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APRIL 22, 1982

RELEASED

The Honorable James A. McClure
Chairman, Committee on Energy
and Natural Resources
United States Senate

Dear Mr. Chairman:

Subject: The Subcontracting Practices of Large
Department of Energy Contractors Need
to Be Improved (EMD-82-35)

On October 29, 1980, the former Chairman, Senate Committee on Energy and Natural Resources requested that we review the subcontracting practices of major Department of Energy (DOE) contractors, particularly those operating national laboratories or other Government-owned, contractor-operated installations. In fiscal year 1980, these contractors initiated about 900,000 procurement actions totaling at least \$2.4 billion. Yet, there was very little information available to the Committee on the acceptability of their procurement practices or whether they were adhering to the principles of Federal procurement regulations.

Following your appointment as Committee Chairman, we discussed this request with your office and agreed to make some adjustments in our scope of work. At the completion of our review, we also briefed your office on the results of our work and, at your office's request, are summarizing our findings and recommendations in this letter.

Federal procurement regulations do not apply per se to DOE operating contractors. Moreover, DOE officials believe that strict adherence to these regulations could be counterproductive and prevent the contractors from efficiently and effectively carrying out their assigned tasks. These contractors are required, however, to follow procedures which approximate most aspects of the Federal regulations and which are intended to guarantee open competition and reasonable prices for goods and services.

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In spite of this, we found that DOE contractors have (1) engaged in practices which prevent or limit competition, (2) awarded subcontracts directly for DOE program offices allowing these offices to bypass Federal and DOE procurement regulations and policies, (3) not fully complied with Federal and DOE conflict of interest regulations, (4) not been required to follow Federal and DOE guidelines relating to the use of consultant-type contracts, and (5) not established adequate controls to evaluate the utility of subcontractor work products and ensure that subcontractor efforts are not duplicated. In its oversight activities, DOE has become aware of some of these deficiencies and has taken or planned corrective actions. For instance, DOE has recently acted to eliminate situations where its contractors, in effect, serve as procurement agents for DOE program offices, often in violation of Federal procurement regulations. More needs to be done, however, to ensure that major DOE contractors adhere to the spirit, if not the letter, of Federal procurement policies.

OBJECTIVES, SCOPE, AND METHODOLOGY

Our objective was to evaluate the subcontracting practices of major DOE contractors--those operating national laboratories or other Government-owned, contractor-operated installations. Specifically, we were asked to review the extent to which:

(1) DOE

- oversees and controls subcontracting activities and
- uses subcontracts to circumvent Federal procurement regulations and policies,

(2) DOE contractors

- engage in practices which prevent or limit competition,
- comply with Federal or DOE conflict of interest regulations,
- use consultant-type contractors to perform governmental functions,
- avoid duplication of efforts and evaluate and disseminate subcontractor work products, and
- comply with Federal and DOE small and minority business programs.

To do this, we selected two major DOE contractors--the Sandia Laboratories (Sandia) in Albuquerque, New Mexico, and the Argonne National Laboratory (Argonne) near Chicago, Illinois--for detailed

review. Each of these has large procurement offices and together represented about 15 percent of the total procurement volume of all DOE operating contractors. The Sandia Laboratories is operated by the Western Electric Company while Argonne is jointly operated by the University of Chicago and the Argonne Universities Association, a consortium of 30 midwestern universities. At these two locations, we summarized the contractors' procurement activities; reviewed their procurement policies, practices, and procedures; and interviewed both procurement and program personnel.

In addition, we examined 30 subcontracts at each location. This was not, however, a statistically valid sample of subcontracts which would allow a projection of our findings to the total procurement operations of either Sandia or Argonne. Rather, it was a selection designed to evaluate the specific issues raised in the Committee's request and to test the procurement policies and procedures of each laboratory. Accordingly, the subcontracts examined included (1) noncompetitive awards; (2) subcontracts over \$10,000 for management, consulting, or other types of professional services (as opposed to subcontracts for supplies, hardware, or construction activities); (3) subcontracts awarded at the specific direction of DOE program offices--situations where the subcontractors were working directly for DOE officials rather than Sandia or Argonne; and (4) subcontracts with small or minority business concerns.

We also did extensive work at DOE Headquarters and the DOE Chicago and Albuquerque Operations Offices which have oversight responsibilities for Argonne and Sandia, respectively. Among other things, we reviewed the Federal and DOE procurement regulations, procedures, and policies (particularly those relating to subcontracting activities); interviewed DOE program and procurement personnel responsible for overseeing and evaluating the procurement activities of Argonne, Sandia, and other large DOE operating contractors; and observed DOE as it evaluated the overall procurement system of the Solar Energy Research Institute in Golden, Colorado. 1/

While our work did not allow us to project the extent of problems throughout DOE and the other operating contractors, it gave us a good understanding of the DOE controls over the subcontracting practices of its large operating contractors and allowed us to pinpoint weaknesses that could be the cause of more extensive problems.

Our review was performed in accordance with GAO's current "Standards for Audit of Governmental Organizations, Programs, Activities, and Functions."

1/We observed this DOE procurement system review because none were scheduled for either Argonne or Sandia during our review.

EXTENT OF SUBCONTRACTING
BY DOE OPERATING CONTRACTORS

To carry out its many energy and defense-related missions, DOE has a large network of research and production facilities, including 12 multiprogram laboratories, 31 specialized laboratories, and 13 nuclear material and weapons production facilities. All of these are Government-owned, but most are operated by university, industry, or nonprofit contractors. They are the principal, technical arm of DOE, representing a capital investment of about \$15 billion and employing over 100,000 people. In fiscal year 1980, these contractors accounted for \$5.1 billion or about 52 percent of DOE's total contracting budget. Of this amount, at least \$2.4 billion was used by these prime contractors to subcontract with other firms or individuals for assistance in carrying out DOE missions.

The following chart summarizes the fiscal year 1980 procurement activities of Argonne, Sandia, and the other operating contractors as reported by DOE's "Integrated Procurement Management Information System." Although we confirmed and adjusted the Argonne and Sandia data during our work at those two locations, the remaining data have not been checked and may be incomplete or inaccurate. DOE's "Integrated Procurement Management Information System" (which is the subject of an ongoing GAO review) has experienced major difficulties in reporting accurate data.

<u>Contractors</u>	<u>Procurement actions</u>					
	<u>Less than \$10,000</u>		<u>More than \$10,000</u>		<u>Total</u>	
	<u>Actions</u>	<u>Value</u>	<u>Actions</u>	<u>Value</u>	<u>Actions</u>	<u>Value</u>
		(millions)		(millions)		(millions)
Argonne	39,813	\$ 28.6	1,759	\$ 103.5	41,572	\$ 132.1
Sandia	86,284	61.6	4,857	179.6	91,141	241.2
Other contractors	<u>741,197</u>	<u>482.9</u>	<u>29,663</u>	<u>1,549.5</u>	<u>770,860</u>	<u>2,032.4</u>
Total	<u>867,294</u>	<u>\$573.1</u>	<u>36,279</u>	<u>\$1,832.6</u>	<u>903,573</u>	<u>\$2,405.7</u>

DOE'S OVERSIGHT OF SUBCONTRACTING
ACTIVITIES COULD BE IMPROVED

DOE has, at least on paper, a comprehensive system for overseeing the procurement operations of its large operating contractors. This involves at least three major operations: (1) concentrated evaluations of the contractors' procurement systems at

least every 2 years, (2) interim surveillance reviews, and (3) a review and approval process for larger value or unique subcontracts before they are awarded. If properly implemented, these actions would be adequate to ensure adherence to Federal procurement policies and practices. We found, however, that they were sometimes shallow in scope or were not always being performed. In addition, they did not cover some of the areas of concern included in the Committee's request.

The first stage of DOE's oversight is the "Contractor Procurement System Review." This is an evaluation of the contractor's overall procurement system which is used by DOE to approve or disapprove the system and to determine how much independent subcontracting authority the contractor should have. Generally, this review is performed at least every 2 years at each of DOE's major contractors but may be extended if DOE determines that it can adequately monitor sensitive areas of the contractor's system. Such a determination had been made at Sandia, and the procurement system review interval had been extended to every 3 years.

Among other things, the Procurement System Review evaluates the contractor's control of sole-source procurements and its program for small and minority business enterprises--two areas your Committee requested that we review. The remainder looks at such things as

- the extent of adequate price competition,
- compliance with cost or pricing data requirements,
- subcontract management, and
- organization of the purchasing operations and training.

It does not cover the contractor's compliance with conflict of interest regulations, its use of consultant-type contracts, or the other areas of concern expressed in your Committee's letter. In addition, we found that the reviews at Sandia and Argonne did not comprehensively evaluate non-competitive procurements. In these cases, the reviewers performed primarily a "check-list" type of analysis and concluded that the controls over sole-source procurements were adequate.

In between Procurement Systems Reviews, DOE field offices are supposed to periodically conduct similar but less comprehensive surveillance reviews. These reviews vary in frequency and scope among the various contractors but are designed to ensure that the procurement systems continue to operate as approved. In the case of Sandia, however, only one scheduled surveillance

review has been conducted by DOE since February 1979--the date of the last Systems Review. It was done in October 1980 but, because of the heavy workload of the DOE staff, the report was never published. A similar situation exists at Argonne, where surveillance reviews have diminished in frequency and have not been formally structured or reported.

The third stage of DOE's oversight operations is the advance review and approval of larger value subcontracts. At Sandia, for instance, DOE reviews, before award, all cost-type subcontracts over \$500,000 and all fixed price subcontracts over \$1 million. Among other things, DOE reviews the

- type of contract being proposed;
- procurement procedures used for competitive or non-competitive awards, bids solicited and received, and negotiations;
- price justification as evidenced by the degree of price competition obtained, the price/cost analysis, and preaward audit; and
- contract terms and conditions and whether they comply with those approved by DOE.

Although this advance review is comprehensive, we found that Sandia only had 39 procurement actions in fiscal year 1980 (out of 3,117 original contract actions) which were subject to this evaluation. The remainder was under the \$500,000/\$1-million review limits established for Sandia.

In addition, DOE procurement officials at Sandia maintain a general awareness of the subcontracting activities and can elect to review, before award, any proposed subcontract of an unusual or sensitive nature. There are also other subcontracts which require some level of DOE review and approval regardless of dollar limitations. Examples include proposed subcontracts which deviate from established procurement policies and practices or which are for the purchase of computer programs or proprietary data.

DOE's review and approval criteria and procedures at Argonne, while not identical to those at Sandia, are also aimed at higher value and unusual or sensitive types of subcontract actions.

DOE CONTRACTORS LIMIT COMPETITION

The cornerstone of Federal procurement regulations is that competition should be obtained to the maximum extent practicable.

This helps not only to minimize opportunities for favoritism and collusion but also provides greater assurance that acceptable supplies and services are obtained at the lowest prices. This does not mean, however, that all contracts must be competitively awarded. To the contrary, sole-source procurements are allowable if only one source is exclusively capable of performing within the time required and at reasonable prices. Such circumstances, however, must be thoroughly documented, supported by special justifications, and reviewed by appropriate procurement and management personnel.

In this context, we found that both Sandia and Argonne had high percentages of non-competitive procurement actions for subcontracts over \$10,000 (63 percent for Sandia and 72 percent for Argonne). But this is not new. DOE had noted the same type of percentages during Procurement System Reviews at Sandia in February 1979 and at Argonne in June 1980. In both cases, however, DOE concluded that the laboratories had adequate procedures for controlling sole-source procurements and did not recommend any major corrective actions.

We do not completely agree with this assessment. While the procedures for controlling non-competitive procurements do appear reasonable, we found that these procedures were not always being followed. At both Argonne and Sandia, for instance, we found that the procurement personnel relied extensively on program officials to determine when or if a sole-source contract was needed. While program officials may properly conclude that only one source is competent and available to do the required work, procurement personnel are responsible for ensuring that this decision is documented and fully supportable. In our view, however, procurement officials did not always have adequate information to judge whether the sole-source procurement was justified. Yet, they approved the procurement action and allowed the contract to be awarded. This was true in the majority of the 53 sole-source procurement actions we reviewed at the two locations.

For example, Argonne awarded a sole-source subcontract to Calvin Kytle Associates, Inc., in Washington, D.C., for approximately \$70,000 to prepare material for a Presidential information clearinghouse. The sole-source award was based on a program office justification that the subcontractor had the required capability from past experience and was available on short notice to carry out the required work. However, the justification did not include any information about the extent that other contractors were considered or the reasons they lacked the capability to perform. In addition, the contracting officer made no effort to verify the justification or to search for other vendors and the responsible program official could not recall the extent that other contractors were considered. The program official noted,

however, that time was a critical factor and the subcontractor had been recommended by DOE.

We do not believe that the previous DOE Procurement System Reviews of Sandia and Argonne went far enough in evaluating non-competitive procurements. In fact, it appears that DOE primarily looked to see if the proper sole-source justifications and other documentation were available in the contract files without questioning the basis for the justifications in any depth or attempting to determine if reasonable efforts were made to find other available and qualified firms.

OPERATING CONTRACTORS HAVE SERVED
AS PROCUREMENT AGENTS FOR DOE
PROGRAM OFFICES

We found that program officials from DOE's headquarters and field organizations had directed Argonne and Sandia to award certain subcontracts on a sole-source basis. Under these circumstances, DOE normally retained all programmatic responsibilities and was the primary beneficiary of the subcontractors' work; Sandia and Argonne merely served as procurement agents. Although records are not kept on the number of times this occurs, officials at Sandia and Argonne were able to identify several of these types of subcontracts for our review.

After reviewing 13 of these DOE "directed" procurements, we found that almost all occurred because Argonne and Sandia could make awards faster than a DOE procurement office. These laboratories are not required to follow all aspects of the Federal and DOE procurement regulations and can expedite the procurement process, particularly if directed to do so by DOE. For instance, Sandia (according to the terms of its contract with DOE) is not required to formally advertise procurements, adhere to Federal or DOE conflict of interest regulations, or follow the Federal definition and controls over the use of consultants. Similar situations exist at Argonne and other DOE operating contractors. Thus, DOE program officials find it easier, in certain circumstances, to award contracts through operating contractors rather than DOE procurement offices. Unfortunately, this often circumvents many of the controls established to protect public monies and ensure adherence to Federal procurement policies and procedures.

This was recently confirmed by DOE's Office of Inspector General during a review at DOE's Solar Energy Research Institute in Golden, Colorado. The Inspector General, in that case, found that the Research Institute had awarded non-competitive contracts at the request of DOE's headquarters personnel and concluded that this circumvented DOE procurement regulations. In addition, we reported on a similar situation last April at the Los Alamos

Scientific Laboratory in Los Alamos, New Mexico. ^{1/} In that instance, a DOE headquarters program office, to save time, was bypassing its own procurement office and directing Los Alamos to award a \$200,000-sole-source subcontract to a consulting firm located in the Washington metropolitan area. As is typical of these cases, however, the subcontractor was to work directly for the DOE program office, not the laboratory which awarded the subcontract. As a result of our report, the subcontract action was reevaluated by DOE and withdrawn before award.

Because of these and other actions, DOE has become aware of the problems associated with directed procurements and is attempting to take corrective action. In August 1981 for example, DOE's Assistant Secretary for Management and Administration, ordered that the practice of directing procurements be discontinued and that DOE contracts be handled through normal procurement channels. This was followed by DOE Order 4200.3 (dated January 15, 1982) which formally prohibited this type of procurement action. It is too early to tell, however, the effect these actions will have on the overall problems.

CONFLICT OF INTEREST REGULATIONS HAVE NOT BEEN IMPLEMENTED

When purchasing certain services, DOE is required to determine if prospective contractors have special interests or relationships which could prevent them from giving impartial, technically sound assistance or advice to the Federal Government. This is done by requiring the contractors to either disclose or disclaim knowledge of situations or relationships which might affect their impartiality or give them an unfair competitive advantage. For example, it might be inappropriate if a prospective contractor had subsidiaries or investments in companies which would benefit from the work to be performed under the contract. This could, depending on the circumstances, present an organizational conflict of interest and either disqualify the contractor from the award or require special contract provisions or other actions to mitigate the potential effects. In any event, adherence to conflict of interest regulations helps detect these types of situations and plays an important part in assuring that DOE receives fair and impartial advice from its contractors.

In this context, it is also important that DOE's large operating contractors follow the same type of regulations. They account for a large portion of DOE's contract dollars and

^{1/}"Need for \$200,000 Subcontract Apparently Eliminated by Reagan Administration Proposal," EMD-81-81, Apr. 24, 1981.

perform many of the same research and development activities normally associated with DOE. We found, however, that conflict of interest regulations had not been fully implemented at the two national laboratories included in our review.

At Sandia, for instance, the prime contract between DOE and Western Electric does not include any conflict of interest clauses. Consequently, Sandia does not formally require prospective subcontractors to submit the necessary information (before the contract award) so that potential conflicts can be identified and resolved. Also, Sandia's subcontracts do not include provisions requiring the subcontractors to disclose conflicts discovered after the contract award. Equally as important, however, Sandia has not voluntarily adopted formal conflict of interest procedures, and DOE has not planned any remedial action until Sandia's contract is renewed in 1983.

Argonne, on the other hand, established conflict of interest procedures in June 1980 (about a year after DOE's current regulations became effective). These procedures require subcontractors to either disclose or specifically disclaim knowledge of possible conflicts--procedures very similar to DOE's. We are not sure, however, how well these procedures are being followed. Our review of several subcontracts awarded after June 1980--and which appeared to be susceptible to conflict of interest considerations--showed that Argonne was not consistently requiring the necessary information or making the appropriate reviews.

OPERATING CONTRACTORS ARE NOT
FOLLOWING FEDERAL GUIDELINES FOR
USING CONSULTANT-TYPE CONTRACTS

A major concern of the Congress and the Executive Branch over the past several years is the extent to which Federal agencies use consultant or support service contractors to perform work that should be performed by Government employees. Office of Management and Budget Circular A-76, for instance, states that certain agency functions are so intimately related to the public interest that they must be performed by Federal employees. Such functions would include the direct management of Federal employees, the selection of program priorities, or the technical analysis and evaluation of research and development activities. In a letter to you dated September 14, 1981, ^{1/} we discussed the extent of this type of contracting at DOE and the problems we had in determining whether contractors were performing these functions or merely assisting DOE.

^{1/}"The Department of Energy's Use of Support Service Contractors to Perform Basic Management Functions," EMD-81-144.

In your Committee's request, however, we were asked to look at this problem from a different angle. More precisely, your Committee wanted to know if DOE's large operating contractors were also using consultant or support service contractors to perform their management functions. This question recognizes that the operating contractors have major responsibilities for many DOE programs. Consequently, if they subcontract for support services, it could have the same impact as if DOE had contracted for the services (i.e., subcontractors could be performing DOE management functions).

In the sample of contracts we reviewed at Argonne and Sandia, we did not find any specific instances where subcontractors were performing what we felt were "Government" management functions. However, we did note a general lack of concern and information relating to this type of subcontracting at the two laboratories. For instance, the laboratories have no consistent definition of a consultant or support service contract, are not required to follow Federal criteria prohibiting the use of contractors to perform agency management functions, and do not report the extent of this type of subcontracting to DOE. More importantly, DOE's oversight of this type of subcontracting is almost non-existent. Consequently, DOE does not know how often operating contractors rely on other subcontractors for management or technical support services or whether such subcontracting is consistent with Federal guidelines.

This was confirmed by a DOE internal audit of consulting services at Sandia. In its August 6, 1981, report, the DOE internal auditors found that Sandia had adequate controls to monitor and regulate the use of individuals as consultants but not firms or organizations. Specifically, the DOE auditors found that Sandia's procurement instructions do not clearly recognize that organizations can perform consulting services. Consequently, Sandia was not accurately identifying and reporting subcontracts for consulting or management support services so that these could be controlled or monitored by DOE or Sandia management.

IMPROVEMENTS NEEDED TO AVOID
DUPLICATION AND TO EVALUATE AND
DISSEMINATE SUBCONTRACTOR WORK PRODUCTS

Your Committee had several interests relating to the subcontractor's work products. Specifically, it wanted to know how DOE's operating contractors

--avoided duplicating either ongoing or past work,

--evaluated the subcontractors' work products in terms of the contract specifications and DOE's programs and missions, and

--disseminated their subcontractors' work products to the public and technical community.

In general, we found that there was no consistent or documented method used by either Sandia or Argonne to avoid duplication of efforts or to evaluate subcontractor work products and performance. On the other hand, each laboratory transmitted subcontractor-produced technical reports to DOE's Technical Information Center in Oak Ridge, Tennessee (DOE's central point for collecting, processing, and disseminating scientific and technical information). Even this, however, was not documented in the contract files.

To avoid duplicating efforts, both Sandia and Argonne procurement offices rely almost exclusively on their program personnel. These people are expected to have sufficient knowledge in their respective program areas to prevent duplication. While extensive literature searches or other actions are sometimes performed, there is no requirement that this be done or documented in the contract files. Consequently, there is potential, depending on the knowledge of laboratory program personnel, for some subcontract efforts to be duplications of past or ongoing work.

The same type of situation exists for evaluations of the subcontractors' performance and work products. Both laboratories generally perform some type of evaluation at the completion of each contract, but it is being done by program personnel and is not documented in the contract files. In addition, we found that the type and quality of the evaluations varied greatly, even among the program offices within each laboratory. Some were merely subjective assessments by technical personnel responsible for monitoring the subcontractors' performance. Others were more formal and were being used by the particular program office as potential references in future subcontract actions. In neither laboratory, however, did the operating contractor have a systematic system in place to (1) evaluate the performance of the subcontractors, (2) document the extent to which the delivered products contributed to DOE's program or missions, or (3) collect information on the performances of all contractors for use in future subcontract solicitations.

Concerning the dissemination of subcontractor work products, we found that both laboratories had formal procedures for submitting the applicable technical reports to DOE's Technical Information Center. This Center, in turn, is supposed to ensure that the reports are distributed within DOE, to its contractors, and, when applicable, to the general public. We did not, however, review the operations of the Information Center or otherwise determine how well it was carrying out this task. We did note, however, that the responsibility for transmitting applicable reports to the Information Center belonged to the program staff,

and that documentation of the transfer was generally not included in the procurement file.

OPERATING CONTRACTORS ARE
COMPLYING WITH DOE SMALL AND
MINORITY BUSINESS PROGRAMS

Each laboratory, in our view, has an extensive program to provide small and disadvantaged businesses the opportunity to participate as subcontractors under the laboratory's prime contract with DOE. These programs have been found in compliance with Federal legislation by the Small Business Administration and are subject to DOE monitoring through quarterly reporting and Procurement System Reviews. We could not judge whether these laboratories reflect the norm for other contractors, but overall procurement from small and disadvantaged businesses in fiscal year 1980 exceeded \$1.3 billion--about half of all operating contract procurements. Thus, from the information we have seen, DOE operating contractors are making extensive use of small and disadvantaged businesses.

CONCLUSIONS

DOE's operating contractors spent about \$2.4 billion in fiscal year 1980 to subcontract for various goods and services. As a result, DOE has developed a comprehensive system for overseeing the contractors and guaranteeing that they adhere to the principle, if not the letter, of the Federal and DOE procurement regulations. This oversight includes (1) detailed Procurement System Reviews at least every 2 years, (2) interim surveillance reviews, and (3) normal review and approval of all larger value or unique subcontracts. We found, however, that the depth and frequency of these reviews could be improved.

For instance, the latest Procurement System Reviews at Sandia and Argonne did not go far enough, in our view, to evaluate the practices used to maximize competition. In addition, they did not cover some of the important and timely topics you asked us to review. This problem was compounded by the fact that DOE surveillance reviews were not being performed as scheduled and only a relatively small number of subcontracts were subject to DOE's advance review and approval process.

For these reasons and others, we found that Argonne and Sandia had high percentages of non-competitive procurement actions; were at times, serving as procurement agents for DOE program offices, allowing DOE officials to bypass Federal and DOE procurement regulations; were not always adhering to DOE conflict of interest regulations or to the controls established for using consultants and other support service

contractors; and had no systematic processes for avoiding duplication of efforts or for evaluating subcontractors' performance and work products.

On the other hand, both Sandia and Argonne had active programs for subcontracting with small and disadvantaged businesses. In fact, throughout all major DOE operating contractors, almost half of the subcontracting (\$1.3 billion in fiscal year 1980) was to either small or disadvantaged business concerns. This reflects, in part, DOE's emphasis on this type of subcontracting during its oversight activities.

RECOMMENDATIONS TO THE SECRETARY OF ENERGY

We recommend that the Secretary of Energy

- improve the DOE oversight of operating contractors by (1) expanding the scope of DOE's Procurement Systems Reviews particularly in the area of non-competitive procurements, organizational conflicts of interest, and the use of consultant and support service contractors and (2) directing that surveillance reviews be planned and performed in a systematic and timely manner;
- promptly enter into negotiations with all operating contractors to include organizational conflict of interest provisions in their current contracts;
- require that operating contractors (1) consider (during the procurement process) the intent of Federal requirements and guidelines relating to consultant and support service contracts and (2) report periodically to DOE on the extent of such contracting; and
- require that operating contractor procurement offices implement more effective and systematic administrative controls designed to avoid duplication of work, ensure prompt and appropriate evaluation of contractor performance, and ensure prompt dissemination of subcontractor work products.

AGENCY COMMENTS

DOE said that, while limited in scope, this report generally presents a fair and balanced assessment of its contractors' procurement operations (see enclosure). DOE disagreed, however, with a recommendation in our draft report that the operating contractors be required to adhere to Federal requirements and guidelines relating to consultant and support service contracts.

In fact, DOE noted that the Government benefits substantially from the contractors' ability to employ consultant and support service contractors to supplement and compliment their work force. Nevertheless, DOE said that it would require its management and operating contractors to consider the intent of the Federal guidelines as part of their normal internal "make or buy" decision process. We agree with this proposed action and have changed our recommendation accordingly.

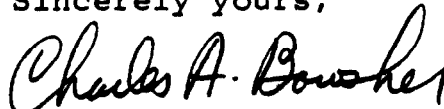
We stress, however, that it is not our intent to prohibit operating contractors from subcontracting for consulting and management support services. When properly controlled, we recognize that these services can provide valuable, short-term assistance that might not be generally available within the contractors' organizations. Instead, it is our goal to strengthen the operating contractors' controls over these types of subcontractors and to ensure that they are properly identified and reported to DOE. This is supported by a DOE internal audit report of consulting services at Sandia, referred to on page 11 of this report.

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As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of the report. At that time, we will send copies to the Secretary of Energy; the Director, Office of Management and Budget; interested congressional committees; and others upon request.

If you have any questions, or if we can be of any further assistance, please let us know.

Sincerely yours,



Comptroller General
of the United States

Enclosure



Department of Energy
Washington, D.C. 20585

FEB 26 1982

Mr. J. Dexter Peach
Energy and Minerals Division
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Peach:

The Department of Energy (DOE) appreciates the opportunity to review and comment on the General Accounting Office's (GAO) draft report entitled "The Subcontracting Practices of Large Department of Energy Contractors Need to be Improved." DOE believes that its Management and Operating contractors carry out their assigned functions, including any subcontracting responsibilities, in an efficient and effective manner.

We believe the report generally recognizes the effective operation conducted by DOE's Management and Operating contractors as well as the Department's comprehensive oversight activities for these contractors. Although limited in scope, the report generally presents a fair and balanced assessment of these contractors' procurement operations and has provided the Department with thoughtful recommendations. In our specific comments provided directly to the members of the GAO audit staff, we do note some inaccuracies and necessary clarifications which should be considered prior to issuance of any final report.

We cannot, however, concur with the recommendation that our Management and Operating contractors be required to adhere to Federal requirements and guidelines relating to consultant and support service contracts. As indicated in the draft report, the GAO audit team found no instance where these contractors or their subcontractors performed "Government" management functions. One of the strengths of the unique relationship which exists between DOE and these contractors is the Government's ability to benefit substantially by taking advantage of the established abilities, innovations and practices of the contractor's organization. Private business organizations normally and regularly employ consultants and support service contractors to supplement and complement their work force. The Federal requirements and guidelines on consulting and support services are designed for and directed at prime procurement actions of executive agencies and departments, not the activities of private business organizations.

We will, however, require our Management and Operating contractors to consider the intent of these Federal guidelines as part of their normal internal "Make or Buy" decision process, which is reviewed as part of DOE's Contractor Procurement System Review program.

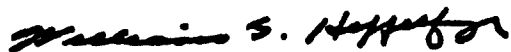
In regard to the recommendation that DOE amend all Management and Operating contracts to include organizational conflicts of interest (OCI) provisions, the Departmental procurement regulations (DOE-PR 9-1.5411, 44 FR 2556-62, January 11, 1979) currently require that an OCI clause be included in such contracts when they are renewed. These contracts are normally renewed on a five-year cycle and, since the regulations were issued in January of 1979, approximately 50 percent of these contracts presently include appropriate OCI clauses. Additionally, it should be noted that OCI has not in the past been a problem with our operating contractors as they are required to be physically and organizationally separated from their parent organizations. Any business conducted with the parent is closely controlled. The only work these contractors perform must be assigned or approved by DOE.

However, in order to accelerate the inclusion of OCI clauses in these contracts, we will require that such clauses be incorporated into these contracts when the annual fee negotiations are conducted.

This Department continues to be committed to the need for effective oversight of these special contracts and will increase its emphasis on surveillance reviews by DOE Headquarters as well as our field operations offices. In our view, the current surveillance procedures are sound and effective, but we recognize the desirability of strengthening the scope and frequency of these reviews.

Specific comments have been provided directly to members of the GAO audit staff. DOE appreciates the opportunity to comment on this draft report and trusts that GAO will consider our comments in preparing the final report.

Sincerely,


William S. Heffelfinger
Assistant Secretary
Management and Administration