



Audit Report



OIG-07-026

ACQUISITIONS: Treasury Franchise Fund Needs to Improve Compliance with Department of Defense Procurement Requirements

January 16, 2007

Office of
Inspector General

Department of the Treasury

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Abbreviations

ARC	Administrative Resource Center
BPA	Blanket Purchase Agreement
COTR	Contracting Officer's Technical Representative
DCFO	Deputy Chief Financial Officer
DFARS	Defense Federal Acquisition Regulations Supplement
DoD	Department of Defense
FAR	Federal Acquisition Regulation
GAO	Government Accountability Office

MIPR	Military Interdepartmental Procurement Request
NDAA	National Defense Authorization Act
O&M	Operations and Maintenance
OIG	Office of Inspector General
OMB	Office of Management and Budget
RTD&E	Research, Development, Test, and Evaluation
Treasury	Department of the Treasury
U.S.C.	United States Code
WHS	Washington Headquarters Service

*The Department of the Treasury
Office of Inspector General*

January 16, 2007

Richard Holcomb
Acting Chief Financial Officer

This report presents the results of an audit we conducted separately, but in coordination with the Department of Defense (DoD) Office of Inspector General (OIG), of DoD procurements made through the Department of the Treasury (Treasury) franchise fund. Our audit was required by the National Defense Authorization Act (NDAA) for Fiscal Year 2006.¹ During fiscal year 2005, FedSource, a component of the Treasury franchise fund and the principal focus of our audit, issued approximately 19,700 contract actions consisting of task orders and modifications on behalf of DoD valued at \$405.1 million.

We initiated our audit in August 2005, shortly after the Government Accountability Office (GAO) issued a report that was critical of FedSource contracting assistance to DoD.² In brief, GAO reported that FedSource (1) generally did not ensure competition for work, (2) did not conduct and document price analyses, (3) sometimes paid contractors higher prices for services than were justified, and (4) relied on administrative personnel who were not trained as contracting officers to ensure that potential contractors had opportunities to submit offers.

Our objective was to determine whether Treasury's procurement policies, procedures, and internal controls applicable to the

¹ The National Defense Authorization Act for Fiscal Year 2006, 119 Stat. 3136, Pub. L. No. 109-163, was enacted January 6, 2006. Section 811 of the act mandates the audit of Treasury by our office and DoD OIG. Similar audits are also mandated for the Department of the Interior and the National Aeronautics and Space Administration and are to be performed by the DoD OIG and the OIGs of those agencies.

² GAO, *Interagency Contracting: Franchise Funds Provide Convenience, but Value to DOD Is Not Demonstrated*, GAO-05-456 (Washington, D.C.: July 29, 2005). The GAO report also examined DoD's use of GovWorks, a franchise fund run by the Department of the Interior. Together, FedSource and GovWorks accounted for approximately 95 percent of services provided by franchise funds to DoD in fiscal year 2003 (the fiscal year on which the GAO report is based).

procurement of property products and services on behalf of DoD, and the manner in which they are administered, were adequate to ensure Treasury's compliance with the laws and regulations that apply to procurements of property and services made on behalf of DoD. To accomplish this objective, we reviewed a sample of 64 task orders at three FedSource centers — Los Angeles, CA; St. Louis, MO; and Baltimore, MD. We also reviewed contracts and blanket purchase agreements at the Administrative Resource Center (ARC), another component of the Treasury franchise fund, located at the Bureau of the Public Debt in Parkersburg, West Virginia. Our objective, scope, and methodology are described in more detail in appendix 1.

Pursuant to the fiscal year 2006 NDAA, the DoD OIG and our office informed the Senate and House Committees on Armed Forces in letters dated March 15, 2006, that we had determined that Treasury was not compliant with DoD procurement requirements, but had a program or initiative in place to significantly improve compliance with DoD procurement requirements.³ Copies of our letters, which also summarized our work and determination, were provided to your staff. Copies of this report will be provided to the Committees on Armed Forces.

Results in Brief

We found that FedSource issued policies and procedures that are responsive, if implemented as described, to address GAO's recommendations. For example, FedSource (1) established policy in July 2005 pertaining to ethical conduct and proper use of contract vehicles; (2) established an acquisition performance measurement program in August 2005 to measure, evaluate, and improve management practices in the delivery of contract administration services to FedSource customers; (3) established a standard checklist in July 2005 for documenting task order files; (4) revised its customer request form for services, with detailed instructions

³ The Fiscal Year 2006 NDAA required that the DoD and Treasury Inspectors General reach one of the following determinations by March 15, 2006 (1) Treasury is compliant with DoD procurement requirements; (2) Treasury is not compliant with DoD procurement requirements, but has a program or initiative to significantly improve compliance with DoD procurement requirements; or (3) neither of these conclusions is correct.

for completing statements of work and quality assurance surveillance plans; and (5) established procedures in September 2005 for using incremental funding of acquisitions. These policies and procedures are discussed in more detail later in this report.

Our review of 64 task orders, which were awarded before the above actions were taken, found conditions that were consistent with GAO's findings. Specifically, we found the following:

- FedSource did not adequately compete all task orders. The contracting officers did not provide fair opportunity for competition for task orders issued against multiple-award contracts and issued awards based on customer preferred services. The task orders also lacked complete documentation required by federal procurement regulations and FedSource policies and procedures. For example, we noted that 31 files did not have independent government cost estimates; 18 files did not have proposals, offers, or quotes evidencing competition; and 32 files lacked price negotiation documentation. We also noted that 1 task order was incrementally (partially) funded, but lacked the required clause limiting the government's payment for and the contractor's provision of services to the amount that was funded.
- Twenty-one task orders lacked a quality assurance surveillance plan, 2 had identical quality assurance plans although the scopes of the task orders differed from one another, and 4 had plans that were inadequate. Quality assurance surveillance plans are required by procurement regulations and specify all work requiring surveillance and the method of surveillance. Additionally, Contracting Officer's Technical Representative (COTR)⁴ designation letters were not consistent with quality assurance surveillance plan instructions for who was responsible for performing quality assurance surveillance. Quality assurance surveillance is necessary to determine that supplies or services received conform to contract requirements. The files lacked evidence that FedSource personnel performed inspections of the contractors' work or had otherwise obtained

⁴ COTRs are responsible for technical monitoring of contract performance. Unlike contracting officers, they are not authorized to contractually bind the government or issue instructions or directions that would change the scope or price of contracted work.

assurance that the contractors performed in accordance with the contract requirements. We were told by FedSource personnel that DoD was responsible for determining if property or services were provided in accordance with the task orders. Although these expectations were spelled out in those quality assurance plans that were documented, the task order files do not provide evidence of monitoring being performed.

For DoD procurements made through 21 FedSource task orders, DoD OIG identified instances where incorrect DoD appropriations were used and where the bona fide need rule was potentially violated. As such, these deficiencies represent potential violations of the Antideficiency Act. While the DoD OIG's findings were principally directed at DoD, they point to a need for FedSource to identify the due diligence it performs when accepting orders to help prevent the use of incorrect appropriations. Our discussions with FedSource management indicated that FedSource also recognizes this need. We also noted that FedSource's three servicing centers had inconsistent procedures for reviewing Military Interdepartmental Procurement Requests (MIPR) and interagency agreements before acceptance. Also, as FedSource management has pointed out, guidance for conducting due diligence is not defined. Accordingly, FedSource should work with DoD in establishing a common set of indicators that it should use to determine which procurement requests require more intense FedSource scrutiny. Furthermore, in accordance with a recent DoD directive, FedSource will need to ensure that the task orders for severable services (services that are continuing and recurring in nature) have periods of performance that do not exceed 1 year from the date of MIPR acceptance.

Consistent with our determination that Treasury was not compliant with DoD procurement requirements but had a program to significantly improve compliance, the fiscal year 2006 NDAA requires that DoD OIG and our office to conduct a second concurrent review of Treasury's fiscal year 2006 procurement of property and services on behalf of DoD. The purpose of this second review is to make another determination, by June 15, 2007, as to whether Treasury is or is not compliant with DoD procurement requirements. A determination of noncompliance by this second review has significant implications for the Treasury franchise fund.

Specifically, DoD would be prohibited from procuring property or services through Treasury in excess of \$100,000 unless (1) authorized by the Under Secretary of Defense for Acquisition, Technology, and Logistics or (2) a subsequent joint review by DoD OIG and our office finds that Treasury is compliant with DoD procurement requirements.

The provision in the fiscal year 2006 NDAA for a second review by DoD OIG and our office underscores the need for FedSource management to ensure that the policies and procedures established in response to the July 2005 GAO report are effectively institutionalized in a timely manner. We are making five recommendations in this report to further ensure that FedSource is procuring property and services on behalf of DoD in compliance with DoD procurement requirements. The recommendations are directed toward ensuring that (1) there is appropriate competition for supplies and services acquired on behalf of DoD and prices paid are reasonable, (2) the task order contract files document compliance with procurement requirements, (3) quality assurance surveillance plans are adequate and implemented and COTR designation letters clearly delineate lines of responsibility for who performs monitoring and how monitoring is to be documented, (4) uniform procedures are developed that outline the steps of a reasonable review (due diligence) to be performed before accepting DoD orders, and (5) task orders for severable services are for periods of performance that do not exceed 1 year from the date of MIPR acceptance.

Management Response and OIG Comment

In the response to our draft report, the Deputy Chief Financial Officer (DCFO) concurred with our recommendations for findings 1 and 2 and partially concurred with our recommendations for finding 3. The corrective actions stated by management, if implemented as described, are generally responsive to the intent of our recommendations. The partial concurrences relate to the certain procurements cited as potential violations of the Antideficiency Act and the extent of due diligence necessary on the part of FedSource. These matters, and our evaluation, are discussed in the Findings and Recommendations section of this report.

The DCFO also expressed concern that the timing of our follow-up review does not allow FedSource or DoD sufficient time to fully institutionalize the improvements and changes recommended and currently underway (i.e., draft report was issued September 14, 2006, with the follow up review focusing on the time period of July through September 2006).

With respect to the DCFO's concern with the timing of our follow-up review, it should be noted that both scope and timing of this review and the follow-up are mandated by the fiscal year 2006 NDAA. Furthermore, the corrective actions taken in response to the recommendations contained in the GAO July 2005 FedSource Report, which very much mirror the recommendations in this report, were established before fiscal year 2006.

The text of the management response is included as appendix 4.

Other Matter

Subsequent to our field work, the Department's Office of General Counsel informed the Department of an instance of possible Antideficiency Act violation related to transactions and activities of the Treasury Franchise Fund. Specifically, contracting and budgetary control weaknesses existing with the Fund may have allowed a potential violation of both the Competition in Contracting Act and the Antideficiency Act for a contract whose ceiling was exceeded without proper competition. This matter was also reported by the Independent Public Accountant in its audit report on the Department's fiscal years 2006 and 2005 financial statements.⁵

Background

Franchise Funds

The Government Management Reform Act of 1994 authorized the Office of Management and Budget (OMB) to establish franchise

⁵ *Audit of the Department of the Treasury's Fiscal Years 2006 and 2005 Financial Statements* (OIG-07-010; issued November 15, 2006). The Independent Public Accountant's audit of these statements was performed under the supervision of the Treasury Office of Inspector General.

fund pilot programs at six executive agencies. Franchise funds are government-run, self-supporting, businesslike enterprises managed by federal employees. The funds provide a variety of common administrative services, such as payroll processing, information technology support, employee assistance programs, and contracting. Franchise funds are required to recover their full cost of doing business and are allowed to retain up to 4 percent of their annual income. To cover their costs, the funds charge fees for the services they provide.

Congress authorized the pilot programs because it expected that franchise funds would be able to provide common administrative services more efficiently than each federal agency on its own. In 1996 and 1997, OMB established franchise fund pilot programs at the Departments of Commerce, Health and Human Services, the Interior, the Treasury, Veterans Affairs, and the Environmental Protection Agency. The programs were to expire in 1999, 5 years after passage of the Government Management Reform Act. The Consolidated Appropriations Act, 2005, amended the past legislation giving the Treasury franchise fund permanent status.

Treasury Franchise Fund Entities Used by DoD

The Treasury franchise fund comprises the following entities: (1) FedSource, (2) ARC, (3) Federal Consulting Group, and (4) Treasury Agency Services. Procurement services to DoD are provided through FedSource and ARC.

The acquisition process for the Treasury franchise fund originates at ARC. ARC performs contract competitions and establishes master contract vehicles from which FedSource issues task orders to meet customer needs. In addition, ARC appoints FedSource's contracting officers, designates COTRs, and conducts compliance reviews to determine whether Treasury franchise fund procurement activities are being carried out in accordance with applicable laws and regulations. FedSource serves as liaison between customers and contractors, develops comprehensive acquisition strategies, works with customers to develop statements of work, competes and awards task orders, develops and participates in quality assurance surveillance plans, and closes out completed task orders.

One type of master contract vehicle awarded by ARC is the “multiple award” contract. A multiple award contract is made with two or more sources under a solicitation who agree to provide the same or similar supplies and services at fixed prices during a fixed period. Such contracts obligate the government to purchase a minimum quantity from each contractor. The government places orders under these contracts for individual requirements.

FedSource’s Process

DoD sends FedSource either a MIPR or an Interagency Agreement as funding documents to procure property or services. These documents should describe the type of property or services requested and identify the appropriation account of the funds being provided. Upon receipt, FedSource reviews the funding documents, and if accepted, issues task orders against master contracts for the requested property or services. Funding documents may fund more than one task order; similarly, multiple funding documents may fund multiple task orders.

Key Laws and Regulations

Procurement activities conducted by federal franchise funds are subject to the same laws and regulations to which other federal government procurement activities are subject, as well as to any additional regulations specific to the funding agency. Three of the principal legal authorities that govern the procurement activities of this review the Federal Acquisition Regulation (FAR), the Defense Federal Acquisition Regulations Supplement (DFARS), and the Antideficiency Act.

The FAR is the primary regulation for use by all federal executive agencies in their acquisition of supplies and services with appropriated funds. It became effective on April 1, 1984, and is issued within applicable laws under the joint authorities of the Administrator of General Services, the Secretary of Defense, and the Administrator for the National Aeronautics and Space Administration, under the broad policy guidelines of the Administrator, Office of Federal Procurement Policy, Office of Management and Budget.

According to the FAR, contracting officers, as a matter of policy and with certain limited exceptions, must promote and provide full and open competition in soliciting offers and awarding government contracts. Contracting officers are to do this through the use of the competitive procedures. As prescribed in the FAR, contracting officers are to purchase supplies and services from responsible sources at fair and reasonable prices. The determination of price reasonableness should be documented in the contract file.

DoD implements and supplements the FAR in the DFARS under the authorization and subject to the authority, direction, and control of the Secretary of Defense. DFARS requires, with certain exceptions, that each procurement for DoD exceeding \$100,000 under a multiple award contract be made on a competitive basis. When using the term “competitive basis” in regard to multiple award contracts, the contracting officer must provide fair notice to all contractors offering the required supplies or services, and ensure that the contractors are afforded a fair opportunity to submit an offer and have that offer fairly considered.⁶

Similarly, the FAR directs contracting officers to provide all contractors under multiple award contracts fair opportunity to be considered for orders exceeding \$2,500 under multiple delivery or multiple task order contracts. This subpart also requires contracting officers to document in the contract file the rationale for placement and price of each order.

The Antideficiency Act prohibits federal government officials from making payments or committing the United States to make future payments for goods or services unless Congress has appropriated sufficient funds to pay for those goods or services. Among other things, the law prohibits the federal government from using funds for other than their intended purpose or making or authorizing expenditure from, or creating or authorizing an obligation under,

⁶ This DFARS provision implements Section 803 of the NDAA for Fiscal Year 2002, enacted as Pub. L. 107-107 on December 28, 2001. As stated in DFARS, exceptions to the fair opportunity process apply when (1) only one contractor is capable of providing the supplies or services required at the level of quality required because the supplies or services are unique or highly specialized or (2) the order must be issued on a sole source basis in the interest of economy and efficiency because it is a logical follow-on to an order already under the contract, provided that all awardees were given a fair opportunity to be considered for the original order.

any appropriation or fund in excess of the amount available in the appropriation or fund unless authorized by law.⁷

GAO Analysis of DoD Use of FedSource

In July 2005, GAO issued a report on DoD's use of franchise funds.⁸ Overall, GAO found that FedSource generally did not ensure competition for work, relied on personnel who were not trained as contracting officers, did not conduct and document price analyses, and sometimes paid contractors higher prices than were justified.

To address these findings, GAO recommended that the Secretary of the Treasury (1) develop procedures and performance measures for franchise fund operations to demonstrate compliance with federal procurement regulations and policies while maintaining focus on customer service, (2) develop procedures for franchise fund contracting officers to work closely with DoD customers to define contract outcomes and effective oversight methods, and (3) assign warranted contracting officers to positions responsible for performing contracting officer functions. Treasury concurred with these recommendations.

FedSource Actions to Address GAO Recommendations

From July to September 2005, FedSource established policies and procedures that, if properly implemented, would be responsive to GAO's recommendations.

- In July 2005, FedSource established policy pertaining to acquisition of goods and services that provided, among other things, that (1) all FedSource personnel are to adhere to the highest standards of ethics in executing contract solicitation, awards, and administration responsibilities; (2) all contracts and blanket purchase agreements (BPAs) are to be used only for their intended purpose; (3) only FedSource personnel are authorized to serve as COTRs on FedSource contracts, BPAs, and other contract vehicles (unless approved by the FedSource

⁷ 31 U.S.C. § 1341(a)(1)(A).

⁸ GAO, *Interagency Contracting: Franchise Funds Provide Convenience, But Value to DOD Is Not Demonstrated*, GAO-05-456 (Washington, D.C.: July 29, 2005).

Vice President of Acquisition); (4) all FedSource centers implement use of warranted contracting officers; and (5) all FedSource personnel are to promote the use of performance-based contracts.

- In July 2005, FedSource established a standard checklist for documentation required to be retained in task order files.
- In August 2005, FedSource established an acquisition performance measurement program as a tool to measure, evaluate, and improve management practices in the delivery of contract administration services to FedSource customers. The acquisition performance measurement program provides for objectives, measures, and goals in the areas of (1) purchase cards, (2) small business goals, (3) compliance, (4) competition, (5) quality assurance, and (6) training. It should be noted, however, that the program goals set for fiscal year 2005 were at levels less than 100 percent of full compliance with procurement requirements. For example, FedSource's objective for compliance is to ensure task orders issued on behalf of customers meet all legal, regulatory, and policy requirements. However, its compliance goal for sampled fiscal year 2005 tasks orders was 80 percent. Likewise, FedSource's goals for quality assurance were set at less than 100 percent for fiscal year 2005. For fiscal year 2006, FedSource's goals in this area are to have surveillance plans in place for all performance-based contracts by March 31, 2006, and documented surveillance on all performance-based task orders by the end of fiscal year 2006.
- In August 2005, FedSource also revised its customer request form for services; the revised form includes detailed instructions for completing statements of work and quality assurance surveillance plans. FedSource also developed guidelines to delineate the role and responsibilities of the customer agency's project officer.
- In September 2005, FedSource established procedures for the use and documentation of task orders that are incrementally funded.

Findings and Recommendations

Finding 1 FedSource Did Not Ensure that Contract Actions Taken on Behalf of DoD Were Adequately Competed or Obtained Best Value

For the task orders sampled by our office and DoD OIG, FedSource contracting practices did not always give contractors a fair opportunity to be considered nor did FedSource always obtain the best value for supplies and services purchased. The exceptions we found include (1) not ensuring that all contractors under multiple-award contracts were given a fair opportunity to compete, (2) awarding task orders for work classified as “routine” to contractors with the lowest markup without considering promotional pricing that may have been offered by other available contractors, (3) awarding task orders to contractors who had marketed the business to FedSource, and (4) awarding contracts to DoD preferred sources without ensuring competition. Additionally, we found that the contract files for most task orders in our sample did not contained adequate documentation to demonstrate that the best value was obtained for supplies and services purchased on behalf of DoD. It should be noted, however, that FedSource has taken or planned actions that should if properly implemented, address these problems.

FedSource practices that limited competition and/or did not provide for the best value:

- ARC established multiple-award contracts under which FedSource centers could issue task orders to fulfill customer requirements. FedSource centers, however, did not ensure that all contractors providing similar services under available multiple-award contracts were given a fair opportunity to compete. FedSource management told us that in the future, all contractors providing similar services would be given a fair opportunity to compete for individual task orders.
- The DoD OIG found that FedSource, as a practice, restricted competition by identifying the requested work as either “routine” or “complex.” Routine work was work that did not have special recruitment, retention, management, or other

technical requirements. Other work was categorized as complex, for which FedSource required proposals for evaluation. Routine work was awarded to the contractor with the lowest markup and overhead rates. However, promotional pricing that may have been offered by other available contractors was not considered in contractor selection. In fiscal year 2005, FedSource made 2,201 routine buys from 2 multiple-award contracts, 2 single award contracts, and 7 BPAs. FedSource management informed DoD OIG that they plan to compete routine buys in the future.

- FedSource awarded a task order in the amount of \$738,013 to renovate a building at an Army facility. We found that the building renovation was not competed because FedSource selected a contractor that brought additional building renovation work to FedSource for award. In essence, if a vendor brought additional business to FedSource, that vendor was awarded the contract, as happened with this task order. In a July 12, 2004, letter, FedSource informed its contractors that the practice of awarding task orders to contractors that directly markets the business was inconsistent with the FAR and that task orders would now be competed among all awardees under multiple award contracts.
- FedSource awarded certain task orders to contractors that were indicated as the preferred source by the ordering DoD entity. For example, FedSource issued a task order in the amount of \$39,415 for the DoD's Washington Headquarters Service (WHS) for the services of a technical consultant. The task order was issued to a BPA contractor on September 30, 2004. The request for the services and an email from the WHS to FedSource with the subject line "DoD WHS – Suggested Source" identified the preferred technical consultant by name. Also, the statement of work named the selected contractor as the suggested source for the award. The task order file did not include a price negotiation memorandum, which should have documented the award process, or other evidence of competition. While customer requests for specific vendors or personnel is not in themselves a problem, FedSource needs to ensure it can demonstrate that if the task order is awarded to the customer's requested source, the contract action complied

with procurement requirements for fair competition and that the a fair and reasonable price was obtained.

- The FedSource task orders in our sample contained inadequate documentation to demonstrate that FedSource obtained the best value for supplies and services purchased. Specifically, 31 files did not have independent government cost estimates. Eighteen files did not have proposals, offers, or quotes evidencing competition. None of the files documented that market research was performed. Instead, FedSource used the same contractors repeatedly. Thirty-two files lacked price negotiation documentation. None of these files contained explanations of FedSource's cost analysis. There was also no documentation indicating that FedSource reviewed historical or industry cost data. Appendix 2 identifies the inadequate documentation found with the task orders we reviewed.

We also found that 1 of the 64 task order files in our sample was incrementally funded⁹ but lacked the required documentation. That task order, issued for asbestos abatement on November 13, 2003, was for \$683,799. The initial DoD MIPR for the task order, issued on July 30, 2003, was for \$370,596. FedSource later received additional funding from DoD increasing the total funding available for the task order to \$555,596. This amount, however, was \$128,203 less than the amount needed to fully fund the task order. When we questioned FedSource personnel about this disparity, they agreed that the task order was incrementally funded. We found, however, that FedSource had not adhered to its own policy or the FAR for documenting incrementally funded task orders. The policy requires that files for incrementally funded task orders include the following:

- total amount needed to fund the task order
- total period of performance
- incrementally funded amount

⁹ By law (Antideficiency Act, 31 U.S.C. § 1341), no office or employee of the government may create or authorize an obligation in excess of the funds available, or in advance of appropriations. If a contract is not fully funded upon award, the FAR requires that the contracts include a clause that expressly limits the government's obligation to reimburse the contractor for costs incurred to the incremental amount funded for the contract. The clause also provides that the contractor is not obligated to continue performance under the contract or otherwise incur costs in excess of the incremental amount funded. As additional funds are allotted for the contract, a contract modification is required.

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- funded period of performance
 - anticipated schedule for availability of additional funds
 - evidence that the customer has been quoted the full-year cost of the work and the period of performance
 - signed statement from the customer indicating that the task order is being incrementally funded and that the funds necessary to complete the project are expected to become available
 - language on the award stating that the funds necessary to complete the project are not currently available and that the federal government's liability is conditioned upon those funds becoming available

The task order file did not contain this documentation.

Among the 64 task order files we reviewed, 18 were from FedSource's Beaufort center. GAO had already identified this center as having procurement issues, including improper execution, improper funding, and documentation weaknesses. Consequently, FedSource management withdrew the Beaufort center's ordering authority and transferred the work to other FedSource centers.¹⁰ Each Beaufort file was assigned a new task order number. An April 21, 2005, FedSource memorandum to the file acknowledged the problems with the files but stated that (1) there was insufficient time to correct the many deficiencies and (2) gaining centers would therefore not be held responsible for any substandard files inherited. In January 2006, we found funding, contractor monitoring, and competition issues, as well as several exceptions to the FAR, in the transitioned Beaufort files. These problems remained unresolved as of March 2006.

We also noted that each FedSource center used different forms when awarding task orders. To address this, in July 2005, FedSource established a standard checklist for documentation. Items on the checklist include, among other things, the customer request form; justifications and approvals/determinations and findings; statement of work/performance work statement; quality assurance surveillance plan; independent government cost estimate; request for proposals; proposals, offers, or quotes; price

¹⁰ According to FedSource management, the Beaufort center was closed on June 30, 2006.

negotiation memorandum; and task order modifications. If properly implemented, the checklist should help ensure that FedSource centers adhere to procurement requirements.

Recommendations

We recommend that the Deputy Chief Financial Officer direct FedSource to do the following:

1. Comply with procurement requirements for fair and open competition when awarding task orders. Specifically, it should ensure that recent policies and other changes to procurement practices discussed in this finding have been implemented and institutionalized to include affording all contractors under multiple award contracts a fair opportunity to compete for task orders.

Management Response

In its response, management concurred with the recommendation. According to the response, FedSource changed its current process on existing contracts to discontinue using the "routine" ordering procedures. Future FedSource-wide contracts will require competition on all task orders through the use of requests for proposals. Modifications were processed to the multiple award contracts on June 29, 2006, to remove "routine" language. FedSource also discontinued the practice of awarding orders to contractors that marketed their FedSource contract on July 12, 2004. FedSource is in the process of providing updated guidance to its offices, customers, and contractors relating to "suggested sources." This guidance was completed November 17, 2006. FedSource has implemented new policies and procedures to address each of these findings. Training has been conducted since March 2006 and will continue to assure compliance.

Management also asserted in its response that based on the ordering procedures in the multiple award contracts, fair notice was provided to all awardees, if complex in nature, by issuing a request for proposal. "Award justification" information was included in the task order file. Additionally, promotional pricing

was considered in contractor selection for routine pricing, and contractors did offer promotional pricing which was incorporated into the contract.

OIG Comment

The corrective actions by management, if implemented as described, address the intent of our recommendation. As part of our second review of FedSource, covering fiscal year 2006 procurements on behalf of DoD, we plan to assess the actions taken. It should be noted, however, that while we saw evidence that promotional pricing by the selected vendor was considered in the routine buys included in our sample, the issue is that FedSource did not compete these buys with other available vendors.

2. Ensure that the contract files for all new task order awards and modifications to existing task orders include documentation of required competition, market research, and price reasonableness.

Management Response

Management concurred with the recommendation. According to its response, in July 2005 FedSource developed a price negotiation memorandum template outlining areas to address for a price reasonableness determination. Since that time, revisions have been made to the template to further improve documentation of the task order files. The revisions were completed on November 17, 2006. The price negotiation memorandum template outlines the competition that occurred, summarizes the evaluation of proposals, and documents fair and reasonable pricing through a market comparison, the independent government cost estimate, and/or historical procurement data. FedSource has also been working closely with DoD customers in developing the independent government cost estimate, which should be prepared as part of the initial request for services received from DoD. FedSource developed a Procedure Memorandum in June 2005, with specific instructions on how to assist customers in developing the independent government cost estimate.

Management also stated that market research is done at the overarching contract level in the acquisition planning stages. Although, a market comparison is performed when determining fair and reasonable pricing. DoD is required to conduct market research prior to using a non-DoD contract based on DoD policy issued in October 2004. FedSource issued an Acquisition Policy Memo dated July 5, 2005, which requires its employees to ensure all internal DoD reviews/approvals required prior to placing an order with FedSource have been completed. FedSource has implemented new policies and procedures to address this finding. Training has been conducted since March 2006 and will continue to assure compliance.

OIG Comment

The corrective actions by management, if implemented as described, address the intent of our recommendation. As part of our second review of FedSource, we plan to assess the actions taken. While we note that DoD requires its facilities to conduct market research to support decisions to use non-DoD contracting offices, market research by FedSource is still required to determine the best approach to acquire the specific services and property requested by DoD.

Finding 2 FedSource Task Orders Lacked Evidence of Adequate Quality Assurance Surveillance

According to the FAR, quality assurance surveillance plans are to be prepared in conjunction with the preparation of the statement of work and should specify all work requiring surveillance and the method of surveillance. Quality assurance surveillance is necessary to determine that supplies or services conform to contract requirements.¹¹ Of the 64 FedSource task order files reviewed, we found that 21 lacked a quality assurance surveillance plan, 2 had identical quality assurance plans although the scope of the task orders was different, and 4 had inadequate quality assurance plans.

¹¹ FAR 46.401.

COTRs are designated by the contracting officer and serve as the government's representative during the technical, acquisition, and pre- and post-award cycles of their assigned contracts. They monitor and document surveillance based on established quality assurance procedures.

We found task orders that lacked quality assurance surveillance plans in the FedSource centers we visited: Los Angeles – 11 task orders, Baltimore – 5 task orders, and St. Louis – 5 task orders. Furthermore, the files for 2 task orders issued by the Baltimore center contained identical quality assurance surveillance plans; but the period of performance in the plans were not consistent with the period of performance specified in the task orders.

We also found that the files for 4 task orders (3 issued by the Los Angeles center and 1 issued by the Baltimore center) had incomplete quality assurance surveillance plans. Although the plans were signed by a DoD project officer, they were not signed by the FedSource COTRs. Additionally, the quality assurance surveillance plans specified that when the DoD project officer signed the timecards or receiving reports they were certifying deliverables have been received and meet the government standard. They also state that FedSource would periodically ask for a copy of the project officer's worksheet to document the contract file. We did not find evidence that contractor monitoring was being performed.

The task orders that lacked or had inadequate quality assurance surveillance plans are identified in appendix 2.

We determined these files as well as the files without plans lacked evidence that FedSource COTRs performed inspections of the contractors' work or had otherwise obtained assurance that the contractors performed in accordance with the contract requirements.

Although FedSource had assigned a COTR to each task order we reviewed, none of the COTRs performed any surveillance on their assigned contracts. Additionally, COTR designation letters were not tailored to the unique requirements of the assigned task orders or the quality assurance surveillance plans. We also found that some COTRs were assigned to several task orders. When we asked

FedSource COTRs whether they had performed or documented surveillance of contractor performance, they stated that responsibilities for monitoring were assigned to DoD and that supervision and monitoring were being performed by the hiring DoD component. For example, one COTR stated that the DoD project officer signed certifying time and attendance reports. The COTRs also stated that they considered DoD's clearance for payment to be an indication that DoD had reviewed and approved the work. No written statements documenting that FedSource had communicated with DoD program managers about performance or acceptance of contractor surveillance was indicated in the task order files. When we informed FedSource management that quality assurance was not being performed, FedSource officials agreed and told us that they were aware of the situation and were taking steps to address it.

Without adequate quality assurance surveillance plans, consistently designated quality assurance responsibilities, timely monitoring of contract performance, and adequate documentation of monitoring, FedSource cannot ensure that it is safeguarding the interests of the federal government in its contractual relationships.

Recommendation

We recommend that the Deputy Chief Financial Officer direct FedSource to work with DoD to establish controls to ensure that (a) quality assurance surveillance plans are established for all task orders; (b) COTR designation letters clearly delineate who is responsible for performing monitoring, consistent with quality assurance surveillance plan instructions; and how monitoring is to be documented for each assigned task order; and (c) monitoring occurs and is documented before contractors are paid.

Management Response

In its response, management concurred with the recommendation. According to management, during the past year FedSource focused its efforts on developing and refining quality assurance surveillance plans with its customers for performance-based contracts. A quality assurance surveillance plan currently exist for every FedSource performance-based task order since July 2005.

FedSource also recognized a need to revise its COTR Delegation of Authority letters, as well as the need to identify its customer agency's responsibilities for monitoring and ensuring the technical requirements of the contract are being met and the performance was within the scope of the contract. Additionally, although the surveillance of task orders is completed at the customer level, FedSource continues to refine the process to ensure clear and concise performance metrics are in place. FedSource is also developing a plan to assist customers with surveillance of their orders by contacting the customer activities on a routine basis to perform surveillance as defined in the quality assurance surveillance plan. These actions were to be completed on January 2, 2007. FedSource team members will document the task order files with findings and report any yellow or red findings to the contractor for corrective action.

OIG Comment

The corrective actions by management, if implemented as described, address the intent of our recommendation. As part of our second review of FedSource, we plan to assess the actions taken.

Finding 3

FedSource Should Implement Additional Due Diligence Procedures to Help Ensure the Proper Use of Government Funds

For DoD procurements made through 21 FedSource task orders, DoD OIG identified instances where incorrect DoD appropriations were used and where the bona fide need rule¹² was potentially violated. As such, these deficiencies represent potential violations of the Antideficiency Act. While the DoD OIG's findings were principally directed at DoD, they point to a need for FedSource to identify what due diligence it performs when accepting orders to help prevent the use of incorrect appropriations. FedSource has

¹² The bona fide need rule is one of the fundamental principles of appropriations law: A fiscal year appropriation may be obligated only to meet a legitimate (bona fide) need arising in, or in some cases arising prior to but continuing to exist in, the fiscal year for which the appropriation was made.

also recognized this need according to our discussions with FedSource management. However, we noted that FedSource's three servicing centers had inconsistent procedures for reviewing MIPRs and interagency agreements before acceptance. As FedSource management has pointed out, guidance for conducting due diligence is not defined. Accordingly, FedSource should work with DoD in establishing a common set of indicators requiring more intense FedSource scrutiny.

As another observation, going forward FedSource will need to ensure that task orders for severable services¹³ do not have periods of performance that exceed 1 year from the date of MIPR acceptance in accordance with a recent DoD internal directive.

Under appropriations law, the concept of funds availability has three elements: purpose, time, and amount. All three must be observed for an obligation or expenditure to be legal. When DoD issues and FedSource accepts a MIPR, DoD records an obligation in its records against its appropriated funds.¹⁴ DoD is primarily responsible for ensuring the proper use of its appropriations. The DoD official who signs the MIPR is certifying this proper use.

The issues noted with the 21 procurements are as follows:

- Incorrect appropriations DoD OIG concluded that the wrong DoD appropriation was used by the ordering DoD component for 9 FedSource task orders. Four of these task orders were for construction projects at Army facilities. The funding MIPRs were obligated against a DoD operations and maintenance (O&M) appropriation, an incorrect appropriation for this work based on the dollar amount of the projects.¹⁵ The other 5 task orders involved improper use by DoD of a Research, Development, Test, and Evaluation (RDT&E) appropriation

¹³ When services are continuing and recurring in nature, the services are severable. Examples of such services in our sample include counseling, analytical, and program management support services.

¹⁴ When FedSource issues a task order for the goods or services requested in the MIPR, it obligates a Treasury revolving fund appropriation. A key feature of a revolving fund is that it is available without further congressional action and without fiscal year limitation.

¹⁵ 10 U.S.C. § 2805 established limits on the use of DoD O&M appropriations for minor military construction projects. Generally, such projects cannot exceed \$750,000 unless approved in advance by the secretary of the armed forces branch concerned and with prior congressional notification.

versus an O&M appropriation. The 9 task orders for which incorrect appropriations were used are identified in appendix 3.

- Bona fide need exceptions The goods and services acquired through 16 FedSource task orders were inconsistent with the bona fide need rule. These 16 task orders included 4 task orders for which DoD OIG also concluded that an incorrect DoD appropriation was used. The common element in these cases is that the task orders were awarded in the fiscal year following the fiscal year appropriation that was obligated by DoD. For example, on September 30, 2004, a DoD component issued and FedSource accepted a MIPR funded with a DoD fiscal year 2004 appropriation to provide repair services on a runway and taxiway with a period of performance from December 1, 2004, to November 30, 2005. FedSource awarded the contract on April 4, 2005, 6 months after accepting the MIPR. The amount of the task order was \$1,188,042. In another example, DoD issued a MIPR on September 13, 2004, for a Public Awareness Campaign and Family Child Care Conference that was obligated using fiscal year 2004 funds. FedSource awarded the related task order in the amount of \$1,027,640 with a period of performance from September 22, 2004, through September 13, 2005. However, the conference that was part of the services was not scheduled until July 2005.

Certain task orders involved severable services. Under DoD procurement requirements, DoD may use funds available for a fiscal year to enter into a contract for severable services that begin during the fiscal year and end in the next fiscal year as long as the contract period does not exceed 1 year.¹⁶ For two task orders, the period of performance, including modifications, exceeded 1 year from the date of initial MIPR acceptance and obligation of the DoD funds. The details of these task orders are presented in the following table:

¹⁶ 10 U.S.C. § 2410a. A similar provision for civilian agencies was enacted as part of the Federal Act Streamlining Act of 1994 and is codified at 41 U.S.C. § 253l.

Task Order				Period in Excess of 1 year From MIPR Acceptance
Number	Amount	Period of Performance	Date MIPR Accepted	
LOS014553 ^a	\$14,483,489	3/14/2005 to 12/31/2005	7/30/2004	5 months
LOS013101	\$121,661	9/30/2004 to 11/30/2005	9/22/2004	2 months

^a The task order was initially issued on March 29, 2005, by the FedSource Beaufort center as no. BEA002638.

A March 2006 DoD internal directive clarified requirements for severable services contracts made through servicing agencies. Specifically, the directive states that under no circumstances should any existing order for severable services using O&M funds extend beyond 1 year from the date the funds were accepted by the servicing agency.¹⁷

Appendix 3 identifies the 16 task orders for which DoD OIG identified bona fide need exceptions based on its review.

It is generally recognized that legitimate rationales exist for an obligation incurred in one fiscal year resulting in the delivery of service in the next one. In the case of service contracts, the need for a particular service may arise in one fiscal year but full performance cannot be completed within that same year. In the case of delivery of goods contracts, there are many valid reasons why delivery cannot be completed in the same year. For example, the contractor may need to fabricate certain components, or the necessary materials may not be available until the next year. The general rule is, "If an obligation is proper when made, unforeseen delays that cause delivery or performance to extend into the following year will not invalidate the obligation." A September 25, 2003, internal DoD directive further recognizes that there are situations when it is appropriate for servicing agencies such as FedSource to retain and obligate the funds in the following year but cautions that the bona fide need must exist for the fiscal year in which the order is made. The directive also cautions that the

¹⁷ Memorandum by the Under Secretary of Defense (Comptroller), dated March 27, 2006, "Proper Use of Interagency Agreements with Non-Department of Defense Entities Under Authorities Other Than the Economy Act."

obligation by the servicing agency should be made promptly in the following year.¹⁸

Although DoD is responsible for the proper use of its appropriations, we believe and FedSource management agrees that FedSource has a due diligence responsibility as well. By virtue of its role as a servicing agency, charged with taking and executing orders, and obligating the United States on behalf of the requesting agency, FedSource has a concurrent duty to ensure the legitimacy and legality of orders that it places. Taking into consideration the limited nature of review possible on the servicing agency's side of a transaction, FedSource's contracting centers, with their expertise in government contracting and appropriations laws and regulations, have a duty to review orders and a duty to ask questions when cautionary flags are raised. Although they may be unfamiliar with the particular characteristics of a specific agency's appropriation, they should be familiar with common rules, laws, and principles that should typically be applied in reviewing an order.

While FedSource management acknowledged the need for due diligence, there is no consensus on which indicators that FedSource contracting officers should consider when they review DoD procurement requests. Each FedSource center established its own procedures for reviewing funding documents such as MIPRs. All had a check for ensuring that the funding document was signed by the ordering agencies and procedures to note the period of availability of the funding (no-year, 1-year). One center instructed staff to review the document for "correct use of funding" and noted that "O&M funding is for one year" and "[RDT&E] is for two or more years." We believe that, working with DoD, FedSource should develop a standard set of procedures and due diligence checks to be followed by its ordering centers. Checks could include

¹⁸ Memorandum by the Under Secretary of Defense (Comptroller), dated September 25, 2003, "Fiscal Principals and Interagency Agreements." The memorandum states, in part: "Every order under an interagency agreement must be based upon a legitimate, specific, and adequately documented requirement representing a *bona fide* need of the year in which the order is made. As always, adequate funds of the appropriate type (procurement, O&M, *etc.*) must be available. If these basic conditions are met, these servicing agencies may retain and promptly obligate the funds in the *following* fiscal year. On the other hand, an interagency agreement may not be used in the last days of the fiscal year solely to prevent funds from expiring to keep them available for a requirement arising in the following fiscal year."

such things as legal limits on the use of O&M appropriations for military construction and the proper use of RDT&E funds. It should also work with DoD to establish more clear parameters for the “prompt” awarding of contracts after the fiscal year of the funding.

Recommendations

We recommend that the Deputy Chief Financial Officer direct FedSource to do the following:

1. Develop uniform procedures that outline the steps of a reasonable review (due diligence) to be performed before FedSource accepts a MIPR. By applying the reasonable standard, FedSource should ensure that the MIPR has the appropriate signatures and that all information appears adequate. If something unusual or out of the ordinary is identified (e.g., a request for military construction that exceeds a legal threshold), FedSource should seek resolution prior to accepting the MIPR or reject the MIPR. FedSource should work with DoD as necessary to establish the elements of such a review.

Management Response

In its response, management partially concurred with the recommendation. According to management, FedSource established uniform procedures that require a due diligence review prior to signing interagency agreements or MIPRs. FedSource issued procedures on July 26, 2006. The review includes checking that signatures from both program and financial officials have been obtained. FedSource is relying on the program official to represent the customer and sign the agreement signifying they approve of the transaction. FedSource is also relying on the financial official to represent the customer and sign the agreement signifying that funds are available and appropriate for the uses outlined. FedSource will not assume responsibility for the lack of due diligence on the part of customer officials that sign the agreements. FedSource should be aware of government-wide and industry specific issues or restrictions for any area of service it is offering; however, the customer is ultimately accountable for any

specific restrictions as to the availability and use of their funds. As such, FedSource disagrees with the example given regarding military construction and thresholds specific to military customers. This is a customer-specific restriction and should be considered by the program and financial representatives of the customers before they sign the interagency agreement or MIPR.

Management also stated that FedSource is willing to work with DoD and other customers to establish a list of checks to be included in FedSource's reasonableness review. This was to be completed on December 15, 2006. However, DoD and other customers will need to establish a methodology for keeping FedSource up to date on the customer's internal policy impacting the checks included in the list. It is important to understand that even with these reasonableness checks in place the customer retains the ultimate responsibility when signing the interagency agreement or MIPR.

OIG Comment

Management's stated action that it established uniform procedures for a due diligence review and is willing to work with DoD and other customers to establish the checks to be included in the review, if done, appears to conform with the intent of our recommendation. As part of our second review of FedSource, we plan to assess these actions.

That said, certain aspects of management's response are of concern. Specifically, management is taking a more limited view of due diligence than we believe is necessary to prevent the types of contracting deficiencies discussed in the finding. This limited view is indicated by its disagreement with the military construction exception (where the military construction limit was exceeded for the type of DoD funds used). We believe the military construction limit, which is prescribed in law, is not some obscure restriction. As such, it is the very type of restriction we would expect to see considered as part of a due diligence review. Going forward, our concern may be addressed as FedSource and its customers come to a common understanding of the due diligence to be performed by

FedSource when accepting orders. Management needs to give this issue continued attention.

2. Ensure that the period of performance of task orders for severable services do not exceed 1 year from the date of the MIPR acceptance.

Management Response

Management partially concurs with the recommendation. According to its response, FedSource and other federal agencies (including DoD's operational and policy departments) interpret the Federal Streamlining Act differently from the conservative approach presented in the finding and recommendation. FedSource is preparing a letter to GAO requesting clarification on this issue. Until GAO provides clear guidance on this issue it will be subject to interpretation. FedSource planned to issue no later than November 30, 2006, that supports the DoD guidance.

Additionally, FedSource takes the position that the customer should be able to receive 12 months of service from the date of its task order as long as the customer obligation (MIPR acceptance) and the FedSource obligation (task order) are made in the same fiscal year. In this case, the customer does not receive any services or benefits that they could not receive without FedSource. In cases where the customer obligation (MIPR acceptance) occurs in one fiscal year and the FedSource obligation (task order) occurs in a subsequent fiscal year, we agree the period of performance should not exceed 12 months from the customer obligation (MIPR acceptance). If the customer were allowed 12 months of service from the date of the FedSource task order in this instance they would be expanding the use of their funds beyond what they could do without FedSource because their funds would have expired at the end of the fiscal year.

The audit report implies possible problems with FedSource awarding task orders in subsequent years. The report states, "The common element in these cases is the task orders were awarded in the fiscal year following the fiscal year appropriation that was obligated by DoD," but then it goes on to say that this

activity is not inappropriate. The report references that the servicing agency's obligation need to be made "promptly" but there is no clear guidance as to what this specifically means.

FedSource also does not agree with the two examples provided referring to DoD's bona fide need issues. Dates alone do not make a bona fide need violation. Just because FedSource awards a task order in subsequent year does not mean that the customer did not have a bona fide need at the time of their obligation. In the runway example, the customer's bona fide need has to do with the condition of the runway the time of the obligation. If the runway needed maintenance then a bona fide need existed. The date FedSource issued the task order for maintenance work could be used to shed doubt whether a bona fide need existed, but the report is silent as to why there was a 6-month timeframe between the MIPR acceptance and the task order. In the Public Awareness Campaign example, it is unclear whether the Family Conference was part of the overall campaign or a separate need. If it were part of the overall campaign, the fact that this specific deliverable was not scheduled until the next fiscal year would not result in a bona fide need violation.

OIG Comment

While seeking GAO clarification is a management prerogative, its action to issue guidance supporting DoD guidance for severable services, if responsive to the DoD guidance and properly implemented by FedSource, satisfies the intent of this recommendation. We believe that the awarding of task orders in the subsequent year of the funding is an area of concern. The further out the task order is awarded relative to the MIPR date should raise a cautionary flag as whether the bona fide need rule was met. In working with DoD to establish the elements of a due diligence review, management should seek DoD expectations for promptness in the issuance of task orders, especially when the task order cannot be awarded in the same fiscal year as the funding source.

While we agree that dates alone do not make a bona fide need violation, the two examples cited in our finding are problematic, and represent potential exceptions to the bone fide need requirement. The runway and taxiway repair services task order involved the widening of a taxiway as opposed to ongoing repair services. Additionally, the period of performance for this work, as stated on the task order, started 2 months after the funding year and before the task order was awarded. These factors should have raised a flag. It should also be noted that the task order file did not contain documentation that might explain why it took 6 months to award the order, and the management response did not include any explanation for this time period. Likewise, the task order file for the Public Awareness Campaign did not show how the Family Conference was an integral part of, and could not be separated from, the other services being acquired which were of an ongoing nature. This component (the Conference) of the procurement request should also have raised a flag as to the bona fide need rule because the conference was scheduled in a subsequent fiscal year of the funding source. In this regard, the management response provides no additional information to support that the requirement was met.

* * * * *

We appreciate the courtesies and cooperation extended to our staff during this audit. The major contributors to this report are identified in appendix 5. If you have any questions, please contact me at (202) 927-5904.

Thomas E. Byrnes
Director, Manufacturing and Procurement Audits

The Department of the Treasury (Treasury) franchise fund, through its FedSource and the Administrative Resources Center components, provides contracting assistance to the Department of Defense (DoD) for a fee. As required by the National Defense Authorization Act (NDAA) for Fiscal Year 2006, Section 811, the DoD Office of Inspector General and our office separately, but concurrently reviewed the procurement policies, procedures, and internal controls of the Treasury franchise fund. Our objective, stated in the law, was to determine whether Treasury: (1) is compliant with defense procurement requirements; (2) is not compliant with defense procurement requirements, but has a program or initiative to significantly improve compliance with defense procurement requirements; or (3) neither of these conclusions is correct. As mandated by NDAA, we entered into a Memorandum of Understanding with DoD OIG, as required by NDAA, to carry out this review and make the determinations required. We executed the Memorandum of Understanding on March 6, 2006, and coordinated with DoD OIG throughout our audit.

We reviewed applicable DoD appropriations laws and applicable Federal Acquisition Regulation and DoD regulations and procurement requirements. We also reviewed a July 2005 Government Accountability Office (GAO) report on FedSource. Additionally, we reviewed FedSource's procurement policies, procedures, and internal controls applicable to the procurement of property and services on behalf of DoD, including policies and procedures established in response to the GAO report. We also interviewed Treasury franchise fund officials and staff.

To test compliance with defense procurement requirements, DoD OIG pulled a sample of FedSource task orders representing high dollar amounts and DoD ordering offices with high volume transactions. We concurred with DoD OIG's approach and reviewed FedSource's files for 64 task orders, and related FedSource Contracting Officer's Technical Representative files. The amount funded by DoD for the sample task orders totaled \$43.2 million and were awarded in FedSource's centers in Baltimore, MD; St. Louis, MO; and Los Angeles, CA. We examined the files for documentation supporting compliance with applicable Federal Acquisition Regulation and DoD procurement requirements,

specifically requirements related to market research, competition, price reasonableness, funding, and the receipt of the property and services ordered. The files were located at the three FedSource ordering centers.

We also reviewed contract files at Administrative Resources Center, located at the Bureau of the Public Debt in Parkersburg, West Virginia, for 15 blanket purchase agreements and single and multiple-award contracts. The blanket purchase agreements, single and multiple-award contracts were master contract vehicles under which FedSource awarded the 64 task orders in our sample.

We performed our audit field work between August 2005 and July 2006. Our audit was conducted in accordance with generally accepted government auditing standards.

Appendix 2
Missing Documentation From FedSource Task Order Files

Task Order Award No.	Amount	Independent Government Cost Estimate	Proposal, Offer, or Quote	Price Negotiation Memorandum	Quality Assurance Surveillance Plan
STL001972-01	\$52,014	N/A		N/A	
STL001972-02	136,139	N/A		N/A	
STL001916-01	64,821	N/A		N/A	
STL001916-02	185,177	N/A		N/A	
STL001457-01	51,249	X			
STL001457-02	94,904	X		X	
STL001457-03	228,384	X		X	
STL001373-02	31,928	N/A		N/A	
STL001373-03	70,180	N/A		N/A	
STL001373-01	25,300	N/A		N/A	
STL001374-03	171,691	X		N/A	
STL001374-01	73,238	X		N/A	
STL001374-02	79,592	X		N/A	
STL001114-26	84,801	N/A	N/A	N/A	
STL001272-17	74,405	N/A	N/A	N/A	
STL001115-23	67,513	N/A	N/A	N/A	
STL001617-13	44,347	N/A	N/A	N/A	
STL001118-07	20,344	N/A	N/A	N/A	
STL001623-15	34,883	N/A	N/A	N/A	
STL001305-21	43,235	N/A	N/A	N/A	
STL001619-02	7,051			N/A	
STL001622-02	7,051	X	X	N/A	
STL001633-04	5,748	N/A	N/A	N/A	
STL002275-01	428,400	X	X	X	O
STL002276-01	35,905	N/A	X	X	O
STL002277-01	484,500	X	X	X	O
STL002432-01	306,000	X	X	N/A	O
STL002433-07	246,168				O
STL002274-01	1,027,640	X	X		
STL002368-01	50,532				
LOS007993-01	692,449	X		X	
LOS008119-01	738,013	X		X	I
LOS008200-01	950,509	X		X	O
LOS008378-01	254,267			X	O

Legend:

X - Documentation missing in task order file

I - Quality assurance surveillance plan documentation was incomplete

O - Task order file had no documentation for quality assurance surveillance plan

D - Task order file contained duplicate quality assurance surveillance plan

Appendix 2
Missing Documentation From FedSource Task Order Files

Task Order No.	Amount	Independent Government Cost Estimate	Proposal, Offer, or Quote	Price Negotiation Memorandum	Quality Assurance Surveillance Plan
LOS011716-01	\$1,683,419	X		X	O
LOS012907	652,467			X	O
LOS013032-01	762,883	X		X	O
LOS013101-01	121,662	X		X	
LOS013139-04	556,048			X	
LOS013342-01	1,105,250	X	X	X	
LOS013406-02	163,317	X		X	O
LOS013626-01	233,699			X	
LOS013969-01	2,714,425	X	X	X	O
LOS014013-011	7,246,377	X	X	X	O
LOS014086-01	432,427	X		X	I
LOS014097-01	303,425	X		X	O
LOS0141280-02	89,890				
LOS014181-01	1,208,054	X		X	O
LOS014227-01	318,330			X	
LOS014468	677,830			X	I
LOS014553-01	14,483,489	X	X	X	O
BAL015420-06	58,787				
BAL119068	10,980				
BAL118876-03	50,001	X	X	X	O
BAL015435-01	44,602		X		
BAL015557-03	42,950		X		D
BAL118884-01	39,415	X	X	X	O
BAL015316-01	46,483			X	
BAL119603	450,000				I
BAL016947-01	75,571				D
BAL118432-01	2,174,401	X	X	X	O
BAL118906	172,993	X	X	X	
BAL118431	251,010	X	X	X	O
BAL118430	143,985	X	X	X	O
	\$43,182,548	31	18	32	27

Legend:

X - Documentation missing in task order file
I - Quality assurance surveillance plan documentation was incomplete

O - Task order file had no documentation for quality assurance surveillance plan
D - Task order file contained duplicate quality assurance surveillance plan

Appendix 3
Task Orders With DoD Funding and Bona Fide Need Exceptions

Task Order No.	Description	Deficiency Noted by DoD OIG	
		Funded with Wrong DoD Appropriation	Bona Fide Need Exception
LOS014181	Taxiway Repair	X	X
STL001373	Management Assistant	X	
STL001916	Analyst III for Urban Operations Project Support	X	X
STL001972	Analyst III	X	X
STL001374	Analyst	X	X
LOS008200	Construction of Main Gate Canopy and Inspection Bldg	X	
LOS013032	Renovation of Bldg 454	X	
LOS008119	Renovation of Bldg 453	X	
LOS007993	Construction of Maintenance Buildings	X	
LOS014553	Counseling Services		X
STL002274	Family Child Care Public Awareness Campaign and Family Child Care Conference		X
STL001457	Analyst IV for Project Support		X
STL002277	Boys and Girls Club of America		X
STL002276	Youth Fitness Activities and Kits		X
STL002433	Entertainment		X
LOS013626	Transportation Relocation		X
LOS014128	Valve Replacement		X
LOS013101	Design and Acquisition Support		X
LOS013406	Repair Underground Vaults in Parking Apron		X
LOS013139	Utilities, Engineering, and Planning Support		X
BAL118884	Applications Consultant		X
Totals		9	16



DEPARTMENT OF THE TREASURY

11/21/06

MEMORANDUM FOR: Thomas E. Byrnes
Director, Manufacturing and Procurement Audits

FROM: Richard Holcomb *Richard M. Holcomb*
Deputy Chief Financial Officer 11-21-06

SUBJECT: OIG Draft Report, Acquisitions: Treasury Franchise Fund
Needs to Improve Compliance with Department of Defense
Procurement Requirements

Thank you for the opportunity to comment on the draft report, "Treasury Franchise Fund Needs to Improve Compliance with Department of Defense Procurement Requirements." FedSource is committed to serving DoD interests by providing the highest quality goods and services through contract vehicles that are compliant with laws, regulations, and administrative policies and procedures.

DoD's use of FedSource as a service provider relieves DoD of the need to increase the size of its acquisition workforce in areas outside of its core missions. FedSource is also able to use the combined buying power of its government customers to pass along savings to DoD and non DoD agencies. In addition to these benefits, FedSource contracts lead the Treasury Department in utilizing the services of small businesses. Our system feeds this data into FPDS-NG thereby assisting DoD in meeting its small business goals as well.

We appreciate your recognition of our efforts to significantly improve FedSource operations. Our efforts have addressed both GAO recommendations and findings outlined in this draft report. However, we are concerned that the timing of the follow up review does not allow FedSource or DOD sufficient time to fully institutionalize the improvements and changes currently underway (i.e., draft reports issued September 14, 2006 with the next year's follow up review focusing on work performed from July through September, 2006 (dates prior to the original draft report). Nevertheless, we are making progress to implement the recommendations.

Our management response to the findings and recommendations follows.

Page 1 of 6

Finding 1: FedSource did not ensure that contract actions taken on behalf of DOD were adequately competed or obtained best value.

Recommendations:

1. Comply with procurement requirements for fair and open competition when awarding task orders. Specifically, it should ensure that recent policies and other changes to procurement practices discussed in this finding have been implemented and institutionalized to include affording all contractors under multiple award contracts a fair opportunity to compete for task orders.

Management Response: Concur

- Based on the ordering procedures in the multiple award contracts, fair notice was provided to all awardees, if complex in nature, by issuing a request for proposal (RFP). "Award justification" information was included in the T.O. file. We have changed our current process on existing contracts to discontinue using the "routine" ordering procedure. Our future FedSource-wide contracts will require competition on all task orders through the use of an RFP. It should be noted that promotional pricing was considered in contractor selection for routine ordering. Contractors did offer promotional pricing which was incorporated into their contract. FedSource considered this promotional pricing in their award determinations. Modifications were processed to the multiple award contracts on June 29, 2006 to remove "routine" language.
- FedSource discontinued the practice of awarding orders to contractors that marketed their FedSource contract on July 12, 2004. FedSource is currently in the process of providing updated guidance to all FedSource offices, customers and contractors relating to "suggested sources". Guidance was completed November 17, 2006. We support DOD's efforts in educating their personnel regarding these practices as well.
- FedSource has implemented new policies and procedures to address each of these findings. Training has been conducted since March 2006 and will continue to assure compliance.

2. Ensure that the contract files for all new task order awards and modifications to existing task orders include documentation of required competition, market research, and price reasonableness.

Management Response: Concur

- In July, 2005 FedSource developed a price negotiation memorandum (PNM) template outlining areas to address for a price reasonableness determination. Since that time revisions have been made to the template to further improve

- FedSource recognized a need to revise our COTR Delegation of Authority letters, as well as, the need to identify our Customer Agency's responsibilities for monitoring and ensuring the technical requirements of the contract are being met and that performance was within the scope of the contract. Currently, the draft delegations of authority and customer roles are being reviewed by the Administrative Resource Center (ARC). Once the letters are approved, ARC will issue revised delegation to FedSource COTRs and FedSource will issue guidance to our customer agencies. This action is estimated to be completed January 2, 2007.

3. Ensure monitoring occurs and is documented prior to making payment to the contractor.

Management Response: Concur

- Although the surveillance of our task orders is completed at the customer level, FedSource continues to refine the process to ensure clear, concise, performance metrics are in place. FedSource is developing a plan to assist customers with surveillance of their orders by contacting the customer activities on a routine basis to perform surveillance as defined in the QASP. This action is estimated to be completed by January 2, 2007. The FedSource team members will document the Task Order files with findings and report any yellow or red findings to the Contractor for corrective action.

Finding 3: FedSource Should Implement Additional Due Diligence Procedures to Help Ensure the Proper Use of Government Funds

Recommendations:

1. Develop uniform procedures that outline the steps of a reasonable review (due diligence) to be performed before FedSource accepts a MIPR. By applying the reasonableness standard, FedSource should ensure that the MIPR has the appropriate signatures and that all information appears adequate. If something unusual or out of the ordinary is identified (e.g., a request for military construction that exceeds a legal threshold), FedSource should seek resolution prior to accepting the MIPR or reject the MIPR. FedSource should work with DoD as necessary to establish the elements of such a review.

Management Response: Partially Concur

- FedSource has established uniform procedures that require a due diligence review prior to signing interagency agreements or MIPRs. FedSource issued procedures on July 26, 2006. The review includes checking that signatures from both program and financial officials have been obtained. FedSource is relying on the program official to represent the customer and sign the agreement signifying they approve of the transaction. FedSource is relying on the financial

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official to represent the customer and sign the agreement signifying that funds are available and appropriate for the uses outlined. FedSource will not assume responsibility for the lack of due diligence on the part of customer officials that sign the agreements.

- FedSource should be aware of government-wide and industry specific issues or restrictions for any area of service they are offering, however, the customer is ultimately accountable for any specific restrictions as to the availability and use of their funds. As such, FedSource disagrees with the example given regarding military construction and thresholds specific to military customers. This is a customer specific restriction and should be considered by the program and financial representatives of the customers before they sign the IA or MIPR.
- FedSource is willing to work with DoD and other customers to establish a list of checks to be included in FedSource's reasonableness review. This is estimated to be completed December 15, 2006. However, DoD and other customers will need to establish a methodology for keeping FedSource up to date on the customer's internal policy impacting the checks included in the list. It is important to understand that even with these reasonableness checks in place the customer retains the ultimate responsibility when signing the Interagency agreement or MIPR.

2. Ensure that the period of performance of task orders for severable services do not exceed 1 year from the date of the MIPR acceptance.

Management Response: Partially Concur

- FedSource and other federal agencies (including DoD's operational and policy departments) interpret the Federal Streamlining Act differently from the conservative approach presented in the finding and recommendation. FedSource is preparing a letter to GAO requesting clarification on this issue. Until GAO provides clear guidance on this issue it will be subject to interpretation. FedSource will issue guidance no later than November 30, 2006 that supports the DoD guidance.
- FedSource takes the position that the customer should be able to receive 12 months of service from the date of FedSource's task order as long as the customer obligation (MIPR acceptance) and the FedSource obligation (task order) are made in the same fiscal year. In this case, the customer does not receive any services or benefits that they could not receive without FedSource. In other words, they could enter into a direct contractual arrangement with a vendor for the same time period as the FedSource task order. In cases where the customer obligation (MIPR Acceptance) occurs in one fiscal year and the FedSource obligation (task order) occurs in a subsequent fiscal year, we agree the period of performance should not exceed 12 months from the customer obligation (MIPR acceptance). If the customer were allowed 12 months of service from the date of the FedSource task order in this instance, they would be expanding the use of their funds beyond what they could do without FedSource

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because their funds would have expired at the end of the fiscal year.

- The audit report implies possible problems with FedSource awarding task orders in subsequent years. The report states, "The common element in these cases is that the task orders were awarded in the fiscal year following the fiscal year appropriation that was obligated by DoD." but then it goes on to say that this activity is not inappropriate. The report references that the servicing agency's obligation needs to be made "promptly" but there is no clear guidance as to what this specifically means.
- FedSource does not agree with the two examples provided referring to DoD's bona fide need issues. Dates alone do not make a bona fide need violation. Just because FedSource awards a task order in subsequent year doesn't mean that the customer did not have a bona fide need at the time of their obligation. In the runway example, the customer's bona fide need has to do with the condition of the runway at the time of their obligation. If the runway needed maintenance then a bona fide need existed. The date FedSource issued their task order for maintenance work could be used to shed doubt whether a bona fide need existed, but the report is silent as to why there was a six-month timeframe between the MIPR acceptance and the task order. In the Public Awareness Campaign example, it is unclear whether the Family Conference was part of the overall campaign or a separate need. If it were part of the overall campaign, the fact that this specific deliverable was not scheduled until the next fiscal year would not result in a bona fide need violation.

Appendix 5
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