

GAO

Report to the Chairman, Committee on  
Government Operations, House of  
Representatives

July 1987

ADP SYSTEM

Patent Office's  
Contract Renegotiation  
Behind Schedule



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**Information Management and  
Technology Division**

B-217448

July 31, 1987

The Honorable Jack Brooks  
Chairman, Committee on Government Operations  
House of Representatives

Dear Mr. Chairman:

This report responds to your March 9, 1987, request to review the status of the efforts by the Department of Commerce's (Commerce) Patent and Trademark Office (PTO) to renegotiate the current contract for the development and deployment of its automated patent system. You requested that we determine (1) PTO's progress in implementing the Committee's requirements for renegotiation (specifically that the contract be for a maximum of 8 years, be fixed price or cost plus fixed fee with well-defined terms, and give the government the right to deal directly with subcontractors if the contract is canceled), and (2) the reason for any delay in the renegotiation.

Our work showed that some progress is being made in renegotiating the automated patent system contract, and that Commerce and the contractor plan to address the Committee's particular items of concern. However, the Committee's requirements will not be accomplished until all negotiations have been completed and the contract modifications executed. Renegotiation efforts are behind schedule because of delays in the preparation and approval of detailed statements of work. Also, audit reports on the contract by the Defense Contract Audit Agency (DCAA) contain findings that may delay execution of the final contract modification. Commerce is about 4 months behind its own schedule for completing the renegotiation, and officials recently told us they now expect to complete the renegotiation 2 to 3 months beyond their original October 16, 1987, deadline.

**Scope and  
Methodology**

We reviewed the request for proposals, the resulting contract for the automated patent system, PTO's Automation Master Plan (Edition 3, April 1987), and the Federal Acquisition Regulations regarding government contracts.

We specifically concentrated on the Committee's three renegotiation requirements: length of contract should not exceed 8 years, the fee arrangement should be fixed price or cost plus fixed fee with well-defined terms, and the government should have the right to deal directly

with subcontractors if the contract is canceled. To determine the status of the renegotiation efforts, we (1) interviewed Commerce and PTO officials, including Commerce's Deputy Assistant Secretary for Special Programs, the Director of Commerce's Procurement and Administrative Services Division, and PTO's Administrator for Automation, and (2) reviewed pertinent documentation, including a January 1987 memorandum of understanding between Commerce and the contractor that stated their basic agreement to renegotiate the contract and outlined the provisions and timeframes to achieve the renegotiation. We discussed their efforts and progress toward completing the renegotiation as set forth in the agreement. We also reviewed the statement of work for one recently completed modification to the contract. In addition, we reviewed DCAA audit reports on the original contract and the contractor's response to the audit findings, and evaluated the effect these may have on the renegotiation process.

We conducted our review from April to July 1987. We limited the scope of our audit work to the status of the renegotiation efforts and the reason for any delay in completing the renegotiation. We did not evaluate the agency's strategy to accomplish the renegotiation. We discussed key facts with Commerce and PTO officials and have included their comments as appropriate. However, we did not request official agency comments on a draft of this report. Our work was performed in accordance with generally accepted government auditing standards.

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## Background

PTO administers the patent and trademark laws of the United States. Patent laws encourage technological advancement by providing incentives to invent, invest in, and disclose new technology. The agency's primary role in administering patent laws is to examine patent applications and grant patent protection for qualified inventions. PTO has repeatedly identified three impediments to its ability to carry out its mission: the growth of paper files, increases in resources required to maintain those paper files, and degrading integrity of the files. In 1980, the Congress, through P.L. 96-517, directed PTO to develop a plan for an office-wide automation program—which it began implementing in 1982. The latest edition of its master automation plan was issued in April 1987.

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In October 1983, Commerce issued a request for proposals for the design, development, implementation, and maintenance of the automated patent system. On April 12, 1984, Commerce awarded a cost-plus-fixed-fee contract to the Planning Research Corporation. At that time, the contract's cost was estimated to be about \$289 million; its projected period for completion was 18 years. Under the contract, Commerce periodically allocates funds when billed by the contractor.

In July 1986 we reported on the status of the automated patent system.<sup>1</sup> In that report, we cited a number of concerns regarding PTO's management of the multimillion dollar patent automation program. One of our concerns was the inappropriateness of a cost-plus-fixed-fee contract estimated to take 18 years to complete. We noted that such a contract is inconsistent with federal guidance and contains minimal contractor cost-control incentives. Federal regulations and guidelines indicate that while cost-reimbursement contracts may be appropriate for the initial phases of the project, firmer prices should be established during the later phases so the government can minimize the risk of cost growth. Because cost-reimbursement contracts are normally used only for design and development, under PTO's contract the government assumed too much risk of higher-than-appropriate costs after development and testing of the patent system.

We recommended that Commerce reassess the patent automation program and include a determination of the most appropriate acquisition strategy to mitigate the government's risk, particularly for implementation and maintenance activities. In addition, we recommended that, to the extent possible, all future acquisition activities include competitive procurement with fixed-price contracts.

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## Commerce Is Renegotiating the Automated Patent System Contract

After our July 1986 report, the Committee and officials of Commerce and the contractor had a meeting at which the Committee's requirements were outlined. At that meeting, Commerce officials also discussed with the contractor the possibility of renegotiating the automated patent system contract. These discussions resulted in a January 7, 1987, memorandum of understanding between Commerce and the contractor to renegotiate the contract in two phases. Phase One would cover the contractor's work through October 16, 1987. Phase Two would include primarily the work necessary to develop and deploy the system. After

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<sup>1</sup>ADP Acquisitions, Patent Automation Encountering Major Planning and Procurement Problems, GAO IMTEC-86-19, July 17, 1986.

deployment, a new request for proposals would be issued for maintenance of the system. Our review showed that Commerce plans to address each of the Committee's requirements noted above during the negotiation of Phase Two.

The agreement between Commerce and the contractor to renegotiate included specific provisions and a timetable to complete the entire renegotiation process by October 16, 1987. Phase Two will cover all work to be accomplished from that date to contract completion. The memorandum of understanding included provisions to:

- shorten the Phase Two contract term to primarily include system development and deployment efforts and delete a portion or all of subsequent system maintenance;
- retain the cost-plus-fixed-fee arrangement for Phase One, but negotiate a "fixed price and/or incentive or award" fee arrangement for Phase Two;
- give the government the right in Phase Two to require the contractor to assign its subcontractor rights to the government in case of termination for default;
- prepare detailed statements of work for each of the phases; and
- require that in Phase Two the contractor include a complete definition of labor categories (e.g., salary level and hours worked on specific jobs) so that individuals billed on contractor's invoices can be easily traced back to the labor categories.

The Phase One contract modification was signed by both parties effective May 18, 1987. The Phase One modification included a detailed statement of work that specifies deliverables and delivery dates for work from December 1, 1986 through October 16, 1987. The modification also provided for a funding level of \$12.5 million (and negotiations to establish a separate total cost and fixed fee) for Phase One for a total of \$75.5 million from the time of the contract award in 1984 through completion of Phase One.

As the first step of Phase Two, a detailed statement of work is being drafted by Commerce and PTO officials. Once completed, it will be delivered to the contractor for review. Negotiations can then begin on the specific provisions listed in the January 1987 agreement for Phase Two, including the Committee's requirements as to length of contract, type of fee arrangement, and assignment of subcontractor rights. Commerce's Deputy Assistant Secretary for Special Programs, whose responsibilities include the patent automation program, told us that Commerce intends

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to negotiate for a reduction in the total contract length from 18 to 8 years (through the completion of Phase Two), then readvertise and award a contract for maintenance of the system after Phase Two is completed.

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## Renegotiation Efforts Are Behind Schedule

Renegotiation efforts have fallen behind the timetable established in the January 1987 agreement. For example, because of the time necessary to prepare a detailed statement of work, the contract modification for the Phase One statement of work due to be signed on February 27 was not signed until May 18, 1987. As noted above, this modification also provided for negotiations to establish a separate total cost and fixed fee for Phase One. These negotiations were in process as of July 16, 1987. Also, the Phase Two statement of work due to be issued on March 5, 1987, to the contractor for consideration was still being reviewed within Commerce as of July 16, 1987. Commerce contracting officials were unsure when it would be ready to be sent to the contractor. Negotiations for Phase Two would begin sometime after the contractor reviews the revised statement of work.

According to Commerce's Deputy Assistant Secretary for Special Programs, the reason for the schedule slippage is in-house delays in completing detailed statements of work for both phases. Commerce and PTO contracting, program, and automatic data processing officials reviewed and commented on drafts of those statements of work. The Commerce Inspector General found deficiencies in the drafts and recommended numerous corrections and improvements before they proceeded further. In the Phase One draft, the Inspector General identified such problems as: insufficient detail of tasks and deliverables, inadequate definition of terms, confusing references, and unclear government responsibilities for accepting deliverables. The Inspector General found that the Phase Two draft: did not sufficiently address work already completed; was based on erroneous assumptions such as the timing of development and testing; significantly redefined the automated patent system; and had not implemented all the recommendations of previous Inspector General reports. These Inspector General recommendations had not been fully incorporated into the Phase Two statement of work as of July 16, 1987.

The development and review process has been more difficult and time-consuming than expected, requiring substantial effort to revise the original contract to an acceptable level of accuracy and specificity. Renegotiation efforts are now about 4 months behind schedule. Commerce's Deputy Assistant Secretary for Special Programs and PTO's Assistant

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Commissioner for Finance and Planning believe that Commerce will not meet its October 16, 1987, deadline. They estimate they will need 2 or 3 additional months past October to complete the Phase Two modification.

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## Unresolved Audit Findings May Delay Renegotiation

DCAA audits of the contractor for the automated patent system noted significant problems. For example, in October 1985, after an audit of the original contract, DCAA informed Commerce that the contractor was not in compliance with certain cost-accounting standards required by the contract and federal regulations. DCAA cited specifically the standards requiring consistency in estimating, accumulating, reporting, and allocating costs. Also, after a recent review of certain aspects of the contract, DCAA sent letters to the contractor (on May 1 and May 7, 1987) that cited problems with the contractor's accounting and billing systems, internal controls, and cost or pricing data submissions, among others.

In letters dated May 21 and May 22, 1987, the contractor agreed with the majority of DCAA's findings and recommendations. In most cases, the contractor agreed to institute and/or implement new policies and procedures to rectify the deficiencies. The major issue remaining is a disagreement between DCAA, which found that public vouchers are not prepared from the company's books and records, and the contractor, which responded that they are.

Discussions continue between DCAA and the contractor to resolve all remaining issues. Resolution is crucial to Commerce's ability to monitor the contract and its related costs. Commerce contracting officials also emphasized to the contractor (1) the need to correct the weaknesses found by DCAA, and (2) the importance of a high-quality proposal without similar deficiencies for Phase Two. The Phase Two proposal is subject to audit by DCAA. An inadequate contractor proposal could delay the approval process.

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## Conclusions

Commerce and the contractor have made some progress with the renegotiation of the current automated patent system contract. Commerce and the contractor agreed in January 1987 to address the Committee's specific requirements.

Slippages have occurred in meeting the January 1987 agreement timetable because it is taking longer than expected within Commerce to complete the detailed statements of work for the contract modifications. The Commerce Inspector General's audit findings have required substantive



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revisions in the statements of work. Also, DCAA's audit findings concerning the contractor's internal systems and procedures may affect the renegotiation process if the contractor's Phase Two proposal has deficiencies similar to those found in the audit of the original contract.

Commerce officials do not believe that they can meet their October 16, 1987, deadline. Several steps remain for completing the contract modification for Phase Two. First, Commerce must complete the Phase Two statement of work; the contractor must review it and submit a proposal that must be audited by DCAA; then Commerce and the contractor must hold contract negotiations.

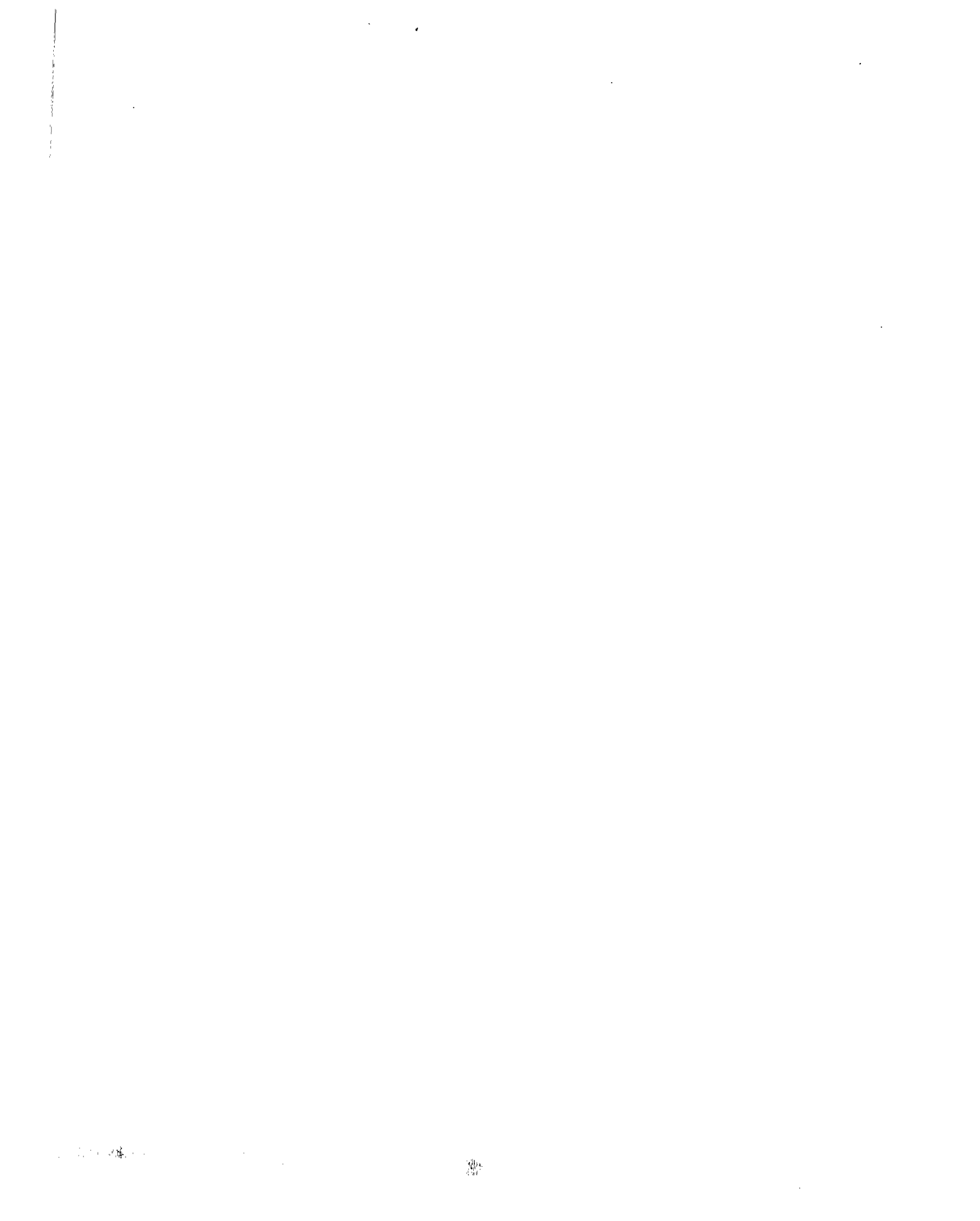
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Sincerely yours,



Ralph V. Carlone  
Director



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