30-04/AMB-04-009

Reviewer	Typist	Writer	Branch Chief	Director	DAM
Date/Initials	6/30/04 dl	6/30/04	6/30/04		

The Farm Service Agency's Management and Control Over Contracting for the Disposal of Surplus Tobacco

The following are our responses to the findings and recommendations contained in the draft audit, "Review of Farm Service Agency's Management and Control over Contracting for the Disposal of Surplus Tobacco," OIG reference number 03099-3-HQ. It is our understanding that our responses to the recommendations (in Part II below) will be included in the final audit report.

PART I FINDINGS AND OUR RESPONSES

A. Selected Method of Tobacco Disposal Was Not Supported

First, it should be made clear that the choice of a method to dispose of the tobacco was not a contracting office function. The program office decides what product or service they wish to procure, and the Contracting Officer (CO) procures it. As long as the statement of work is in compliance with the requirements of the Federal Acquisition Regulation, and the requisition has funding, the CO's responsibility is to buy the item or service. Allowing the CO to second-guess technical decisions with no technical expertise or knowledge of the genesis of the requirement would be inappropriate.

The decision to burn this particular batch of tobacco was not in violation of any federal, departmental or agency regulations, and arguably was in compliance with the current Departmental initiative to "think green." While merely dumping the tobacco in a landfill would have been the cheapest approach, many contracts are made on the basis of their social value rather than their economic merit. By law we are required to award some contracts at a price higher than the simplest technical approach may call for.

B. Pre-Award Review Methodology Lacks Procedural Guidance and Controls

This acquisition was performed in accordance with the FAR, the Agriculture Acquisition Regulation (AGAR), Procurement Policy Memorandum (PPM) 94-4 (Procurement Planning), PPM 95-02 (Presolicitation and Precontract Review) and was signed off twice by the chief of the Acquisition Management Branch and the head of the Policy and Oversight Section. The CO complied with all regulations, laws and guidance in writing, negotiating and award of this contract.

The IG's primary issue seems to be with regard to the determination by the CO that Biomass had the technical wherewithal and financial capacity to perform this contract.

The facts are these: Biomass possessed a biomass-burning facility, and this facility, while not yet fully operational, was licensed by the Ohio EPA to operate for one year pending further licensing. (The statement in the audit that Biomass was not permitted to operate is incorrect.) Biomass was a company with no prior federal experience to evaluate; however, the FAR does not condone the downgrading or elimination of a firm

that is starting up. One of the purposes of the FAR is to ensure that companies like Biomass are *not* discriminated against in award evaluations. We obtained references on the principal officer of the firm. We obtained a Dun and Bradstreet (D&B) report, which did not note any reasons to deny award to Biomass. There is only so much analysis that can be performed on a new contractor.

A decision was made by the project office to visit the site. This is not a FAR requirement, but it was an indication of the extra steps made by FSA to ensure a good contract. The COTR, a tobacco expert with years of experience in this field and with all the required training for his COTR duties, determined that Biomass had the proper equipment and financial capacity to perform this contract.

The ultimate failure of this contract was not due to incapacity or false assertions made by Biomass, but rather the odd decision by the Ohio EPA subsequent to the award that tobacco was not a biomass product, but rather a waste product. This decision, outside of the control of either Biomass or the United States Department of Agriculture (USDA), made the contract unperformable at the price quoted, since Biomass planned on selling the generated electricity to offset the costs of the burning.

PART II RECOMMENDATIONS AND OUR RESPONSES

Recommendation 1: Formally prescribe a documented planning process to be established and implemented prior to the solicitation of bids. Establish controls to ensure that personnel assigned have the technical ability to make recommendations for the scope of services to be obtained such that the desired outcome is performed in a manner that is most cost efficient and effective.

Response: A documented planning process for acquisition prior to the solicitation of bids or offers is in place and was adhered to in the conduct of the Biomass procurement. An acquisition strategy plan was determined, as evidenced in the contract file. The acquisition plan was completed and approved in accordance with procedures established by the FAR, the Agriculture Acquisition Regulation (AGAR), and Farm Service Agency (FSA) procurement policy memorandum (PPM) 94-4.

Controls are established to ensure that personnel assigned have the required technical ability. In addition to the technical requirements of established position descriptions detailing technical expertise requirements, on-the-job training, the existing performance management system and annual appraisals, technical personnel receive specific Contracting Officer Technical Representative (COTR) training in accordance with USDA Departmental Regulation DR5001-1. Contracting personnel are mandated to meet specific education, experience, and training requirements by USDA DR5001-1 and additionally have a biennial continuing education requirement. The assigned personnel met or exceeded all required experience, education, and training requirements of USDA DR5001-1.

Technical personnel are tasked with defining their requirements, including determining the most effective methodology, based on their subject matter expertise, market analysis, and the information available to them at the time. Price is not the only factor to be considered in any acquisition and sometimes is not the primary driver of the ultimate purchase decision. The source selection process itself is geared to "best value" which doesn't necessarily mean lowest price. In fact, in order to further other social or economic goals, the Government often considers price as a less important factor. For example, the socio-economic goals for small business specifically allow a price differential to be paid in order to further the use of small and disadvantaged businesses and the purchase of environmentally correct materials, often at a higher than market price, is encouraged and in some instances, required.

The selected disposal methodology on this procurement was chosen based on the information ascertained using acceptable research techniques, i.e. consultation with experts such as the Environmental Protection Agency (EPA) Headquarters and other agricultural commodity experts. While written documentation of this research isn't necessarily in evidence, there is also no substantiation leading one to believe that adequate investigation did not in fact occur. As evidenced by individual state EPAs, there is controversy within the environmental community, among technical experts, as to the proper classification of this "waste." It was therefore logical to assume that EPA Headquarters would be the ultimate experts in this field and their opinion was the driving force behind the selected disposal method. It is unreasonable to expect those outside a technical area to question the expertise and capability of assigned personnel and adequate controls are in place using the existing personnel and acquisition regulations.

Recommendation 2: Establish formal, written guidelines and requirements over the conduct of pre-award and past performance reviews. The guidelines should ensure that prospective contractors have demonstrated either satisfactory prior performance of the scope of work of a prospective contract, or can demonstrate that they have the technical and financial capability necessary to make any physical plant changes required to complete the contract.

Response: The FAR and AGAR provide formal guidance on the conduct of pre-award and past performance reviews. Pre-award reviews are rare and only performed when determined necessary by a Contracting Officer. Formal, detailed, written guidelines can't logically be implemented to address every unique aspect of the acquisition or other technical processes. That's why the law, regulations, and the FAR are subject to interpretation and allow for the judgment of the technical experts. Any guideline written to address pre-award reviews would be obsolete by the next time one might possibly be required. Also, much of a pre-award review, by its nature, is specific to the company and/or industry involved so any guidance provided would be generic in nature and already covered by the FAR.

As stated in the findings, FAR 9.106-1 states that pre-award reviews are only required when information *on hand* or *readily available*, including information from commercial sources, isn't sufficient to determine responsibility. In this particular acquisition, no

formal pre-award survey was required, nor performed. The findings presented clearly show a failure to differentiate between pre-award survey and past performance.

The information on hand and readily available was sufficient to determine responsibility. The Dun & Bradstreet report had no adverse information, i.e. debts, late payments, and specifically showed the company's status as a corporation doing business since 1997 with 50 or more employees. The List of Parties Excluded from Federal Procurement and Nonprocurement Programs was reviewed, as stated in the findings and documented in the contract file as a positive affirmation in the award recommendation. Additionally, a site visit was performed by the COTR and positive statements regarding the firm's viability were received from two separate knowledgeable parties as well as the contractor itself. FAR 9.105-1 specifically states that in making a determination of responsibility the Contracting Officer must consider relevant past performance information, using sources such as, the prospective contractor, suppliers, subcontractors and customers of the prospective contractor. As stated in the findings, FAR 9.103 states that an affirmative determination of responsibility is required and that in the absence of information clearly indicating that the contractor is responsible, then the Contracting Officer must determine the contractor as nonresponsible. There was no absence of information; there was adequate positive information to determine the contractor responsible. The adverse information cited in the findings was all obtained after the fact (reference 2 Apr 03 letter from Biomass to Ohio EPA as quoted in the findings; received after award which was made on 30 Jan 03).

The audit itself states, on page 5 and per the FAR, that Contracting Officers request and consider the advice of specialists, e.g. technical personnel. As evidenced in the contract award memorandum, and the findings, the Contracting Officer stated that the technical expert's advice was relied on in making the positive responsibility determination. FAR 9.103 specifically states that the contractor and other sources, such as suppliers, subcontractors, and customers, are sources of information for determining responsibility. As stated in the findings, that too was documented in the file by letters from two separate firms doing business with the contractor. It is procedurally correct to accept a contractor's statements as fact unless and until proven otherwise. For example, contractors self-certify their status as a small business, that they comply with applicable laws, etc. and these statements aren't questioned unless a Contracting Officer has reason to believe otherwise.

Recommendation 3: Establish internal controls, such as review criteria, for contracting officers responsible for determining whether completed pre-award or past performance reviews have been competently performed, and whether the conclusions and recommendations of the reviewer are adequately supported.

Response: Established FSA policy PPM 95-2 already requires that pre-award reviews of both solicitations and awards be completed. The Contracting Officer, the head of the Special Projects Section, and an established review committee consisting of the head of the Policy and Oversight Section and the Branch Head are tasked with review of these actions. As evidenced in the contract file, reviews were completed for both issuance of

the solicitation and award of the resultant contract. The review comments in the contract file address the incorrect statements in the findings concerning the "pre-award review" requirement and it's subsequent reversal as well as the statements that Biomass's "unreasonably low bid" was accepted without question.

The established review policy and procedures in place review all aspects of both solicitations and awards, not just pre-award review or past performance, to ensure compliance with all procurement rules and regulations as well as the soundness of all decisions. Based on the information readily available at the time, in accordance with the FAR, business judgement, and in consideration of the needs of the Agency, the contract was properly reviewed and awarded.

Recommendation 4: Ensure that personnel conducting pre-award or past performance reviews have sufficient training and technical expertise to perform the review and render a competent supported determination. Where necessary, engage the services of technical experts to support those staff personnel conducting the review.

Response: As stated previously, both technical and acquisition personnel have the training required by the USDA. The pace of acquisition rarely allows the time for training on specific topical areas when needed, i.e. just-in-time. As stated in the findings, the COTR had received training on pre-award surveys. As previously stated in this response, pre-award surveys are rarely done; the decision to conduct a pre-award survey is made after receipt and evaluation of proposals, immediately before an award. The acquisition process would have to be cancelled due to the unreasonable time frame necessary for receipt of training. Congressional time constraints in this particular acquisition didn't allow for any significant schedule slippage and putting the acquisition process on hold while someone sets up and attends training would have been unacceptable.

The services of technical experts are utilized to support staff personnel in many areas. There still has to be a sufficient level of internal expertise to not only determine the adequacy of the expertise being hired but to monitor performance and make the final decision on the adequacy of their work. Also, as is the case with many things, there are often conflicting, and perfectly valid, expert opinions. Environmental issues in particular are an area of significant differing opinions on technical issues. So, while hiring an expert may seem an easy solution, it doesn't resolve the basic problem as one can literally hire an expert to support any position.

Recommendation 5: Take appropriate administrative action with regard to the individuals responsible for the award and administration of this contract.

Response: If by this statement the OIG is recommending adverse action, we strongly disagree. The OIG has not demonstrated that the actions taken were in violation of any law, regulations or required procedure. Actions taken were timely and done in the best interests of the Government. The actions taken in responding to each adverse event

protected the best interest of the Government and demonstrated a professionalism that should be lauded not punished.