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SEP 24 2010

MEMORANDUM FOR UNDER SECRETARY OF THE NAVY
UNDER SECRETARY OF THE ARMY
UNDER SECRETARY OF THE AIR FORCE
DIRECTORS OF THE DEFENSE AGENCIES

SUBJECT: Interagency Contracting Problems Continue at DOD Organizations

The Department needs your assistance to improve interagency acquisitions and provide better value to the warfighter. Our audits have shown that significant improvement in interagency contracting procedures have not occurred since we began auditing the subject six years ago. We believe a fundamental reason for repeat deficiencies is that the DOD users who request goods and services through interagency contracts are not performing adequate requirement determinations and funding determinations before the acquisition, and contract oversight is not performed after the contract is awarded.

The DOD Office of Inspector General (IG) issued 16 audit reports addressing DOD purchases made through non-DOD agencies from FY 2004 through FY 2009. Overall, we visited seven non-DOD agencies that purchased goods and services on behalf of DOD. From FY 2004 through FY 2009, the agencies made about 98,750 purchases, valued at approximately \$15.6 billion, for DOD organizations. We reviewed 869 of these purchases valued at approximately \$1.9 billion. We visited 35 Air Force sites, 26 Army sites, 25 Navy sites, 14 Defense agencies, and 12 other DOD sites. We also visited the non-DOD contracting agencies that awarded contracts on behalf of DOD.

Most of the 869 purchases reviewed contained problems in the areas of acquisition planning, funding, and contract administration (attachment).

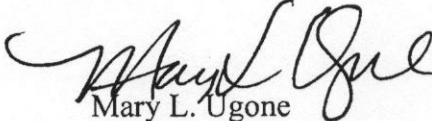
- Improvements are still needed in acquisition planning for non-DOD purchases. Specifically, DOD organizations did not meet requirements for best interest determinations, Military Interdepartmental Purchase Requests preparation, DOD contracting officer review for purchases of more than \$500,000, independent Government cost estimates (cost estimates), and interagency agreements.
- Improvements are still needed in using proper funds which, as we identified numerous potential Antideficiency Act violations. For example, 608 of 869 purchases had potential Antideficiency Act violations. DOD organizations generally replaced expired or incorrect funds with the proper funds and eliminated the violations. However, controls to prevent funding violations are needed because investigating and then correcting funding violations are labor intensive and lengthy business endeavors.
- Improvements are still needed in contract administration, such as designating contracting officer's representatives (CORs), performing contract surveillance, reviewing invoices, and documenting past performance. Non-DOD agencies did not consistently assign

CORs to monitor contracts. DOD officials should serve as the COR when accepting work, signing invoices, and performing contract surveillance.

Non-DOD agencies, the DOD acquisition community, and the DOD financial community have addressed key acquisition and funding problems as a result of prior audits. However, the requirements generator and program officials are not fulfilling their appropriate responsibilities in acquisition planning and contract administration, particularly on requirements determination and oversight as part of interagency agreements to determine whether DOD funds are properly spent and administered.

The DOD requesting officials have responsibilities from initial acquisition planning through contract administration. DOD issued policy to funding and contracting officials for interagency contracting. We believe that your offices need to issue guidance and provide training to reduce the continuing omissions of requirements details in acquisition planning for interagency purchases and the lack of appropriate contract administration of those purchases. Your assistance is needed to reduce the problematic interagency acquisitions and ensure the prudent expenditure of scarce funds.

Please direct questions to the Assistant Inspector General for Acquisition and Contract Management, Mr. Richard Jolliffe, at (703) 604-9201 (DSN 664-9201).


Mary L. Ugone
Deputy Inspector General
for Auditing

cc: Under Secretary of Defense for Acquisition, Technology, and Logistics
Under Secretary of Defense (Comptroller)/Chief Financial Officer

Attachment:
As stated

Attachment: Interagency Contracting Problems

Background

Over the last 6 years, the National Defense Authorization Act required the DOD Office of Inspector General (IG) to perform 16 audits of interagency acquisitions. (See list of DOD IG audit reports on pages 7 and 8.) Overall, we visited seven non-DOD agencies that purchased goods and services on behalf of DOD that included the Department of Energy, the Department of the Interior, the Department of the Treasury, the General Services Administration, the National Aeronautics and Space Administration, the National Institutes of Health, and the U.S. Department of Veterans Affairs.

We visited 112 DOD organizations, some multiple times. See the table for the DOD organizations and number of sites we visited.

Table. DOD Organizations and Number of Sites DOD IG Visited

DOD Organization	Number of Sites Visited
Air Force	35
Army	26
Navy	25
Defense Agencies	14
Other	12
Total	112

Most of the 869 purchases reviewed contained problems. For example, in our first interagency report, No. D-2005-096, "DoD Purchases Made Through the General Services Administration," July 29, 2005, we stated that for 91 percent of purchases, DOD organizations lacked acquisition planning. Most recently, DOD IG Draft Report, "More DOD Oversight Needed for Purchases Made Through the Department of Energy," August 9, 2010, reports that for 93 percent of purchases, DOD organizations lacked documented market research, which is part of acquisition planning.

However, non-DOD agencies, the DOD acquisition community, and the DOD financial community have addressed key violations of the Federal Acquisition Regulation (FAR) and the financial management regulation. The Under Secretary of Defense (Comptroller)/Chief Financial Officer issued DOD Regulation 7000.14-R, "DOD Financial Management Regulation," (DOD FMR) volume 11A, chapter 18, "Non-Economy Act Orders." The Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics (OUSD [AT&L]) issued multiple memoranda that address interagency acquisitions and Defense Federal Acquisition Regulation Supplement changes. OUSD also emphasized interagency contracting at numerous conferences. Finally, DOD enhanced the training of its acquisition personnel.

Issues Needing Attention

Our audit reports continue to identify issues in the acquisition planning, funding, and contract administration of purchases made for goods and services.

Acquisition Planning. We reported inadequate acquisition planning of non-DOD purchases. Specifically, DOD organizations did not meet requirements for best interest determinations, Military Interdepartmental Purchase Requests preparation, DOD contracting officer review for purchases of more than \$500,000, independent Government cost estimates (cost estimates), and interagency agreements.

DOD organizations either developed an inadequate assessment or did not develop an assessment to support a best interest determination in selecting the non-DOD agency to fulfill the DOD mission requirement. The October 29, 2004, Office of the Secretary of Defense memorandum, "Proper use of Non-DoD Contracts," requires a best interest determination to support a particular non-DOD agency to fulfill the DOD need. Further, the requesting official is to provide evidence of market research and demonstrate the cost-effectiveness of the procurement method used. However, 421 of 522 purchases¹ did not have evidence of adequate acquisition planning. For example, DOD IG Report No. D-2008-050, "FY 2006 DOD Purchases Made Through the Department of Treasury," states that all 29 task orders reviewed lacked documentation that DOD performed market research. DOD officials confirmed that they did not seek acquisition alternatives because of concerns with the DOD contracting offices' ability to timely fill orders within the fiscal year of the funds. Because DOD organizations' best interest determinations were insufficient, it is not certain that using a non-DOD agency to assist in meeting mission requirements was truly in DOD's best interest.

DOD organizations did not include clear, precise, and specific information on Military Interdepartmental Purchase Requests, which are used to transfer funds from DOD to a non-DOD agency. Section 1501, title 31, United States Code, "Documentary Evidence Requirement for Government Obligations," requires a binding agreement between two agencies in writing that will report the specific goods to be delivered or services provided. As a result of these audits, on January 18, 2008, the OUSD (AT&L) issued a memorandum, "Interagency Acquisition," that stated that program managers and requirement officials must ensure that statements of work and requirements are clearly, precisely, and completely specific to the item or service being procured. However, 679 of 996 Military Interdepartmental Purchase Requests or purchases² had incomplete supporting documents. Specifically, DOD organizations issued Military Interdepartmental Purchase Requests that lacked a detailed description of the goods and services, did not specify the period of performance for purchased services and/or delivery requirements for goods. For example, DOD IG Draft Report, "More DOD Oversight Needed for Purchases Made Through the Department of Energy," states that for a \$3.2 million proposal, DOD organization funding documents lacked specificity or the period of performance. Without the

¹The purchases will not add up to 869 for the categories discussed in this memorandum because guidance was continuously updated and issued. Also, we conducted the audits differently and did not always review the same categories.

²DOD organizations sometimes sent multiple Military Interdepartmental Purchase Requests to non-DOD agencies for a purchase.

required elements on a Military Interdepartmental Purchase Requests, DOD increases risk of funding problems and establishing an improper interagency contract order.

DOD requirement officials must ensure that a DOD contracting officer conducts a review of purchases exceeding \$500,000, as required by DOD FMR volume 11A, chapter 18, "Non-Economy Act Orders." Before changing the DOD FMR, on October 16, 2006, the Under Secretary of Defense (Comptroller)/Chief Financial Officer issued a memorandum, "Non-Economy Act Orders," with this requirement. A DOD contracting officer review will help to ensure that the order will comply with statute, policy, regulation, and local component requirements and procedures. However, DOD organizations did not always coordinate with a DOD contracting office for a review or ensure that the planned purchase met all applicable DOD requirements. The latest report, DOD IG Draft Report, "FY 2008 and 2009 DOD Purchases Made through the General Services Administration," states that 33 of 50 purchases reviewed lacked an adequate contracting officer review. DOD organizations' omission of contracting officer reviews may have resulted in DOD not obtaining the best value for acquired supplies and services. Unless the DOD requiring officials seek to obtain contracting officer reviews, DOD contracting officers will likely not know the requirement for goods or services exists.

DOD organizations developed insufficient cost estimates. Officials use the cost estimates to budget for requirements and ensure that reasonable prices are obtained. However, in many cases, cost estimates lacked the basis for the estimate, did not identify the source activity, or lacked a date to determine whether the cost estimate was developed and relevant prior to award. For example, 117 of 139 purchases reviewed lacked the proper support. DOD organizations prepared the cost estimates with no basis or explanation of how the DOD organization developed the estimate. For example, DOD IG Report No. D-2008-066, "FY 2006 and FY 2007 DoD Purchases Made Through the Department of the Interior," March 19, 2008, states that a Southwest Acquisition Branch contracting officer relied on a cost estimate that was not signed or dated, and it did not show how the estimated information was developed for a \$8.9 million purchase. DOD needs complete cost estimates to accurately budget for goods and services and to mitigate the risk of incurring higher charges and paying more than market value.

Non-DOD agencies awarded contracts and task orders on DOD's behalf with incomplete interagency agreements. On June 6, 2008, the Office of Federal Procurement Policy issued a memorandum, "Improving the Management and Use of Interagency Acquisitions," that requires that interagency agreements address delineation of roles and responsibilities for purchases to ensure that clear lines of responsibility exist between the requesting (DOD) and servicing agency. However, 277 of 342 purchases contained inadequate interagency agreements. Many interagency agreements did not cite the statutory authority and the period of performance. Contract or task order awards should occur with an agreed-upon interagency agreement between the DOD organization and the non-DOD agency to ensure that each knows their roles and responsibilities for areas such as acquisition planning and contract administration. For example, a Navy Warfare Development Command official stated that he relied on General Services Administration officials for the acquisition planning because they always completed the acquisition plan. However, guidance requires that both the requesting and serving agency perform acquisition planning. A properly prepared interagency agreement would clearly

delegate this responsibility to both. Inadequate interagency agreements can negatively impact the execution of the interagency acquisition. This responsibility generally rests with the requiring agency.

Funding. We reported that DOD organizations used either the wrong type of funds or expired funds for purchases, which lead to numerous potential Antideficiency Act violations. For example, 608 of 869 purchases had potential Antideficiency Act violations. DOD organizations generally replaced expired or incorrect funds with the proper funds and eliminated the violations. This area improved with updated financial guidance, new interagency agreement requirements, and increased attention to funds by the financial community as well as by the non-DOD agencies making the purchases. However, preventing funding violations is important because investigating and then correcting potential funding violations is an extremely ineffective business practice.

Contract Administration. We reported deficiencies in contract administration, which consists of contracting officer's representative (COR) designations, surveillance, invoice review, and past performance documentation. The October 31, 2008, OUSD (AT&L) memorandum, "Meeting Department of Defense Requirements Through Interagency Acquisition," requires that interagency agreements clearly define the roles and responsibilities of the requiring and assisting agencies for contract administration.

Non-DOD agencies did not consistently assign CORs to monitor contracts. DOD officials should serve as the COR when accepting work, signing invoices, and performing contract surveillance. DOD officials should nominate a properly trained DOD program official and ensure the non-DOD agency designate that person as the COR for monitoring contractor performance. The Defense Federal Acquisition Regulation Supplement Subpart 201.6, "Contracting Authority and Responsibilities," requires that contracting officers designate a properly trained COR in writing prior to contract performance to assist in technical monitoring or administration of a service contract. However, 161 of 383 purchases did not have designated DOD CORs. DOD IG Report No. D-2009-064, "FY 2007 DoD Purchases Made Through the National Institutes of Health," March 24, 2009, states that a contract with a potential value of \$63.7 million did not have a properly designated COR. The COR had only 4 hours of training and no prior experience with performing the necessary duties. The COR stated that he did not actively monitor the contractor's performance and had other duties that occupied a significant amount of time. On March 29, 2010, the Under Secretary of Defense for Acquisition, Technology, and Logistics issued a memorandum, "DOD Standard for Certification of Contracting Officer's Representatives (CORs) for Service Acquisitions," to establish COR competencies and training. If adhered to, this guidance should improve compliance. Without a designated DOD-trained COR, increased risk exists for poor performance monitoring, increased cost, and not fulfilling the provisions of interagency contract orders.

DOD and non-DOD agency officials did not ensure surveillance efforts were well defined, adequate, and implemented when used in conjunction with a contract or task order. Non-DOD agency officials awarded task orders either without surveillance plans or inadequate surveillance plans. DOD FMR, volume 11A, chapter 18, states that requesting officials must establish quality

surveillance plans for non-Economy Act orders and ensure execution that would facilitate the oversight of the goods provided or services performed by the non-DOD agency. Further, FAR Part 46.4 "Government Contract Quality Assurance," states that surveillance plans should be prepared in conjunction with the statement of work. However, 323 of 395 purchases had no surveillance plan or an inadequate surveillance plan. For example, DOD IG Report No. D-2009-043, "FY 2007 DoD Purchases Made Through the U.S. Department of Veterans Affairs," January 21, 2009, states that on September 24, 2007, a Veterans Affairs contracting office awarded a contract for the purchase of a sterilizing unit, with a delivery date of October 31, 2007. The contracting office sent the vendor a letter stating the vendor submitted an improper invoice because it did not include a proof of delivery. The contracting office requested proof of delivery. Neither the DOD customer nor the vendor ever provided proof of delivery. The review of receiving reports should be included in the surveillance plan. Additionally, with DOD use of Veterans Affairs, surveillance problems were worse during the follow-up audit. Also, there was no surveillance plan for the \$63.7 million DOD purchase through the National Institutes of Health. Effective surveillance is necessary to provide assurance that goods or services purchased conform to contract requirements.

DOD and non-DOD agency officials did not ensure that invoices were adequate or that the COR had the responsibility to review them. Non-DOD agencies paid invoices that were insufficient and did not include detailed costs, as required by FAR 32.905, "Payment Documentation and Process." FAR 32.905 states that invoices should include the description, quantity, unit price, and extended price of the supplies or services. Invoices did not match the cost proposal, and labor categories were not consistently applied from proposal to award. The interagency agreement and surveillance plan should include monitoring responsibilities assigned to a DOD COR and the method for monitoring to ensure that billing charges receive adequate review and are properly accepted. For example, during two recently completed audits, we found that for 21 of 50 invoices reviewed, costs were applied to incorrect labor categories, an error that would likely have been caught with a proper review process in place. We also found charged labor categories that were not included in the proposal or contract modifications. Inadequate invoice review and acceptance can result in acceptance of inadequate goods and services and improper payments.

DOD organizations did not collect past performance information, and non-DOD agencies did not record past performance information when contracts met thresholds specified by FAR and DOD regulations. Past performance information contains contractor performance data to be used for future source selections. The June 6, 2008, Office of Federal Procurement Policy memorandum addresses past performance. The requesting agency (DOD) must track, measure, and report the contractor's performance to the servicing agency. However, 150 of 182 purchases reviewed contained inadequate past performance information. For example, Report No. D-2009-043 states that the 79th Medical Support Group, Deputy Flight Commander, issued a justification for non renewal of a contract. The contractor's on-site supervisor lacked the skills to effectively inspect and identify deficiencies and maintain the daily workload. Further, violations of fire and safety codes existed. However, the requesting agency did not collect or record past performance information on the purchase. Therefore, the poor performance was not available for

consideration in future source selections. A lack of accurate and complete past performance reporting may negatively impact the source selection process.

Actions Taken

DOD has implemented and updated existing policies to improve the interagency acquisition process. These actions started with the October 29, 2004, Office of the Secretary of Defense guidance, which addresses the proper use of non-DOD contracts. The guidance states that requirement officials have primary responsibility to ensure compliance for interagency acquisitions. Success will depend on a team approach with support from the financial management and contracting communities.

Our audits resulted in policy changes to improve the interagency acquisition processes for funding and contracting. The October 16, 2006, Under Secretary of Defense (Comptroller)/Chief Financial Officer memorandum resulted in the addition of DOD FMR volume 11A, chapter 18, which required a best interest determination, contracting officer review, fund certification, and bona fide need for non-Economy Act orders. On June 6, 2008, the Office of Federal Procurement Policy issued extensive policy on interagency agreements, which addresses the requesting and servicing agency's responsibilities for acquisition planning, contract execution, and contract administration. DOD endorsed the interagency agreements policy issued by the Office of Federal Procurement Policy.

Further, OUSD (AT&L) has issued many memoranda on interagency agreements. The January 18, 2008, OUSD (AT&L) memorandum states that program managers and requirement officials should be actively involved in the interagency acquisition process. The program managers and requesting officials have shared responsibility for ensuring that best value is obtained on purchases for supplies and services. On September 20, 2005, OUSD (AT&L) issued a memorandum, "Interagency Acquisition: A Shared Responsibility," that states that teamwork and communication are critical to the success of interagency acquisitions. The Defense Procurement and Acquisition Policy (DPAP) Web site (http://www.acq.osd.mil/dpap/cpic/cp/interagency_acquisition.html) contains a comprehensive listing of guidance.

Additionally, OUSD (AT&L) and the various non-DOD agencies signed memoranda of agreement to take action and address the problems identified. The agencies include the Department of the Interior, the General Service Administration, the National Aeronautics and Space Administration, and the National Institutes of Health.

DOD IG Audit Reports

Draft Report, "FY 2008 and 2009 DOD Purchases Made Through the General Services Administration," (Project No. D2009-D000CF-0259.000)

Draft Report, "More DOD Oversight Needed for Purchases Made Through the Department of Energy," (Project No. D2009-D000CF-0069.000)

Report No. D-2009-064, "FY 2007 DoD Purchases Made Through the National Institutes of Health," March 24, 2009

Report No. D-2009-043, "FY 2007 DoD Purchases Made Through the U.S. Department of Veterans Affairs," January 21, 2009

Report No. D-2008-122, "Follow-up on DoD Purchases Made Through the Department of the Interior," August 18, 2008.

Report No. D-2008-082, "Summary Report on Potential Antideficiency Act Violations Resulting From DoD Purchases Made Through Non-DoD Agencies (FY 2004 Through FY 2007)," April 25, 2008

Report No. D-2008-066, "FY 2006 and FY 2007 DoD Purchases Made Through the Department of the Interior," March 19, 2008

Report No. D-2008-050, "FY 2006 DoD Purchases Made Through the Department of the Treasury," February 11, 2008

Report No. D-2008-036, "FY 2006 DoD Purchases Made Through the U.S. Department of Veterans Affairs," December 20, 2007

Report No. D-2008-022, "FY 2006 DoD Purchases Made Through the National Institutes of Health," November 15, 2007

Report No. D-2007-044, "FY 2005 DoD Purchases Made Through the Department of the Interior," January 16, 2007

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

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

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

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

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