

GAO

Report to the Chairman, Committee on
Governmental Affairs, U.S. Senate

October 1991

ENERGY MANAGEMENT

DOE Actions to Improve Oversight of Contractors' Subcontracting Practices



**Resources, Community, and
Economic Development Division**

B-245444

October 7, 1991

The Honorable John Glenn
Chairman, Committee on Governmental
Affairs
United States Senate

Dear Mr. Chairman:

As you requested, we reviewed the Department of Energy's (DOE) Contractor Purchasing System Review (CPSR) Program, which oversees the extensive subcontracting activities of the Department's management and operating (M&O) contractors. This review is part of a special GAO audit effort to help ensure that areas vulnerable to fraud, waste, abuse, and mismanagement are identified and that adequate corrective actions are taken. This effort focuses on 16 areas, one of which is DOE contractor oversight. At your Committee's August 1, 1991, hearing on DOE procurement and subcontracting, we testified on the preliminary results of our review of DOE's CPSR Program.¹ This report describes the subcontracting deficiencies occurring at DOE, identifies shortcomings in DOE's CPSR Program, and discusses the corrective actions that DOE has committed to take in its CPSR Program in response to our findings.

Results in Brief

We believe that DOE's M&O subcontracts, totaling over \$5 billion in 1990, are vulnerable to fraud, waste, and abuse—a fact that is reflected in DOE's recent Contractor Purchasing System Reviews. Poor procurement practices of the M&O contractors, coupled with inadequate oversight by DOE, have led to excessive subcontract costs that are borne by the government. Among other things, DOE's reviews have shown that M&O contractors often do not ensure that subcontract prices are fair and reasonable, and that these contractors are also restricting competition by inappropriately using sole-source purchases.

Improvements in DOE oversight are needed to address M&O subcontracting weaknesses. DOE's Contractor Purchasing System Reviews have succeeded in identifying a number of internal control problems at M&O contractors. Limitations in the review program, however, restrict DOE's ability to identify all significant procurement weaknesses that exist and to ensure that identified problems are corrected. These limitations

¹DOE Management: DOE Needs to Improve Oversight of Subcontracting Practices of Management and Operating Contractors (GAO/T-RCED-91-79, Aug. 1, 1991).

include insufficient headquarters oversight of the scope and depth of the reviews, a reluctance by DOE to withhold or withdraw purchasing system approval even when serious deficiencies are identified, and inadequate follow-up by field offices of contractors' responses to CPSR recommendations.

DOE is currently taking actions to address the problems we identified. DOE will (1) have the CPSR Program centrally managed by headquarters staff, (2) conduct the reviews more often, and (3) issue Department-wide requirements and procedures for the conduct of the revised program. To implement these corrective actions, DOE plans to increase its headquarters CPSR staff from one position to five and require that each field office allocate two full-time staff positions to the program. In addition, DOE's Director of Procurement will make the decisions on whether to approve or disapprove contractors' purchasing systems, and field offices will be required to submit quarterly reports on the status of contractors' responses to CPSR recommendations.

Background

Most of DOE's subcontracts are awarded by contractors who manage and operate DOE's research and production facilities. During fiscal year 1990, DOE obligated about \$13.8 billion to the M&O contractors and of these funds more than \$5 billion was spent on subcontracts. These subcontracts are awarded and administered through purchasing systems that are established by the individual M&O contractors. DOE must approve written descriptions of the purchasing systems.

DOE oversees subcontracts awarded by its M&O contractors primarily through Contractor Purchasing System Reviews, generally conducted for each of the contracts once every 3 years by DOE field offices (operations offices).² On the basis of the review results, the field offices generally approve contractors' purchasing systems with recommendations to correct identified problems, and set specified dollar thresholds above which contractors must obtain advance DOE approval of subcontracts. If DOE disapproves purchasing systems or lowers the advance approval thresholds, the cognizant field office must review and approve an increased number of subcontracts. In the intervening years between CPSRS, DOE field offices are to provide oversight, termed "surveillance," that includes monitoring contractors' responses to the purchasing review recommendations and reviewing subcontracts in excess of the established dollar thresholds.

²In 1990 DOE had 52 M&O contracts with 35 contractors.

DOE Reviews Disclose Significant M&O Subcontracting Deficiencies

The Contractor Purchasing System Reviews that DOE conducted during the most recent 3-year cycle revealed many fundamental deficiencies in contractors' purchasing systems. Reports from 37 of 40 recent reviews disclosed significant cost deficiencies; that is, contractors were not adequately performing and documenting the basic analyses needed to ensure that subcontract prices were fair and reasonable. For example, DOE reported that one contractor demonstrated an overall lack of awareness of the importance of establishing fair and reasonable prices and that another contractor generally accepted cost proposals at face value.

More than half of the reviews also identified a lack of adequate procurement planning as well as questionable sole-source purchases. These deficiencies can restrict competition and limit the government's ability to obtain the best contract terms. Also, 16 of the reviews expressed concerns about the uses of contract modifications. Among other things, the reviews reported that contractors (1) changed the scope of existing contracts when new contracts should have been used and (2) priced initial contracts under dollar thresholds that required DOE advance approval and subsequently used contract modifications to increase the prices above the DOE review thresholds.

Procurement deficiencies cited in DOE reviews that increase the risk for fraud, waste, and abuse include awarding subcontracts after work on the contracts has begun; inadequate separation of duties, such as allowing the same individual to order goods and services and verify their receipt; reliance on requisitioners (for example, program officials) rather than procurement officials (buyers) to determine supply sources; and a contractor policy that permitted buyers to accept gifts, such as meals and tickets, in contravention of DOE's policies.

Weaknesses in DOE's CPSR Program Limit Its Effectiveness

While DOE's Contractor Purchasing System Review Program has identified weaknesses in M&O contractors' purchasing systems, the program has limitations that reduce its effectiveness. In particular, the program still does not ensure that all procurement activities are reviewed and that appropriate actions are taken to correct procurement deficiencies.

DOE headquarters has developed a guide that sets forth the relevant purchasing criteria DOE field offices should address in the Contractor Purchasing System Reviews. However, although it is aware that some reviews do not address all purchasing criteria, DOE does not require the field offices to follow its guide. Furthermore, DOE headquarters does not sufficiently examine field offices' reviews to determine whether the

reviews were adequate in scope and depth. For example, rather than independently verifying that reviews have covered all aspects of the contractors' procurement systems, DOE headquarters relies solely on statements by the review team leader that areas not clearly addressed in the report have been reviewed in sufficient depth. Finally, when DOE headquarters determines that a review has not included significant procurement areas, it does not require the responsible field office to review the omitted areas until the next review—3 years later.

To correct deficiencies identified in the reviews, DOE headquarters requires its field offices to submit surveillance plans describing oversight that will be performed between the reviews. However, for the reviews conducted from 1988 through 1990, DOE field offices have not submitted surveillance plans in almost 50 percent of the cases. In addition, many of the surveillance plans that have been submitted include broad descriptions of the oversight to be conducted—they do not specify tasks to be performed, methodologies to be used in the follow-up reviews, or whether the field offices will be reviewing the effectiveness of contractors' responses to review recommendations. In June 1991 we found that the DOE San Francisco office had conducted its very first surveillance review at Lawrence Livermore National Laboratory just that month and that it had not yet issued a surveillance plan.

Some of these deficiencies are illustrated by the reviews that were performed of Reynolds Electrical & Engineering Company, the manager of DOE's Nevada Test Site. None of the three most recent reviews of Reynolds evaluated contract administration—an area in which reviews of other contractors have reported numerous deficiencies. DOE headquarters only became aware of this omission when a DOE headquarters procurement analyst participated in the latest review—something that rarely takes place. Further, after discovering that reviews of Reynolds had omitted contract administration, DOE headquarters did not require the field office to review the contract administration function until the next review. Also, significant deficiencies that were identified in earlier Reynolds reviews have not been corrected. For example, reviews in 1984, 1986, and 1989 all cited deficiencies in two critical purchasing activities: inattention to subcontract costs and inadequate justifications for noncompetitive purchases.

DOE has not taken appropriate corrective action when reviews have identified serious deficiencies in the contractors' procurement systems. For example, a recent DOE report stated that during 1990, purchasing system approval should have been either withheld or withdrawn (for

example, by reducing the level of contracting authority) in several cases until the contractors had corrected all major deficiencies. However, such action was not taken.

We are concerned that field office decisions may be driven more by resource constraints than by review findings because disapproval of purchasing systems or reduction of contracting authority thresholds requires DOE to increase its review of individual subcontracts. For example, in November 1990 a special DOE procurement review of EG&G, Inc.—the M&O contractor at the Rocky Flats Plant in Colorado—led by DOE's Procurement Director resulted in disapproval of the purchasing system by DOE headquarters. This occurred less than 4 months after the field office's review had resulted in approval of the contractor's system.

DOE Plans to Improve Oversight

On July 9, 1991, the DOE Director of Procurement told us that DOE plans to restructure its CPSR Program to address the weaknesses we identified. To increase DOE headquarters oversight of the program, DOE plans to have the CPSR Program centrally managed and conducted by headquarters staff, augmented by field staff. Currently, the program is decentralized, with each field office designing and conducting the reviews and determining the appropriate actions to take in response to review findings. In addition, DOE plans to conduct CPSRs on its M&O contracts every 2 years rather than every 3 years, which is the current schedule. DOE also plans to (1) issue Department-wide requirements and procedures for the conduct of the revised program and (2) revise its current CPSR Guide and reissue it as a directive rather than as guidance. DOE also plans to request additional headquarters staff for the program. DOE headquarters currently allocates the equivalent of one full-time analyst to CPSR Program oversight. On August 15, 1991, the Director of the Office of Management Review and Assistance said that he is requesting five staff positions for the CPSR Program, the minimum number he believes is needed at headquarters to implement the corrective actions planned.

To help ensure that procurement deficiencies are corrected, DOE plans to give headquarters some decision-making authority that is now delegated to the field offices. For example, field offices are currently responsible for approving contractors' purchasing systems. In some cases, field offices have approved contractors' purchasing systems when DOE headquarters believed it would have been more appropriate to disapprove them or to lower DOE advance review thresholds. DOE's Director of Procurement said that in the future he, rather than the field offices, will make the decisions to approve or disapprove contractors' purchasing

systems. He also said that in the future decisions on the appropriate advance DOE review and approval thresholds will be made at headquarters rather than at field offices.

To address problems of insufficient field office follow-up on contractor responses to CPSR recommendations, DOE plans to require that field offices (1) report quarterly on the status of contractor responses and (2) submit supporting information that demonstrates progress toward implementation. DOE also plans to establish a system in which field site managers report to the Deputy Secretary and to cognizant program officials when identified problems are not corrected in a timely manner. DOE plans to require that each field office allocate two staff positions that will be devoted to the CPSR Program full-time.

DOE's progress in implementing its CPSR Program changes will be reported in its quarterly High Risk Area Progress Report on Contract Management. DOE estimates that the changes will be in place by the end of fiscal year 1992.

Conclusions

We believe that the corrective actions DOE plans to implement in its CPSR program are appropriate. Assuming that DOE obtains the staffing resources needed and fully and effectively conducts the program, the changes should address the program limitations that we found. We plan to follow up on DOE's actions in the future as part of our work on DOE contractor oversight.

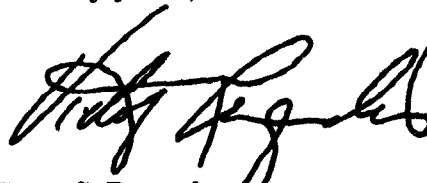
We performed our work at DOE headquarters and at its field offices in Albuquerque, New Mexico, and San Francisco, California, between July 1990 and June 1991. To examine the CPSR Program, we interviewed DOE officials responsible for overseeing and implementing the program, reviewed CPSR records, and analyzed 40 CPSR reports on M&O contractors performed by DOE field offices from 1988 to 1991.

Our work was performed in accordance with generally accepted government auditing standards. As requested, we did not obtain written agency comments on a draft of this report. However, we discussed information in the report with DOE officials, who agreed that it was accurate.

Copies of this report are being sent to congressional energy committees and subcommittees; the Secretary of Energy; the Director, Office of Management and Budget; and other interested parties. If you have any

questions, please call me at (202) 275-1441. Major contributors to this report are listed in appendix I.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Victor S. Rezendes". The signature is fluid and cursive, with the first name being the most prominent.

Victor S. Rezendes
Director, Energy Issues

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Related GAO Products

DOE Management: DOE Needs to Improve Oversight of Subcontracting Practices of Management and Operating Contractors (GAO/T-RCED-91-79, Aug. 1, 1991).

Energy Reports and Testimony: 1990 (GAO/RCED-91-84, Jan. 1991).

Energy Management: DOE Needs to Better Implement Conflict-of-Interest Controls (GAO/RCED-91-15, Dec. 26, 1990).

Energy: Bibliography of GAO Documents January 1986 - December 1989 (GAO/RCED-90-179, July 1990).

Energy Management: DOE Controls Over Contractor Expenditures Need Strengthening (GAO/RCED-87-166, Aug. 28, 1987).

The Subcontracting Practices of Large Department of Energy Contractors Need to Be Improved (GAO/EMD-82-35, Apr. 11, 1982).

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