

GAO

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

June 1993

DOD COMPUTER
CONTRACTING

Inadequate
Management Wasted
Millions of Dollars



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United States
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Information Management and
Technology Division

B-253431

June 25, 1993

The Honorable John Conyers Jr.
Chairman, Committee on
Government Operations
House of Representatives

Dear Mr. Chairman:

This report responds to your January 4, 1993, request that we review the activities of the Department of Defense's Office of the Deputy Comptroller for Information Resources Management, Systems and Services Directorate, during the period June 1988 through January 1991. This directorate was responsible for providing computer hardware, software, and related services to the Office of the Secretary of Defense (OSD) and its subordinate organizations. This review, which was begun by a GAO staff member detailed to your committee, was initiated after several allegations of inappropriate management and an internal Defense review. The Defense review disclosed that senior officials of the directorate may have participated in a number of questionable contracting activities, which resulted in unneeded equipment and services and excessive payments.

In discussions with your office, we agreed to complete the review and prepare a report summarizing its results. Specifically, we agreed to assess whether the directorate had adequate internal controls, followed proper contracting procedures, appropriately managed certain contracts, and needed several specifically identified training contracts. We also agreed to report any corrective actions taken after January 1991. We did not evaluate the operation or management of the new Systems and Services organization, other than to review the actions taken to address identified problems. Details of our objectives, scope, and methodology appear in appendix I.

Apart from our management review, the Defense Criminal Investigative Service is investigating criminal activities alleged to have occurred within Systems and Services during this time.

Results in Brief

The Systems and Services Directorate lacked internal controls and consistently exercised poor contract management in the 2 1/2-year period ending January 1991, during which the government spent almost \$16 million on unneeded or unjustified computer equipment and services.

Specifically, these problems resulted in (1) lost equipment and unnecessary warehouse costs worth almost \$1.5 million; (2) over \$9.5 million in contracts awarded for equipment, software, and services without required justification; (3) \$2.3 million spent for a resources management system and a related subsystem that were discontinued because they never worked properly; (4) payment of an estimated \$250,000 for services that may not have been received; (5) about \$2 million paid for excessive technical and maintenance services; and (6) more than \$200,000 spent annually on little-used computer training facilities.

The former director was replaced in January 1991, as part of a broader Department of Defense reorganization. The new director has taken actions to correct these problems and prevent them from occurring in the future. These actions have improved OSD's management over the manner in which it acquires information technology for its own use.

Background

During the 2 1/2 years covered by this review, the Systems and Services Directorate was responsible for providing information technology and supporting services to OSD and its 17 subordinate organizations, including the Assistant Secretaries of Defense for Health Affairs and for Program Analysis and Evaluation. Specifically, the directorate was responsible for supplying these groups with the computers and software they needed to meet their mission goals. The directorate also provided for computer maintenance and made computer-related training available to these groups.

During the review period, the Systems and Services Directorate reported to the Secretary of Defense through the Deputy Comptroller for Information Resources Management and the Defense Comptroller. In January 1991, as part of a broader Department of Defense reorganization, the Systems and Services Directorate was removed from the Deputy Comptroller for Information Resources Management's chain of command. It was reduced to a division and placed under the Directorate for Information, Operations, and Reports. This directorate reports to the Secretary of Defense through Washington Headquarters Services and through the director, Administration and Management.

Internal Controls Either Were Not Established or Not Implemented

Adequate internal controls ensure that methods and procedures adopted by management provide reasonable assurance that obligations and costs comply with applicable laws and that funds, property, and other assets are safeguarded against waste, loss, or misappropriation. During the period of our review, Systems and Services operated without certain required internal controls. In other instances it established controls but did not properly implement them. This situation led to an increased risk of contract abuse, a lack of budgetary accountability, and the loss of government property.

Lack of Separation of Duties Increased Risk of Contract Abuse

Federal policy states that key duties and responsibilities in authorizing, processing, recording, and reviewing transactions should be separated among individuals. The purpose of this safeguard is to ensure that no one individual controls all key aspects of a transaction or event, thereby reducing the risk of errors or irregularities.

Systems and Services had no such separation of duties; the former director had authority to influence all phases of contract award and management. Specifically, as the authorizing official, he chose the winning vendors of individual contracts. He also acted as project manager on one contract, performed contracting officer's technical representative functions on two procurement actions and, on at least one contract, prepared the technical specifications.

Further, under a special arrangement, this director also had control over contract administration. This special arrangement occurred through a January 19, 1990, memorandum of understanding between the Department of Defense Comptroller and an Army contract support group. Under this memorandum the former director became the immediate supervisor of the individual who administered all of Systems and Services' contracts. This individual's responsibilities included initiating documents to authorize payments for contractor services, ensuring that contract files were complete and accurate, and modifying the contracts. This organizational arrangement gave the former director authority over functions that established requirements, awarded contracts, and administered them.

After the reorganization in January 1991, these procedures and activities were changed. The new director said he limits his activities to those of authorizing official. He told us he does not prepare technical specifications or act as the project manager for any contracts. Further, on February 13, 1991, a new memorandum of understanding eliminated Systems and

Services' supervisory responsibility over the individual administering the contracts.

Contingency Fund Lacked Budgetary Accountability

Systems and Services maintained a revolving contingency fund under the control of the former director. This fund was used to finance joint OSD projects such as OSD-wide computer maintenance and technical services, and for unforeseen emergencies. From 1989 through 1991 this fund ranged from \$2.2 to \$7 million—approximately 5 to 17 percent of Systems and Services' operations and maintenance budget during this period. Because it was not reviewed by the OSD comptroller, and because OSD organizations were unable to identify how much was paid from the fund for their individual maintenance and service work, Systems and Services was able to purchase equipment and services through this fund without accounting for its expenditures.

According to the former Systems and Services director and budget officer, they informed the OSD organizations about the amount of money available in the fund, how it would be spent, and provided related financial information through a computer network. The budget officer also explained that agency representatives provided input regarding their maintenance needs, which in turn was used to determine how much money to put into the fund to cover OSD-wide maintenance expenses for the year.

However, according to the director of the Directorate for Information, Operations, and Reports, detailed fund expenditures were not reported to the individual organizations. He explained that money was obligated early in the fiscal year to individual maintenance contracts before the actual maintenance needs were fully identified. He added that as the year progressed, the OSD organizations were "charged-back" to cover the funds withdrawn from the contingency fund to pay the maintenance contractors, and that these charges were not necessarily in direct proportion to the services received.

Documentation and organization representatives support his position. Two representatives said that they were billed for their shares of costs without any detailed supporting documentation. As a result, these organizations could not verify that their shares of costs were accurate. In addition, representatives from three other organizations said that they could not determine how much money from the contingency fund had

been spent on their organizations, or how much was available for their additional needs.

The new director reviewed the fund in January 1991 and determined that it lacked accountability. Consequently, he eliminated it and allocated all contingency funds to the 17 OSD organizations. Each organization is now directly responsible for funding its own requirements, and is directly charged for services received.

Government Property Lost Through Failed Vendor Accounting

Federal policy states that access to resources and records should be limited to authorized individuals, and that a periodic comparison should be made of the resources and the recorded inventory to determine if the two agree. Two contractors did not properly account for their government inventories, resulting in the loss of government computers and related equipment.

On August 15, 1988, Systems and Services awarded a \$2.3-million, 4-year contract for management of automated data processing equipment that was declared excess. The contractor was responsible for transporting the equipment from excessing organizations to its warehouse, storing the equipment, redistributing it to other organizations, or disposing of it, and maintaining appropriate records of these activities.

The former director said that the contractor managed these activities by keeping inventory records and conducting annual inventories of the equipment. However, the new management found that this contractor did not properly maintain accountability for these government assets. The new director took his own inventory and compared it with the contractor's records. This inventory showed that only half (400 of the 800 items in the contractor's records) could be located, and that an additional 2,100 items in the warehouse were not listed on the contractor's inventory. The new director told us he was unable to determine whether equipment had actually been lost or if this was just a recordkeeping problem. When he identified these problems he terminated the contract, obtained a government-leased warehouse staffed by federal employees, and established procedures that made the individual OSD organizations accountable for their own equipment. He reported that the warehouse change will save about \$720,000 annually, and that the new procedures will provide better accountability over federal equipment.

Another contractor provided a variety of automated data processing-related services to OSD. To assist it in providing these services, the government provided this contractor with about \$1 million of government equipment, which it was responsible for safeguarding. However, a June 11, 1991, inventory revealed that approximately \$750,000 of this equipment could not be located. The new director referred this information to the Defense Criminal Investigative Service in June 1991. A Defense Criminal Investigative Service official told us that because of a lack of complete, accurate, supporting records, the service is not actively pursuing this case. He added, however, that if additional evidence becomes available as a result of two related, ongoing investigations, the service will consider initiating an investigation.

Contracting Procedures Were Not Followed

Federal Information Resources Management Regulation 201-20.103-2 & 3 requires agencies to prepare a requirements analysis justifying the planned acquisition before awarding a contract. However, in four instances involving over \$10.7 million in procurement actions, Systems and Services awarded contracts without properly documenting that the equipment or service was needed.

Interdepartmental Procurement Request

On June 30, 1989, Systems and Services sent a military interdepartmental procurement request to the National Security Agency, asking for a sole-source purchase of \$990,000 worth of workstations and related computer equipment. In these situations the requesting organization is responsible for ensuring that the equipment request is justified. The requester is supposed to maintain internal records that justify the requirement and show the purpose of the equipment, and the intended installation site. However, none of this information was in the contract files. Instead, a memorandum in the file from a Systems and Services branch chief stated that the appropriate requirements review and alternatives analysis had not been completed.

The branch chief said that while he was away on vacation, the former director approved this procurement without the supporting documents. The former director said he did not remember seeing his branch chief's memorandum in the file. He also stated that he did not specifically remember the contract, but assumed it was appropriately justified.

File Servers

On January 10, 1990, Systems and Services arranged for the sole-source purchase of file servers valued at \$293,000. Contract documents stated that the file servers were needed to support the workstations mentioned above. To the extent the requirements for the workstations on the previous contract were not justified, the justification for this procurement was invalid.

Workstations

On July 16, 1990, the former director awarded a \$9.2-million contract to a corporation for 300 new workstations and 405 kits to upgrade older model workstations. Although Systems and Services asked the OSD organizations to justify their needs in February 1990, it awarded this contract before it received the required justification from some organizations, and without receiving justification from others.

The former director told us that the required documentation had been completed and he had personally reviewed it before awarding the contract. This statement is, however, inconsistent with contract documents and statements from Systems and Services and OSD organization representatives. No written documentation supporting the need for the 705 workstations and upgrade kits was found in the contract file. While 11 informal requests had been sent electronically to Systems and Services, none had been received until at least 1 month after the contract was awarded. Two Systems and Services officials, responsible for reviewing the documents that justified the need for the contract, told us such justification was never prepared; they said the former director wrote the requirements for the contract without input from the using organizations.

Representatives from eight OSD organizations we contacted said they never formally requested this equipment. Four of these representatives said that, instead, Systems and Services called them after the equipment had been purchased and encouraged them to take it. The other four representatives said they did not use this brand of equipment and, thus, had no need for it.

The new director of Systems and Services determined that many of these workstations were not needed. He terminated the contract on August 7, 1991, after over \$8 million had been spent. This action saved about \$1.2 million that remained on the contract.

Special Services

One contractor was awarded a \$601,000 task order for fiscal years 1990 and 1991 to (1) produce "Point of View," an electronic newsletter for users on a computer network; (2) catalogue all of the software provided by a specific vendor that was being used by OSD; and (3) establish a help desk for this brand of computer. Current Systems and Services officials stated that justification for these tasks did not exist, and that they probably cost too much.

The newsletter was put on the computer network once a month, and involved no printing expense. The OSD catalogue of the software included non-job-related items such as computer games for Space Fighter, Pac-Man, blackjack, and Chinese chess. The help desk was never staffed or put into operation.

The new Systems and Services director reviewed this contract and questioned the need for these services. He terminated the contract on January 14, 1991, after over \$250,000 had been spent. This action saved \$350,000 that remained on the contract.

Poor Contract Management Resulted in Significant Waste

OSD Administrative Instruction No. 56 states that Systems and Services shall assess and manage computer and office automation resources. It specifies that such management should include (1) providing technical guidance and direction for the development of systems to ensure that the requirements are satisfied by the contractor, (2) monitoring the expenditure of funds to ensure that they are warranted, and (3) reviewing and evaluating the OSD organization's requirements to ensure that they are technically feasible. Because Systems and Services did not properly manage its contracts, it accepted inadequate products, paid for services that may not have been received, and purchased services that were not required.

Inadequate Products Accepted

During the period of our review, Systems and Services paid one contractor through task orders to create and maintain one project and develop another one. The new management found that neither project worked properly and terminated both. The projects are described below.

During a 2-year period starting in October 1988, this contractor was paid \$2 million to develop and maintain a resources management system for processing and tracking procurement actions within the Systems and Services Directorate. This system was supposed to provide support for

such things as recording, processing, and tracking fiscal information; preparing the budget; financial planning for future operations; and inventory equipment management and control. The Systems and Services budget officer during this period told us that she worked with the contractor to obtain the required system. She said the components were being delivered as requested, but not all had been effectively integrated. For example, she said that while the budget component was integrated with OSD's budget and finance system, the requisition and reconciliation components were still being batch-processed via modem, and information from the OSD organizations had to be obtained via floppy disks.

Systems and Services' new management found that it took seven people to support the system; for one OSD organization alone, only 30 of 80 accounting transactions were on the system; records for reconciling OSD-wide obligations were 2 years behind; and a \$500,000 task order had been awarded to the contractor to continue developing the system during fiscal year 1991. The new director concluded that the system was not working properly and that it would cost too much to make it usable. He discontinued the system and canceled the \$500,000 task order on January 14, 1991. A Systems and Services employee subsequently used commercial software and spent less than 2 weeks to develop a less complex system that met their procurement tracking needs.

This contractor was also tasked with developing an Interim Requisition Processing System so that it could be used to create forms and record relevant information. This effort started in 1989 and took approximately 3 months to complete. Systems and Services accepted the contractor's system even though it had not been properly documented. A Systems and Services branch chief estimated that the 7th Communications Group spent approximately 1 staff year in an effort to document the system. When the new director arrived, he determined that the system did not function as required and was not adequately documented. This task order was canceled on January 14, 1991, after a \$300,000 investment.

Payments Made for Services That May Not Have Been Received

During the period of our review, Systems and Services also paid a contractor to provide maintenance on its equipment. The contract specified that payment was to be made on the basis of materials used and time spent on this activity. Systems and Services routinely paid for the time and materials billed by this contractor without verifying that the services had been performed or that the bills were accurate. This resulted from lack of procedures and poor contract management.

Systems and Services had no policy that required the organization receiving the service to certify in writing that the task had actually been completed. Further, Systems and Services' contracting officer's technical representative did not properly verify that the contractor had completed tasks under the time and materials contract. Consequently, Systems and Services paid these bills without assuring that they were accurate.

After the reorganization, Systems and Services' new management determined that the existing contract management was inadequate. They implemented new procedures that require both the receiving OSD organizations and the contracting officer's technical representative to certify that the billed tasks have been completed before the contractor is paid.

The new director conducted a preliminary review, which indicated that as much as \$250,000 was paid for services that may not have been received. He referred this case to the Defense Criminal Investigative Service for further investigation. The Service is continuing its investigation and is coordinating its activities with the U.S. Attorney's Office regarding potential criminal irregularities.

Unneeded Services Procured

On at least three contracts, Systems and Services paid for unnecessary or excessive work. Three factors contributed to this problem. First, tasks were ordered against time and materials contracts, which were renewed year after year without assessing if the need still existed. Second, these task orders were paid from the contingency fund, where OSD organizations could not determine how much was spent for their individual maintenance and service work. Third, Systems and Services did not manage the contracts to ensure that the service was needed.

Systems and Services scheduled excessive maintenance under the time and materials contract. Because the maintenance was paid from the contingency fund, OSD organizations could not identify how much they were paying for their individual service. Defense officials reported that each organization's costs were arbitrarily derived by the systems and support staff, rather than being based on usage. The new Systems and Services director implemented a procedure requiring the individual organizations to identify and pay for the cost of the services provided to them by this contractor. When the individual organizations realized the actual cost of the support they were receiving, they reduced their

requirements. The new director estimated that this reduction saved about \$700,000 in annual maintenance expenses.

Another contract provided facility management support for computer equipment used throughout OSD. The total value of related work tasks for 1991 was \$880,000. We asked the former director if he had ever reviewed these tasks to determine if they were still needed. He said he had not, that it was the responsibility of his contracting officer's technical representative to conduct program reviews. The new management performed a program review of this contract and determined that some of the tasks were overstaffed and others unnecessary. Consequently, these tasks were canceled or modified, resulting in savings of \$293,000 that would have been paid for services during the remaining 9-month period in 1991.

The third contract was awarded on April 1, 1988, for technical support. It contained option years through 1991. This contract cost from \$1 million to \$2 million annually, based on the amount of service provided. The former director confirmed that the contract had been awarded prior to his arrival. He added that he relied on budget information to estimate the OSD organizations' support needs in awarding the option years.

The new director assessed the OSD-wide need for technical support under this contract by surveying all OSD organizations and obtaining estimates of their needed technical support. Following this assessment, he reduced this contractor's technical support, which resulted in a \$1-million reduction in the fiscal year 1991 contract option.

Unnecessary Training Contract Options Exercised

One of the Systems and Services Directorate's responsibilities was to provide computer-related training to OSD personnel. However, over the years, options on training contracts were exercised without follow-up to ensure that the training was needed or used. After its reorganization in 1991, Systems and Services' new management contacted OSD users regarding their training needs and found that three of these training contracts were unnecessary. Consequently, it terminated the contracts and closed the facilities, resulting in savings of \$200,000 in contractor fees and \$260,000 in government-furnished equipment.

The three contractors maintained training facilities at Silver Spring, Maryland; Buzzard's Point, Washington, D.C.; and Falls Church, Virginia.

The use being made of each facility when these contracts were terminated is described below.

One contractor received about \$200,000 per year to operate a training facility in Silver Spring, Maryland. The new director of Systems and Services said that this facility trained only eight OSD personnel during the first quarter of 1991. Other students were from non-OSD-related groups, such as contractors performing Systems and Services work and the 7th Communications Group. The new director terminated the task order in March 1991, eliminating the \$200,000 annual fee. He also reassigned government-owned computers and equipment worth over \$130,000 that had been furnished to the contractor.

The second contractor used government-furnished equipment including workstations, a disk drive, and two printers to provide training at a Defense facility at Buzzard's Point, Washington, D.C. The new director said he found that no one was being trained at this facility. He closed this training center in April 1991, and transferred the government equipment to the Pentagon.

The third contractor trained about one person per week at a warehouse in Falls Church, Virginia. This center and the warehouse was closed in April 1991. Government-owned equipment worth over \$130,000 was reassigned to other uses.

The former director said that supporting documentation had been prepared to justify the training made available to the OSD organizations. However, he also told us that he was unaware that a training facility existed at Buzzard's Point during his years at Systems and Services. We found no supporting documentation in the contract files for any of these training facilities.

Conclusions

The Systems and Services Directorate inappropriately managed contracts and acquired equipment during the 2 1/2-year period ending January 1, 1991. This resulted in millions of dollars of equipment purchases that were not justified, lack of control over government equipment, and unnecessary training contracts.

While the scope of our audit was limited, this breakdown in controls suggests the potential for similar problems elsewhere and demonstrates a need for more aggressive OSD oversight. Preventing the recurrence of these

types of problems in the future will depend on Defense's vigilant use of sound internal controls and effective contract management.

Agency Comments and Our Evaluation

As requested, we did not obtain agency comments on a draft of this report. However, we provided a summary of the facts to officials from the Directorate for Information, Operations, and Reports; the former and new directors of Systems and Services; and officials from the Defense Criminal Investigative Service. The director of the Directorate for Information, Operations, and Reports, and the new director of Systems and Services agreed with our facts and termed the former director's written statement (see below) as generally inaccurate. The Defense Criminal Investigative Service also agreed with our facts.

The former director of Systems and Services declined to discuss the facts with us; instead, he provided a written statement, which disagreed with many of our facts. He also wrote that the new Systems and Services management had the benefit of several contract actions that his office had initiated and was in the process of evaluating at the time of the reorganization. During our audit he also told us that when he took over Systems and Services in June 1988, the directorate had serious personnel and management problems, and that one reason he was assigned to the directorate was to correct these problems. The former director's written statements and our evaluation follow.

Separation of Duties

The former director said he was not appointed and did not act as an authorizing official or a contracting officer's technical representative. He also said he did not write technical specifications in their entirety; the memorandum of understanding addressed the contract function, not payments, and that this authority was changed before January 1991. However, the contracting documents contain his signature as the authorizing official, and his employees told us that he performed the duties of the contracting officer's technical representative and wrote the technical specifications for several contracts. We changed the report to clarify that he had control over documentation to initiate payments, rather than over the payments themselves. Finally, the change in authority was dated February 13, 1991.

Contingency Fund

The former director said the fund was not really a contingency fund, but stated that it was used for unknown/undefinable organizations. He added

that an organization line item "contingency" was in budget material seen by OSD comptroller staff. Records show that this was a contingency fund. Further, the Systems and Services budget officer during the period of our review stated that this was a contingency fund. She also stated that it was consolidated with other funds for budget submission and thus could not be reviewed by the OSD comptroller.

Workstations

The former director stated that since only 7 of the 17 OSD organizations used the brand of workstations we addressed, we may have used statements from the non-using organizations to support a statement that the equipment was not formally requested. He also said that his office had already determined that the entire contract would not be needed before the new director assumed responsibility, thus it was not surprising that this director lowered the total amount of the contract through formal documentation. We modified our report to show that four organizations that used this brand of workstation never formally requested them. The former director provided no documentation showing that his office had considered lowering the amount of this contract.

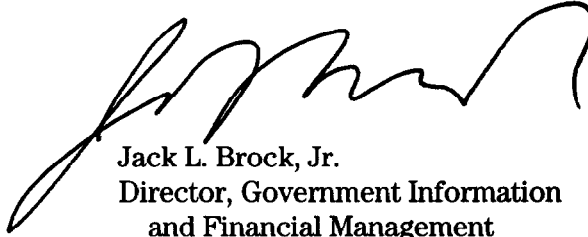
Contract Management

The former director stated that since the resources management system was not started until November 1989, there would not have been 2 years of data for reconciliation until November 1991. The new director told us that auditors were attempting to reconcile 1988 data on the system when he assumed responsibility in January 1991.

We conducted our work from February through May 1993, in accordance with generally accepted government auditing standards. Unless you publicly announce the contents of this report earlier, we plan no further distribution of it until 10 days from the date of this letter. We will then send copies to the Secretary of Defense; copies will also be made available

to others upon request. Please contact me at (202) 512-6406 if you have any questions about this report. Major contributors to this report are listed in appendix II.

Sincerely yours,



Jack L. Brock, Jr.
Director, Government Information
and Financial Management

Objectives, Scope, and Methodology

In January 1993, the Chairman, House Committee on Government Operations, asked us to complete a review of the management practices that occurred from June 1988 through January 1991 in the Department of Defense, Office of the Deputy Comptroller for Information Resources Management, Systems and Services Directorate. The Committee review was prompted by various allegations of inappropriate management and by an internal Defense review, which disclosed that senior officials of the directorate may have participated in numerous questionable contracting activities. The Committee began its work with a staff member detailed from GAO. When the staff member's temporary assignment expired, the Chairman requested that we complete the work and prepare a report summarizing the results.

In subsequent discussions with the Chairman's office, we agreed to assess whether the directorate, during the period in question, (1) had adequate internal controls, (2) followed proper contracting procedures, (3) appropriately managed certain information technology contracts, and (4) needed specifically identified training contracts. We also agreed to report on any corrective actions taken by Defense after the period of our review.

To accomplish our first objective we reviewed the directorate's internal controls and contracting procedures and assessed their adequacy. We asked responsible officials who had worked in the directorate what internal controls were used to ensure appropriate contract award and management, and assessed the effect of inadequate internal controls and contracting procedures on specific contracts.

We analyzed seven contracts that had been identified by Defense's internal management review as having problems. Two of these contracts were for training and the remaining five were for computer equipment and related services. We reviewed the contracts to ascertain whether required documentation justifying their award had been prepared. We also talked to contracting officials (including the former director of Systems and Services) and users, and reviewed contract files to determine how the contracts were initiated and managed, and to assess whether the resulting equipment and related services were needed.

We also obtained statements from the director of the Directorate for Information, Operations, and Reports, and the current director of Systems and Services, regarding actions taken to address the problems identified.

We reviewed supporting documentation to assess the validity of these statements.

We conducted our work primarily at the Systems and Services Directorate (now a division) in Arlington, Virginia. Additional work was conducted at other organizations within the Office of the Secretary of Defense, Washington, D.C.

As part of our review we relied on workpapers that were developed by the GAO staff member detailed to the Committee for its initial investigation. These workpapers were independently reviewed by GAO management and were determined to meet GAO's auditing standards.

Major Contributors to This Report

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