

GAO

Report to the Ranking Minority Member,  
Subcommittee on Oversight of  
Government Management and the  
District of Columbia, Committee on  
Governmental Affairs, U.S. Senate

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October 1995

# INTERAGENCY CONTRACTING

## Controls Over Economy Act Orders Being Strengthened







United States  
General Accounting Office  
Washington, D.C. 20548

National Security and  
International Affairs Division

B-258879

October 20, 1995

The Honorable Carl Levin  
Ranking Minority Member  
Subcommittee on Oversight of Government Management  
and the District of Columbia  
Committee on Governmental Affairs  
United States Senate

Dear Senator Levin:

This report responds to your concerns about abuses of interagency orders for goods and services under the Economy Act. As you requested, we examined the early impact of the Department of Defense's (DOD) policy changes for interagency orders on the Department of Transportation's Volpe National Transportation Systems Center. We also reviewed recent Coast Guard initiatives and legislative changes extending statutory requirements on interagency orders to other federal agencies.

## Results in Brief

Because of past practices, the National Defense Authorization Act for Fiscal Year 1994 required the Secretary of Defense to issue regulations that strengthened controls over DOD's interagency orders for goods and services. In a February 1994 memorandum, and in advance of the statutorily required regulations, the Secretary took additional steps to increase DOD's interagency transaction controls by requiring, among other things, that DOD's interagency orders be (1) as convenient and cheap as other alternatives and (2) approved at a level no lower than senior executive service, general officer, flag officer, or activity commander. In November 1994, the Coast Guard independently developed reforms that paralleled these DOD initiatives.

DOD is still adjusting to the changes introduced by Congress and the Secretary. There is an abundance of guidance available to Air Force, Army, and Navy contracting activities, but a sample of fiscal year 1995 Volpe Center purchases made by the services showed that not all files contained the information required by the Secretary's memorandum. In addition, DOD has not yet implemented a statutorily mandated monitoring system for its interagency purchases. The monitoring system is currently scheduled for implementation in October 1995.

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DOD contracting with the Volpe Center has been declining since fiscal year 1992. While it is difficult to pinpoint exact causes for the downward trend, more recent declines appear to be a result of DOD's implementation of the more restrictive environment for interagency orders. Likewise, a similar recent decline in Coast Guard purchases at the Volpe Center appears to be related to the introduction of the Coast Guard reforms.

The Federal Acquisition Streamlining Act of 1994 (FASA) generally extended the restrictive interagency transaction controls applicable to DOD to other federal agencies. The implementing draft regulation, while consistent with FASA, is not as stringent as the DOD or Coast Guard cost policies.

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## Background

The Economy Act, as amended (31 U.S.C. 1535), authorizes the head of an agency to place an order with another agency for goods or services if, among other requirements, a decision is made that the items or services cannot be obtained by contract as conveniently or cheaply from a commercial enterprise. The interagency ordering practice authorized by the Economy Act, sometimes referred to as "contract off-loading," can save the government duplicative effort and costs when appropriately used. Examples of appropriate use may include circumstances of one agency already having a contract for goods and services similar to those needed by another agency, or an agency having unique capabilities or expertise that qualify it to enter into or administer a contract.

In July 1993, the Subcommittee on Oversight of Government Management, Senate Governmental Affairs Committee, held a hearing to examine the practice of off-loading at federal agencies and the abuses of this practice. Its hearing record,<sup>1</sup> which included testimony from the Inspectors General of DOD, the Department of Energy, and the Tennessee Valley Authority, was critical of DOD's and other agencies' off-loading practices. Subsequently, the National Defense Authorization Act for Fiscal Year 1994 required the Secretary of Defense to prescribe regulations governing DOD's use of the Economy Act that included specific statutory limitations intended to rectify identified abuses.

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## The Volpe Center

The Volpe Center is a federally owned and operated facility located in Cambridge, Massachusetts, and was established in 1970 to fulfill the need

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<sup>1</sup>Off-loading: The Multimillion Dollar Loophole in Government Contracting, Hearing Before the Subcommittee on Oversight of Government Management, Committee on Governmental Affairs, U.S. Senate, July 30, 1993.

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of the newly formed Department of Transportation for an in-house systems research capability. Since then, the center's research, analysis, and project management expertise has been applied to a wide variety of transportation and logistics problems. Its only funding is through formal reimbursable agreements negotiated with individual agencies for specific tasks.

Initially, the center's services were provided almost exclusively to the Office of the Secretary of Transportation and the operating administrations within the Department of Transportation. As its capabilities evolved and its systems approach became better known, demand grew within non-Department of Transportation agencies. Through a formal memorandum of understanding with DOD, the Secretary broadened the center's mission in 1985 to include work on transportation and logistics problems facing other agencies, including the Joint Chiefs of Staff and the U.S. Transportation Command. Similar arrangements were made with civilian agencies.

The Volpe Center's current labor pool consists of about 1,500 personnel evenly divided among 3 labor categories: federal employees, on-site contractor employees, and off-site contractor employees. On-site contractors provide services in computer analysis, technical information support, and documentation support. The off-site contractor employees comprise a "multiple contractor resource base," which allows quick, competitive access to a broad range of high technology capabilities and skills needed to meet the Volpe Center's programmatic requirements. Volpe Center contracting is regulated by the Federal Acquisition Regulation.

In response to an audit conducted by the Department of Transportation's Inspector General, the Volpe Center issued formal work acceptance criteria in February 1995. According to Volpe Center management, the criteria are designed to assure that the center will not accept projects unless it can make substantive contributions derived from its status as part of the federal government. Examples of substantive contributions include project definition and planning in cooperation with the requesting agency, and support of contracts awarded and administered by the Volpe Center.

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## DOD Cost Initiative Expanded Statutory Requirements

In advance of promulgating regulations, the Secretary issued a policy memorandum in February 1994 that imposed limitations on the use of Economy Act orders by DOD activities. The Secretary's policy, which addressed Economy Act orders released outside of DOD for contract action, was, however, more stringent than either the National Defense Authorization Act for Fiscal Year 1994 or the Economy Act in the area of cost considerations by requiring a determination that the supplies or services cannot be provided "as conveniently and cheaply" by contracting directly with a private source. The Authorization Act did not address this cost issue and the Economy Act uses the phrase "as conveniently or cheaply." The Secretary's use of the "and" rather than the "or" introduces more cost analysis into the decision-making process.

The Secretary also changed the level of approval authority for Economy Act purchases. Instead of having contracting officers or other officials designated by the agency head approve Economy Act transactions, the Secretary's memorandum placed the approval level no lower than a senior executive service official, a general or flag officer, or an activity commander.

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## Coast Guard Has Initiated Cost Reforms Similar to DOD

The Coast Guard, which is a component of the Department of Transportation, has acquired services from the Volpe Center. In November 1994, the Coast Guard issued an instruction providing guidance on its use of the center. The instruction established a review, justification, and approval process to ensure that acquisition of Volpe Center services are in the Coast Guard's best economic interest. The instruction designates the Director of Finance and Procurement, a senior executive service position within the Office of the Chief of Staff, as the approving official for all Coast Guard work performed through the center.

The guidance requires a demonstration that the cost to use the Volpe Center is at least roughly comparable to commercial cost. To document this comparability, Coast Guard sponsors must develop an independent estimate of expected project costs using recognized techniques such as engineering analysis, market research, or application of actual cost data from prior projects.

While the Coast Guard instruction acknowledges that the Volpe Center offers convenience, it is the Coast Guard policy that the center shall be used when there are clear economic, technical, and mission-essential reasons for doing so. For example, officials informed us that in one area of

the country the Coast Guard is now completing 5 years of environmental compliance and restoration work with the Volpe Center. They explained that the center's support was critical in the early years of this work for the Coast Guard to gain an understanding of the various technologies involved in restoring areas at Coast Guard installations that were contaminated. Coast Guard officials said it has acquired the technical expertise and it is now ready, at least in that area of the country, to transition away from the center for this work and contract directly with private companies.

## DOD Is Still Adjusting to Contracting Changes

The Air Force, Army, and Navy have each taken a different approach to implementing the Secretary's policy memorandum. Collectively, however, they are producing similar mixed results. While there is considerable up-to-date guidance available to contracting officials on interagency purchases, not all DOD files on Volpe Center projects we reviewed contained required information. In addition, DOD has not yet implemented a statutorily mandated monitoring system for interagency purchases; the monitoring system is currently scheduled for implementation in October 1995.

## Service Guidance Is Abundant

The Air Force introduced the Secretary of Defense's policy changes in June 1994 through a revision to its Federal Acquisition Regulation Supplement. The supplement states that the Air Force shall not place an order with another agency unless adequate supporting documentation, including a Determination and Finding (D&F)<sup>2</sup>, is prepared. The D&F must be approved at a level no lower than senior executive service, flag or general officer, or activity commander. The activity's contracting office is required to retain a record copy of each D&F in a central file. The supplement offers a model format for the D&F, which requires that 12 specific findings be listed, including 1 that states "the supplies or services cannot be provided as conveniently and more economically by private contractors under an Air Force contract."

The Army implemented the Secretary's policy changes in an August 1994 policy letter from the Office of the Assistant Secretary, Army Contracting Support Agency. The letter states that before an Economy Act order for supplies or services is released outside DOD for contracting action, a written determination prepared by the requiring activity that addresses the

<sup>2</sup>A D&F documents the findings and conclusion of the approving official and generally addresses the following issues: legal authority, adequacy of funds, convenience, cost, expertise of the servicing agency, contract administration compliance, and bona-fide need. Other supporting documentation, such as an independent government estimate, is used in the preparation of the D&F.

elements in the Defense Secretary’s memorandum shall be approved by the head of the requesting agency or their designee. The D&Fs are required to be prepared in the same format required by the Air Force, to include that “the supplies or services cannot be provided at the time required and more economically by contractors under an Army contract.”

In contrast to the Air Force and Army’s delegation of approval authority, the Navy initially did not delegate approval authority below the Assistant Secretary of the Navy for Research, Development, and Acquisition. Toward the end of 1994, the Assistant Secretary delegated approval authority to the Deputy for Acquisition and Business Management.<sup>3</sup> In January 1995, as permitted by the Secretary of Defense’s memorandum, the Deputy redelegated authority to approve D&Fs to eight activities with contracting authority. However, approval authority for Economy Act orders placed with the Volpe Center and with agencies not subject to the Federal Acquisition Regulation was retained by the Deputy for Acquisition and Business Management.

**Some Project Files Lacked Required Documentation**

Despite efforts by the services to strengthen controls over Economy Act purchases, our review of fiscal year 1995 Air Force, Army, and Navy projects with the Volpe Center indicated that the controls were not fully implemented. Of the 13 purchase requests we reviewed, 7 lacked approved D&Fs. The results of our review are summarized in table 1.

**Table 1: Summary of Fiscal Year 1995 Air Force, Army, and Navy Project File Reviews**

	<b>Air Force</b>	<b>Army</b>	<b>Navy</b>	<b>Total</b>
Dollar value of purchases	\$1,770,291	\$597,890	\$3,211,900	<b>\$5,580,081</b>
Number of purchases reviewed	6	2	5	<b>13</b>
Number with approved D&Fs	3	1	2	<b>6</b>
Number without approved D&Fs	3	1	3	<b>7</b>

In two of the three Air Force cases where a D&F was not prepared, the project managers were not aware of the requirement to prepare a D&F; in the other case, a draft D&F was prepared by the requiring activity, reviewed by a contracting officer, but never completed or signed. In the Army case where a D&F was not prepared, Army officials had no excuse other than

<sup>3</sup>The Deputy for Acquisition and Business Management was formerly known as the Deputy for Acquisition Policy, Integrity, and Accountability.



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they “just missed it.” One official suggested that some Army activities may not have understood the August 1994 policy letter. In one of the Navy cases without an approved D&F, ordering officials justified the transfer of 1995 funds on the basis of a D&F that covered 1993 and 1994 funding; subsequent to the transfer of funds, reviewing officials rejected this justification. The other two Navy cases involved purchases by a Marine Corps ordering activity. Similar to the Army case, Marine Corps officials explained that, regarding the preparation of D&Fs, the purchases “just fell through the cracks.”

The documentation for services’ projects with approved D&Fs showed different approaches to meeting the Defense Secretary’s requirement to elevate the consideration of cost. The Air Force D&Fs mainly emphasized that the estimated general and administrative expense rate of 9 percent charged by the Volpe Center appeared reasonable and did not exceed the actual cost of entering into and administering the interagency agreement under which the order is filled. The Air Force documentation also showed that business reviews were performed by the contracting officers; the business reviews indicated that independent government cost estimates had been completed.

The documentation for the approved Army project computed the dollar value of the administrative fee and included an “information paper” prepared for the general officer who signed the D&F. The information paper indicated that the project would be transitioning from Volpe Center support to the Army’s on-site contractor support in about 4 months.

The approval for the two Navy cases involved purchases by a Marine Corps ordering activity different from the one above, which did not have approved D&Fs. These purchases were covered by a D&F prepared shortly after the Secretary’s memorandum, but approved under the criteria in effect before the memorandum. Thus, the D&F did not contain a finding on the cost comparison cited in the Secretary’s memorandum. However, Navy officials said that they concurred with approvals such as these because, at that time, no new detailed implementing guidance was available to ordering activities.

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## DOD Monitoring System Not Yet Established

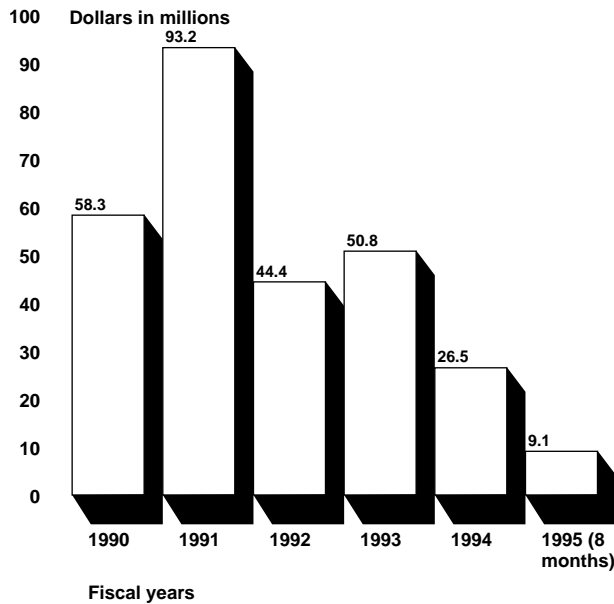
The National Defense Authorization Act for Fiscal Year 1994 directed that DOD establish a monitoring system for Economy Act purchases not later than 1 year after the November 30, 1993, enactment of the act. That monitoring system has not yet been implemented. An official from the

Office of the Under Secretary of Defense for Acquisition and Technology informed us, however, that the monitoring system has been developed and is now awaiting approval. The monitoring system is currently scheduled for implementation on October 1995.

## Dollar Value of DOD and Coast Guard Orders at Volpe Center Has Decreased

DOD Economy Act orders placed with the Volpe Center peaked in fiscal year 1991 at \$93.2 million, which accounted for about 39 percent of the center's budget. By fiscal year 1994, DOD funding dropped to \$26.5 million, which accounted for about only 13 percent of the center's budget. Funding transfers for the first 8 months of fiscal year 1995 indicate that DOD funding will only be one-half of fiscal year 1994 funding. The funding data are summarized in figure 1.

**Figure 1: Comparison of DOD New Obligation Authority Transferred to Volpe Center, Fiscal Years 1990-95** (as of May 31, 1995)

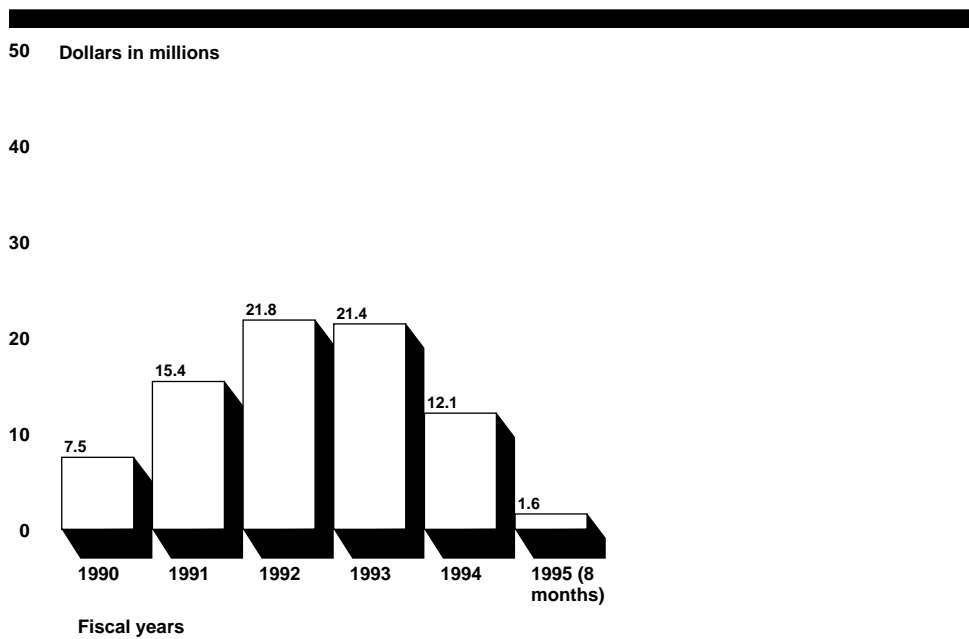


It is difficult to pinpoint exact causes for the downward trend. However, the more recent declines may be a result of the 1993 Subcommittee hearing, resulting legislation, and the 1994 implementation of a more restrictive contracting environment by the Secretary of Defense.

### Dollar Value of Coast Guard Orders at Volpe Center Has Also Decreased

Coast Guard orders placed with the Volpe Center reached their highest levels in fiscal years 1992 and 1993 when over \$21 million in new obligation authority was transferred each year. Funding dropped by almost half in fiscal year 1994. Fiscal year 1995 new obligation authority may be about half of the fiscal year 1994 total. The funding data are summarized in figure 2.

**Figure 2: Comparison of Coast Guard New Obligation Authority Transferred to Volpe Center, Fiscal Years 1990-95**  
(as of May 31, 1995)



As with the DOD data, it is difficult to identify exact causes for the downward trend. However, the November 1994 instruction with its cost and approval requirements may have been a contributing factor.

### FASA Extends Reforms to Non-DOD Agencies

FASA required that the Federal Acquisition Regulation be revised to include statutory requirements governing the exercise of Economy Act authority. The requirement is virtually identical to that required of DOD by the National Defense Authorization Act for Fiscal Year 1994. In March 1995, a proposed draft regulation was published in the Federal Register. The proposed regulation requires a determination that the ordered goods or services cannot be provided by contract as conveniently or cheaply by the

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requesting agency from a commercial enterprise. FASA did not require the more stringent “and” language applicable within DOD.

The regulation authorizes determination approval authority to reside with the contracting officer or another official designated by agency regulation, except that if the servicing agency is not covered by the Federal Acquisition Regulation, approval authority may not be delegated below the senior procurement executive of the requesting agency. Such procedures are consistent with FASA.

FASA also requires that by mid-October 1995 the Administrator for Federal Procurement Policy establish a monitoring system for Economy Act purchases for Federal civilian agencies, similar to the requirement for DOD.

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## Agency Comments

In commenting on a draft of this report, both the Departments of Defense and Transportation concurred with the report. Both suggested some technical changes to the draft, and we have incorporated them, where appropriate. DOD’s comments are presented in appendix I. The Department of Transportation’s comments were provided orally.

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## Scope and Methodology

We interviewed management officials and examined project management and budget documents, statements of work, cost summaries, military interdepartmental purchase requests, project plan agreements, and other program documentation. We performed work at the Department of Transportation’s Volpe National Transportation Systems Center, Cambridge, Massachusetts, and Headquarters, United States Coast Guard, Washington, D.C. We also contacted policy representatives within the Office of the Assistant Secretary of the Air Force for Acquisition; the Office of the Assistant Secretary of the Army for Research, Development, and Acquisition; and the Office of the Assistant Secretary of the Navy for Research, Development, and Acquisition. Our review was performed in accordance with generally accepted government auditing standards and includes information obtained through May 1995.

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We are sending copies of this report to the Chairman, Subcommittee on Oversight of Government Management and the District of Columbia, Senate Committee on Governmental Affairs; other interested congressional committees; and the Secretaries of Defense and Transportation. Copies will also be available to others on request.

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Please contact me at (202) 512-4587 if you or your staff have any questions concerning this report. Major contributors to this report were Charles W. Thompson, Paul M. Greeley, and Paul G. Williams.

Sincerely yours,

A handwritten signature in black ink that reads "David E. Cooper". The signature is written in a cursive style with a large, prominent "D" and "C".

David E. Cooper  
Director, Acquisition Policy, Technology,  
and Competitiveness Issues

# Comment From the Department of Defense



ECONOMIC  
SECURITY

**ASSISTANT SECRETARY OF DEFENSE**

3300 DEFENSE PENTAGON  
WASHINGTON DC 20301-3300



12 SEP 1995

Mr. David E. Cooper  
Director, Acquisition Policy, Technology,  
and Competitiveness Issues  
National Security and International  
Affairs Division  
U.S. General Accounting Office  
Washington, D.C. 20548

Dear Mr. Cooper:

This is the Department of Defense (DoD) response to the General Accounting Office (GAO) draft report, "Interagency Contracting: Controls Over Contract Off-loads Being Strengthened, But Implementation Issues Remain," dated August 14, 1995 (GAO Code 705071/OSD Case 9981).

The Department has reviewed the report and concurs without further comment. Informal comments proposing technical changes to a preliminary draft were previously provided. The Department appreciates the opportunity to review the report in draft form.

Sincerely,

A handwritten signature in black ink that reads "Josh Gotbaum".



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