United States General Accounting Office

GAO

Report to the Chairman, Subcommittee on Oversight and Investigations, Committee on Energy and Commerce, House of Representatives

August 1994

ENERGY MANAGEMENT

Modest Reforms Made in University of California Contracts, but Fees Are Substantially Higher

RESTRICTED--Not to be released outside the General Accounting Office unless specifically approved by the Office of Congressional Relations. RELEASED

GAO/RCED-94-202

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

Resources, Community, and
Economic Development Division

B-246522

August 25, 1994

The Honorable John D. Dingell
Chairman, Subcommittee on Oversight
and Investigations
Committee on Energy and Commerce
House of Representatives

Dear Mr. Chairman:

As you requested, this report provides information on the 5-year contracts that went into effect in 1992 between the Department of Energy (DOE) and the University of California for the management and operation of the Los Alamos National Laboratory, the Lawrence Livermore National Laboratory, and the Lawrence Berkeley Laboratory. The report contains recommendations designed to ensure that (1) DOE has adequate controls over the University of California, including the research projects the university sponsors at the laboratories, and (2) DOE's proposed changes in contracting policy are cost-effective and fair.

As arranged with your office, unless you publicly announce its contents earlier, we will make no further distribution of this report until 30 days after the date of this letter. At that time, we will send copies to the Secretary of Energy; the Inspector General, Department of Energy; the Director, Office of Management and Budget; and other interested parties. We will also make copies available to others on request.

This work was performed under the direction of Victor S. Rezendes, Director, Energy and Science Issues, who can be reached on (202) 512-3841 if you or your staff have any questions. Major contributors to this report are listed in appendix III.

Sincerely yours,

Keith O. Fultz

Keith O. Fultz
Assistant Comptroller General

Executive Summary

Purpose

The Department of Energy (DOE) contracts with the University of California to provide about $2.5 billion a year for research and development work at the Los Alamos National Laboratory, the Lawrence Livermore National Laboratory, and the Lawrence Berkeley Laboratory. In the past, these contracts contained many special, nonstandard clauses that reduced or eliminated DOE's authority to direct the university's actions and contributed to management problems that resulted in losses of millions of dollars' worth of government property, excessive subcontracting costs, and the loss of classified documents. In 1992, DOE and the University of California negotiated new 5-year contracts.

At the request of the Chairman, Subcommittee on Oversight and Investigations, House Committee on Energy and Commerce, GAO examined the terms of these contracts. This report addresses (1) DOE's efforts to add standard clauses typical of DOE's other contracts and eliminate requirements that weakened DOE's authority, (2) the compensation that DOE negotiated for the current contracts, and (3) proposed changes in contracting policy announced by DOE in February 1994 that may apply to these contracts with the university.

Background

To protect the government's interests, DOE's policy is to use the standard clauses for federal contracts in the Federal Acquisition Regulation and DOE's Acquisition Regulation. However, because the University of California has viewed its role as a public service and required terms that reflect mutual interest, the earlier contracts omitted or modified a number of standard clauses. For example, those contracts (1) narrowed the limited instances in which DOE could require the university to incur a financial risk and (2) required DOE and the university to mutually agree to any changes (known as "mutuality requirements"). As a result, DOE could not require the university to make policy or procedural changes in the laboratories' operations, and identified management deficiencies were not corrected for years. In 1991, GAO recommended changes to the contracts to ensure, among other things, that clauses deviating from the standard language provided DOE with authority at least equivalent to that in the standard clauses.[1]

Results in Brief

For the current contracts, DOE negotiated standard clauses for some business management practices—property management, procurement

[1] Energy Management: DOE Has an Opportunity to Improve Its University of California Contracts (GAO/RCED-92-75, Dec. 26, 1991).

systems, and internal audits—that improve DOE's authority and clarify expectations for performance in these areas, potentially resulting in better management of the laboratories. However, these gains could be minimized by a special clause on dispute resolution that continues the principle of mutual agreement. DOE agreed to deviations from standard clauses in instances in which the university expressed strong opposition and did not adopt GAO's recommendation that deviations from standard clauses should provide DOE with authority at least equivalent to that provided in DOE's standard clauses. Some nonstandard clauses in the contracts offer DOE significantly less authority than the standard clauses. For example, the university has the right to direct its own research at the laboratories without DOE's advance approval—a standard requirement—potentially reducing the priority given to DOE's projects. As a result of the nonstandard contract terms, the University of California continues to be subject to fewer controls than DOE's other nonprofit contractors.

In addition, the compensation provided to the university under the contracts has more than doubled—from $13 million to about $30 million a year. In justifying the fee increase, DOE pointed to the university's acceptance of additional financial risk. However, DOE acknowledges that paying fees in exchange for increased risk has been costly and has not improved the accountability of its for-profit contractors. Without criteria for measuring the benefits of having the university assume limited risks against the fees paid, DOE is continuing an approach that has so far been costly and ineffective.

Proposed changes to its contracting policy that DOE announced in February 1994 provide the Department with increased controls and leverage in negotiating its contracts. However, DOE's proposed policies include criteria that may be used to waive the policies in some cases. Given the number of policy waivers DOE has granted to the university in the past, it is uncertain whether the Department will require the university to comply with the new policies, including increasing the financial risks for the contractors or opening the contracts to competition for the first time. If DOE were to waive the competition requirements for the university—one of DOE's largest contractors in terms of expenditures—the inconsistent application of these requirements could reduce DOE's potential negotiating gains.

Principal Findings

DOE Achieved Some Standardization, but New Nonstandard Clauses Weaken Its Authority

DOE made some progress in negotiating standard terms in its contracts with the university. The university has agreed to comply with specific standards and criteria in important business management areas such as property management, procurement, and accounting. The university also accepted criteria for cost allowability more similar to those that generally apply to DOE's other nonprofit contractors. The new contracts permit either DOE or the university to propose modifications to the contracts at any time, to be negotiated "in good faith."

However, like the mutuality requirements in the previous contracts, a new, nonstandard clause establishes a process for resolving disputes that limits DOE's ability to unilaterally direct the university to take actions. The new process, aimed at resolving the chronic communications problems that arose in the past, calls for up to three rounds of negotiations to resolve disputes, may be applied to any issue that either DOE or the university wants to raise, and does not specify time limits for the negotiations. This process has not yet been invoked by either DOE or the university to resolve a dispute, and it is too early to determine if it will work as planned. DOE officials reported that the university has demonstrated a willingness to resolve some disagreements to DOE's satisfaction without resorting to the issues resolution process. However, GAO has concerns about what may happen if the university and DOE cannot readily resolve a dispute. Needed corrective actions could be delayed, as was the case in the past, because the process does not include time limits or a mechanism for DOE to terminate negotiations and invoke its authority to resolve disputes under the standard disputes clause, which is also included in the contracts.

DOE negotiated away other authority that some standard clauses would have provided, thereby limiting its ability to ensure that adequate policies, procedures, and controls are in place to protect the government's interests. For example, one nonstandard clause may enable the university to fund its own research projects at the laboratories without obtaining DOE's approval. All other contractors must get DOE's approval for such work to ensure, among other things, that the Department's own work requirements are met. In another clause, DOE agreed to limit its access to records of communications between laboratory and university attorneys. As a result, management problems or deficiencies could be concealed from DOE.

Increased Fees for the University May Not Be Cost-Effective for DOE and Are Based on Exceptions to DOE's Policies

DOE has substantially increased the compensation it pays the university annually, in large part on the basis of the additional financial risks the university assumed. Most of the $17 million annual increase is directly attributed to these financial risks. However, DOE has reported that a similar approach of paying for-profit contractors higher fees to incur greater financial risk if they take inappropriate actions has not been cost-effective, primarily because the contractors' risks—which are greater than those of the university—were still too limited to bring about improved performance. Also, for the University of California contracts, DOE followed its fee policy for nonprofit contractors rather than its policy for educational institutions, permitting higher fees without the restrictions that would normally apply. It did so because the university would not agree to increased financial risks without increased fees. Furthermore, DOE did not comply with some applicable fee policies, weakening the support and justification for the amounts it agreed to pay.

DOE's Proposed Contract Reforms Allow for Waivers in Some Cases

In its February 1994 proposal, DOE calls for developing more stringent reimbursement policies for its profit-making contractors and applying these same policies to its nonprofit contractors. Because the contractors' financial risks would increase, the Department proposes to modify its official policy against paying fees to nonprofit educational contractors, a policy it has waived in the contracts with the university. This change could eliminate the double standard DOE has created by waiving its policy for the University of California, its largest nonprofit educational contractor. DOE is also proposing to open contracts to competition after no more than one extension and to negotiate the terms of any contract before the decision to extend is made. Thus, the university contracts could be subject to competition for the first time since the laboratories were established more than 40 years ago. However, the proposed rules allow for waivers from the policies in some cases. Given the number of policy waivers that DOE has granted the university, it is not certain that the proposed policies will be applied to the university contracts. Inconsistent application of the proposed contracting reforms could reduce DOE's potential negotiation gains and place at a disadvantage other contractors that are not treated similarly.

Recommendations

GAO recommends that the Secretary of Energy require (1) the Department's Chief Financial Officer and the Deputy Assistant Secretary for Procurement and Assistance Management to review the nonstandard clauses in the university contracts in which DOE has less authority than is provided in DOE's standard clauses and propose contract modifications as appropriate and (2) the University of California to obtain DOE's advance approval for laboratory staff to conduct research for the university. GAO further recommends that the Secretary require the Deputy Assistant Secretary for Procurement and Assistance Management to ensure that (1) paying contractors fees for incurring increased financial risks is cost-effective and (2) the new policies for nonprofit contractors apply to DOE's largest nonprofit contractors, such as the University of California.

Agency Comments

As requested, GAO did not obtain written agency comments on a draft of this report. GAO discussed the facts in this report with DOE officials in the offices of General Counsel, Procurement, Laboratory Management, Field Management, and Defense Programs, including the Deputy Assistant Secretary for Procurement and Assistance Management and the Deputy General Counsel. GAO also discussed the facts with a Special Assistant to the President of the University of California, who offered suggestions for improving accuracy and clarity. The comments from the agency and the university tended to minimize the potential impact of the nonstandard clauses on DOE's ability to effectively oversee the contracts. GAO believes that (1) the standard terms are designed to protect the government's interests, (2) the nonstandard terms affect important areas of contract oversight, and (3) the justifications for the deviations are weak.

Contents

Appendixes

Related GAO Products

Abbreviations

DEAR	DOE Acquisition Regulation
DOE	Department of Energy
FAR	Federal Acquisition Regulation
GAO	General Accounting Office
GSA	General Services Administration
M&O	management and operating

Introduction

The University of California has been the contractor for the Department of Energy's (DOE) Los Alamos National Laboratory, Lawrence Livermore National Laboratory, and Lawrence Berkeley Laboratory since these federal laboratories were established in the 1940s and 1950s. The Los Alamos and Livermore laboratories are dedicated primarily to nuclear weapons research and development, while the Berkeley laboratory focuses on civilian energy research and development, such as energy conservation. DOE's total expenditures at the three laboratories in fiscal year 1993 were about $2.5 billion. The three contracts are substantially the same and typically have been renewed for 5-year periods. During the most recent contract negotiations, in 1991, DOE attempted to incorporate major changes in the new contracts following a series of negative audit reports that documented a number of contract deficiencies. The current contracts, signed in 1992, will expire in 1997.

DOE's Contracting Policies and Practices

DOE uses management and operating (M&O) contracts for its research, development, production, and testing facilities, including the Los Alamos, Livermore, and Berkeley laboratories.[2] The M&O contract approach, conceived by a predecessor agency that developed atomic weapons in the Manhattan Project during World War II, is characterized by limited interference in the contractors' work and indemnification (reimbursement) of almost all the contractors' costs. Under the Manhattan Project, typical procurement methods, such as the requirement for competitive bidding, were relaxed in order to produce atomic capability under emergency conditions and under circumstances of extreme urgency, risk, and security.

After the war, such management contracts were continued for the operation, maintenance, or support of government-owned research, development, production, or testing facilities, both nuclear and nonnuclear. Currently, the majority of DOE's 52 M&O contracts are with for-profit contractors, which received funding of $11.2 billion in fiscal year 1993.[3] However, 18 of these contracts are with 14 different nonprofit organizations, primarily educational institutions, which received $5.1 billion in funding in fiscal year 1993. Based on the level of contract expenditures, the University of California is DOE's largest nonprofit M&O contractor and second largest M&O contractor overall.

[2]DOE had 52 M&O contracts in 1993.

[3]The funding reported here represents contractual obligations to the contractors.

The M&O contracting approach envisions a long-term relationship for the operation of government-owned facilities in a spirit of partnership, rather than the typical arm's length relationship between buyers and sellers of products and services. To protect the government's interests, DOE's policy is to use the standard contract clauses established for federal contracts in the Federal Acquisition Regulation (FAR) and the DOE Acquisition Regulation (DEAR). The FAR establishes uniform policies and procedures for contracting by all executive agencies, and the DEAR contains DOE's regulations implementing and supplementing the FAR. In the DEAR, DOE has established standard clauses specifically for its M&O contracts that may be used in place of some standard FAR clauses. As a result, DOE's M&O contracts contain both FAR and DEAR clauses, some of which apply only to M&O contracts.

DOE manages its M&O contracts through a headquarters organization that sets contract policy; the organization is headed by the Deputy Assistant Secretary for Procurement and Assistance Management, who is also DOE's procurement executive. Field offices award and administer the contracts. DOE's Oakland Operations Office[4] administers the M&O contracts for the Livermore and Berkeley laboratories, while the Albuquerque Operations Office administers the contract for the Los Alamos laboratory. DOE's Chief Financial Officer is responsible for, among other things, (1) developing and maintaining departmental policy on the oversight of contractors' financial management and (2) directing and conducting special reviews.

Nonstandard Clauses in Previous University of California Contracts Resulted in Losses and Inefficiencies

A number of reports by GAO and DOE's Inspector General have shown that DOE's previous M&O contracts with the University of California did not adequately protect the government's interests.[5] Congressional hearings have also addressed management problems at the laboratories that can be attributed, in part, to the nonstandard contract clauses. For example, the Subcommittee on Investigations and Oversight, House Committee on Science, Space, and Technology, held a hearing on July 31, 1991, on the administration of the Livermore, Los Alamos, and Berkeley contracts.[6] GAO and DOE's Inspector General discussed various management problems and

[4]Formerly called the San Francisco Operations Office.

[5]See "Related Reports by DOE's Office of Inspector General" in app. I and "Related GAO Products" at the end of this report.

[6]See DOE Management: Management Problems at the Three DOE Laboratories Operated by the University of California (GAO/T-RCED-91-86, July 31, 1991) and Hearing before the Subcommittee on Investigations and Oversight of the Committee on Science, Space, and Technology, U.S. House of Representatives, No. 57, July 31, 1991.

shortcomings, such as significant losses of government-owned property and classified documents, as well as numerous procurement deficiencies, including the extensive use of costly sole-source subcontracts. In addition, in August 1991 hearings before the Senate Committee on Governmental Affairs, GAO discussed the inappropriate use of sole-source contracts at the Livermore laboratory and the excessive costs that resulted.[7]

The contracts contained many special clauses that (1) reduced or eliminated DOE's authority to direct the university's actions and (2) reduced incentives for the university to be accountable. For example, nonstandard clauses in the contracts restricted DOE from unilaterally requiring the university to make policy and procedural changes in the laboratories' operations, unless the changes were required by law or executive order. These restrictions were referred to as "mutuality requirements" because DOE and the university had to mutually agree to any changes. The clauses on procurement and property management contained these mutuality requirements, and for years the university did not correct significant deficiencies in procurement and property management identified by DOE and GAO because it could not reach agreement with DOE on corrective actions.

The nonstandard property management clause, together with a clause that generally protects the university against liability for losses of government property, fostered a lack of contractor accountability that resulted in the loss of millions of dollars worth of government property. For example, in April 1990 we reported that the Livermore laboratory could not account for about $45 million in government-owned property.[8] Although the university told the press that it subsequently found approximately 99 percent of the missing property, we reported in May of 1991 that about 13 percent of the inventoried equipment, acquired at a cost of $18.6 million, was still missing.[9]

Similarly, a deviation from the standard procurement clause provided the university with a rationale for not obtaining DOE's approval of costly vehicle leases. For example, we found that 58 vehicles were leased from the university at rates that were substantially higher—about $600,000 more

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

[8]Nuclear Security: DOE Oversight of Livermore's Property Management System Is Inadequate (GAO/RCED-90-122, Apr. 18, 1990).

[9]Nuclear Security: Property Control Problems at DOE's Livermore Laboratory Continue (GAO/RCED-91-141, May 16, 1991).

for all the vehicles—than the General Services Administration's (GSA) vehicle leasing rates. Under the leases, a van leased from the university cost $439 per month, while a similar vehicle leased from GSA would have cost $151. Furthermore, the fees paid to the university included an administrative fee of $70 per vehicle each month, primarily for the university's service of submitting monthly bills to the laboratory.

Overall, a 1990 report by DOE's Inspector General identified 21 standard DOE clauses that were either omitted or modified in the University of California contracts, including the procurement and property management clauses.[10] Some other significant deviations omitted or narrowed the limited instances in which DOE's policies would have required the university to incur a financial liability. As a result, the university was not held to the same standards as other nonprofit contractors when DOE evaluated its contract costs. For example, under DOE's historical contracting policies for nonprofit contractors, the only contract costs not paid are those resulting from willful misconduct or lack of good faith by the contractor's top-level management personnel; costs found not to be reasonable on the basis of, among other factors, the exercise of prudent business judgment; and costs specified in the contracts as unallowable. However, DOE's contracts with the university specified only 13 unallowable cost categories, while the standard federal clause included 35 items. As a result, costs that are not allowable under standard federal contracts, such as interest on debt, were paid under the university's contracts.

A special clause included in the contracts also eliminated the university's liability for some unallowable costs if the university certified that the expenditures were made "in good faith." In addition, the contracts did not require contract costs to meet the standard prudent business judgment criterion. Therefore, the university could not be held to this criterion in determining whether costs should be reimbursed.

The contracts also did not include the standard clause that requires M&O contractors to conduct, to DOE's satisfaction, annual internal audits of allowable costs. This deviation led DOE's Inspector General to report a material internal control deficiency in 1991. Another important standard clause, the standard disputes resolution clause, was omitted from the University of California contracts; this clause provides DOE's contracting

[10]General Management Inspection of the Department of Energy's San Francisco Operations Office (DOE/IG-0290, Sept. 20, 1990).

officer with the authority to resolve disputes that arise under the contract.[11]

In Previous Contracts, the University Opposed Many Standard Clauses

The university rejected DOE's attempts to incorporate more standard clauses into its contracts during negotiations for the 5-year contracts in effect from October 1987 through September 1992. The university, which views its role as the contractor for the laboratories as a public service, required contract terms and conditions that reflected mutual interest and intentions and did not expose the University of California or the state of California to financial risks. The university objected to DOE's standard terms, which give DOE authority to direct the contractor's actions,[12] and threatened not to renew the contracts if the standard clauses were included. Because of the weight this threat carried in the contract negotiations with DOE, the university did not accept DOE's negotiation proposals.

Similarly, in 1990 the University of California's President would not agree to a request by the Secretary of Energy to modify the contracts to incorporate the standard clauses on allowable costs and property management. According to the President, such changes would fundamentally alter the nature of the university's relationship with DOE and "carry profound consequences for the University's ability to sustain this relationship." The President indicated that the university would only agree to standard clauses that would preserve the university's "no-risk, no-reward" position, in which the university does not accept either financial risks or benefits.

DOE Considered Options and Studied Issues Regarding Contract Renewals

In an August 1990 memorandum to DOE's General Counsel, the Secretary of Energy acknowledged that the Board of Regents of the University of California could vote in September 1990 to discontinue operating the three DOE laboratories beyond the termination of the contracts in 1992. Believing it would be prudent to study alternatives to the operations of the laboratories, the Secretary requested a study to evaluate the options available for managing the laboratories if DOE did not renew its contracts with the university. Completed in September 1990, the study recommended, among other things, that DOE conduct a market survey of possible replacement contractors and solicit proposals as required under

[11]The contracting officer's decisions may be appealed or litigated.

[12]The university described the standard clauses as creating "an unacceptable superior-subordinate relationship."

the competitive selection process. The report indicated that DOE should start the competitive process immediately because competing the contracts would take at least 2 years.

However, in September 1990 the university's Board of Regents voted to continue operating the laboratories, and DOE's focus shifted from opening the contracts to competition to developing a negotiation strategy for extending the contracts with the university. For example, in November 1990 DOE formed a committee—referred to as the "Steering Committee for Renewal of Contracts at LBL, LANL, and LLNL"—to identify improvements needed in the university's management of the laboratories. The committee identified six such areas. DOE sought to obtain from the university, before the Secretary decided whether to extend the contracts or open them to competition, a commitment to improve two areas that were of major importance to DOE: management oversight of the laboratories and compliance with environmental, safety, and health laws and regulations.

In early 1991, the steering committee held several meetings with the university to determine (1) whether the university was committed to improving its management of the laboratories and (2) how the improvements that the university agreed to make should be implemented. These prenegotiation discussions resulted in the steering committee's recommendation to the Secretary that DOE extend the three contracts and immediately enter into negotiations with the university. They also resulted in a set of ground rules for both parties to use during contract negotiations.

In July 1991, the Secretary authorized the renewal of the university's contracts, and in September 1991, DOE began formal negotiations with the university. In our December 1991 report on the University of California contracts,[13] we recommended changes in the contracts to ensure that adequate policies, procedures, and controls were in place to protect the government's interests. Specifically, we recommended that (1) the new M&O contracts with the University of California contain DOE's standard clauses on procurement and property management and (2) clauses that deviated from any other standard clauses provide DOE with authority at least equivalent to that provided in DOE's standard clauses.

[13]Energy Management: DOE Has an Opportunity to Improve Its University of California Contracts (GAO/RCED-92-75, Dec. 26, 1991).

The University Accepted More Standard Clauses in the Current Contracts

The university agreed to accept several specific standard clauses at the inception of negotiations for the 1992-97 contracts. This change in position occurred after the negative audit reports, discussed above, documented the government's risk under the previous contracts. The university agreed that any deviation from the standard clauses must be appropriately explained by the university and approved by DOE headquarters on the basis of criteria specified at the beginning of the negotiation process. An important element in the university's change in position was DOE's agreement, at the outset of the negotiations, to the university's criteria for justifying deviations from standard clauses. Specifically, DOE agreed to allow modifications in instances in which standard clauses would (1) have an unacceptable impact on the quality of science or academic freedom, (2) be incompatible with the "no-risk, no-reward" operation of the laboratories, (3) result in exposing the university to "unacceptable legal risk," or (4) not sufficiently specify a standard against which DOE would evaluate the university's management performance. Two of the criteria relate to the university's belief that DOE's standard clauses were developed primarily for application to profit-making contractors.[14]

According to a university official, the university took earlier reports of management problems at the laboratory very seriously. As a result of the congressional hearings in 1991, for example, university management increased its involvement in overseeing the contracts and set out to establish a businesslike approach to respond to DOE's concerns. In examining DOE's demands for more accountability, the university wanted to strike a balance between implementing controls to ensure that business aspects were managed in an acceptable manner and providing an environment in which science was not hampered.

The negotiations were concluded in November 1992, when the contracts were executed. According to both university and DOE officials, the negotiations for the 1992 contract involved real negotiations, with compromises on both sides.

[14]DOE has separate clauses for nonprofit contractors in key areas such as financial and legal risk but does not have a comprehensive set of standard clauses for nonprofit contractors.

DOE Has Also Recognized That It Needs to Change Its M&O Contracting Policies

In addition to documenting specific problems with the University of California contracts, GAO and others have identified fundamental weaknesses in DOE's contracting practices. For example, we reported in April 1992 that DOE's contracting approach has fostered an environment that provides opportunities for waste, fraud, abuse, and mismanagement.[15] The problems we found under the M&O contracts included widespread mismanagement of federal property and funds, DOE reimbursements to contractors for money and materials stolen by contractors' employees and for fines that the contractors had incurred for violating environmental laws, missing secret documents, and excessive subcontracting costs. Some of these issues are broader than the specific contracting problems identified with the University of California's contracts, which relate to omitting or altering DOE's standard clauses.

The former and current Secretaries of Energy have taken steps to correct the problems identified by GAO, DOE's Inspector General, and others. For example, under the former Secretary, DOE changed its policies on cost reimbursement for profit-making contractors to make the contractors more accountable to DOE. Also, in June 1993 the current Secretary established a Contract Reform Team to evaluate DOE's contracting practices and formulate specific proposals for improving those practices. The advance copy of the report of the Contract Reform Team, issued in February 1994, proposes a number of changes in contracting policy. We discuss these initiatives further in chapter 3.

Objectives, Scope, and Methodology

As requested by the Chairman, Subcommittee on Oversight and Investigations, House Committee on Energy and Commerce, the overall objective of this review was to examine the terms of DOE's current contracts with the University of California for the Los Alamos, Livermore, and Berkeley laboratories, which went into effect in 1992. As agreed, this report addresses (1) DOE's efforts to add standard clauses typical of other DOE contracts and eliminate requirements that weakened DOE's contract authority, (2) the compensation that DOE negotiated for the current contracts, and (3) proposed changes in contracting policy announced by DOE in February 1994 that may apply to the contracts with the university.

To evaluate the current contracts, we compared the clauses in these contracts with the standard FAR and DEAR clauses and the clauses in the earlier contracts. We also examined DOE's negotiation records and

[15] Energy Management: Vulnerability of DOE's Contracting to Waste, Fraud, Abuse, and Mismanagement (GAO/RCED-92-101, Apr. 10, 1992).

interviewed DOE's chief negotiators. Because the university's chief negotiator has retired, we interviewed university officials who attended the negotiations. We relied primarily on previous GAO and DOE Inspector General reviews for assessments of the university's performance under the earlier contracts and the performance of DOE's M&O contractors in general. Our evaluation of nonstandard contract clauses in the contracts focused on whether the terms protected the government's interests; for example, by providing DOE with the authority to direct the university's actions. We did not evaluate the implementation of the terms of the contracts as part of this review.

To examine contract compensation, we compared the fee payments under the current contracts with the maximum fees payable to nonprofit and for-profit organizations under DOE's guidelines and the compensation paid under the previous contracts. We reviewed and discussed DOE's policy and criteria for paying fees to nonprofit institutions with appropriate DOE officials. We also reviewed the February 1994 report of the Contract Reform Team to determine how the proposed changes in contracting policy would affect the University of California contracts.

We performed our work at DOE's headquarters, Albuquerque Operations Office, and Oakland Operations Office from July 1993 to June 1994 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 the facts in this report with DOE officials in the offices of General Counsel, Procurement, Laboratory Management, Field Management, and Defense Programs, including the Deputy Assistant Secretary for Procurement and Assistance Management and the Deputy General Counsel, who generally agreed with the report's accuracy. We also discussed the facts with a Special Assistant to the President of the University of California, who did not provide an overall assessment of the facts in the report but offered specific suggestions for improving accuracy and clarity. We have incorporated comments from DOE and the university where appropriate.

Current Contracts Include More Standard Clauses, but Other Clauses Weaken DOE's Control

In negotiating its current contracts with the University of California, DOE was partially successful in achieving its goals of (1) increasing the number of standard contract clauses in the contracts and (2) removing provisions that reduced or eliminated DOE's authority to direct the university's actions in business management areas, such as property management. For example, the contracts contain the standard clauses for property management, procurement systems, and internal audits—replacing nonstandard clauses in the earlier contracts that had limited DOE's authority to direct policy and procedural changes at the laboratories. However, DOE's authority under the standard clauses may be weakened by the addition of a new, nonstandard clause establishing an "issues resolution process" aimed at avoiding the serious communications problems and stalemates that occurred under the earlier contracts. The process calls for up to three rounds of negotiations to resolve contractual disputes but does not specify time limits for the negotiations. Because DOE and the university have not yet used the new process to resolve a disagreement, it is too early to determine whether it will result in the timely resolution of disputes.

DOE reported that it agreed to deviate from the standard clauses in instances in which the university expressed strong opposition. As a result, several new provisions in the present contracts provide DOE with less control over the university than the standard clauses or clauses in the previous contracts. For example, DOE does not have authority over some university-sponsored research projects conducted at the laboratories and may not have access to communications between the laboratory attorneys and the university attorneys. Because nonstandard clauses were used, DOE's research projects may not receive sufficient effort and attention, and management problems or deficiencies may not come to DOE's attention.

Current Contracts Include More Standard Contract Clauses

DOE believes its negotiations have accomplished the goals of (1) incorporating the maximum use of standard contract clauses, including standard financial requirements, and (2) eliminating mutuality requirements in business management areas. For example, the contracts now contain the standard clauses for property management, procurement systems, and internal audits. In the previous contracts, nonstandard clauses requiring DOE and the university to mutually agree on any changes DOE wanted in these important business management areas limited DOE's authority to direct the university's actions. The current contracts also contain the standard clauses for accounting standards and the resolution of contractual disputes.

As a result, the laboratories must maintain property management systems that comply with sound business practices and DOE's regulations. They must also implement formal policies, practices, and procedures for subcontracting that are acceptable to DOE and in accordance with DOE's policies. In addition, annual internal audits of costs incurred at the laboratories are required and must be satisfactory to DOE. The laboratories are also required to comply with generally accepted accounting principles and practices. On the whole, these changes affect business management, establishing specific standards and criteria for the university to follow in significant management areas such as accounting.

The current contracts also include more standard criteria for cost allowability[16] and maintain the narrow liability limits that reflect DOE's historical policy of reimbursing nonprofit M&O contractors for almost all costs. As a result, cost allowability criteria in the University of California contracts are now more similar to the standards applied to other nonprofit contractors. For example, the contracts now include 30 of the 35 standard unallowable cost items.[17] In addition, the contracts eliminate the special exemption in the previous contracts allowing the university to avoid liability for some unallowable costs by certifying that the expenditures were made in good faith. Finally, the contracts now include the reasonableness standard for cost allowability; if DOE determines that the university has not exercised prudent business judgment for some expenditures, these costs could be unallowable under the contracts.[18]

The current contracts also continue to reflect DOE's policy of reimbursing nonprofit M&O contractors for property losses and for fines and penalties incurred in the performance of their contracts, except for those caused directly by bad faith or willful misconduct on the part of a few top-level officials. Under these contracts, the liability is limited to six officers of the regents of the University of California and the three laboratory directors. In addition, the contracts reflect the financial risk requirements imposed on all government contractors by the Major Fraud Act of 1988. This act limits the allowability of costs incurred by contractors in connection with defending legal actions brought against them by the federal government or states. As a result, under the current contracts, the university may be liable for the costs of legal actions in some cases.

[16]Such criteria are contract terms that define DOE's general criteria for cost allowability as well as the costs that are specifically allowable and unallowable under the contracts.

[17]DOE determined that five of the standard unallowable cost items, such as research and development costs, did not apply to these contracts, and eight of the standard items were modified somewhat.

[18]This outcome is subject to the issues resolutions process discussed in the following section.

New Clause on Resolving Disputes May Weaken Authority of Standard Clauses

A new, nonstandard clause establishing an issues resolution process that DOE added to the contracts may minimize its success in incorporating standard clauses for business management issues and eliminating provisions that limited its authority. This process calls for up to three rounds of negotiations to resolve disputes and may be applied to any issue that either DOE or the university wants to raise. According to the contracts, this process may be used to resolve conflicts involving claims; policy, operational, management, or procedural issues; and the applicability of DOE's orders[19] or other directives. The intent of the process is to get the right parties together to resolve problems in a timely manner.

The negotiations to resolve disputes are to include officials from DOE, the university, and the laboratories. The first round of negotiations is to include DOE's deputy procurement director, the deputy managers of DOE's Oakland and Albuquerque field offices, and the deputy or associate directors for administration from the laboratories. If these parties cannot reach agreement, they elevate the disagreement to the next level. The subsequent round involves higher-ranking officials, and the third round is negotiated by the Secretary of Energy and the President of the University of California. The process relies on the parties to reach mutual agreement on how to resolve a dispute and is the basis for the university's conclusion that mutuality requirements were retained in the contracts.

Under the process, none of the parties—including the Secretary of Energy—has the authority to direct the way to resolve the conflict. In addition, the contract does not specify when or how to elevate disputes to the next stage. For example, the process does not set time limits for the negotiations at any of the stages.

According to DOE and the university, they needed a process for resolving disputes to overcome the "chronic" communication problems that existed in the past. These problems have led to long-term stalemates. For example, DOE and the Livermore laboratory disagreed for more than 5 years over the appropriate size of the vehicle fleet for the laboratory. Similarly, for years the Livermore laboratory would not agree to establish property management systems that complied with DOE's policies. During this time, we found poor property management controls that resulted in the laboratory's being unable to account for millions of dollars worth of government property.[20]

---

[19] DOE's orders establish its policies and procedures.

[20] GAO/RCED-90-122 and GAO/RCED-91-141.

DOE and the university view the issues resolution process as experimental and have not yet invoked this process to resolve a dispute. While establishing a clear means of resolving contractual conflicts is a sound management approach,[21] the process DOE adopted could diminish the success of its effort to incorporate more standard clauses into the contracts and eliminate contract provisions that reduced the Department's authority to direct the university's actions. For example, while the current contracts contain the standard clause on disputes, which gives DOE's contracting officer the authority to make decisions on contract disputes, the issues resolution clause states that this process must be used first at either party's request. More importantly, the clause does not give DOE the authority to determine that it has spent sufficient time and effort to resolve a dispute and to elevate it to DOE's contracting officer for resolution. As a result, DOE may be required to negotiate with the university for unspecified periods of time.

In addition, the broad scope of the issues resolution process could subject the newly added standard clauses to negotiation. For example, while the contracts contain the standard clause on property management, which establishes the property management systems to be complied with, disagreements could arise over implementation of the requirements.

DOE officials told us they believe that including the standard clause on property management precluded the use of the issues resolution process on this subject. However, we do not find a basis for this opinion since the contracts (1) do not limit the applicability of the process and (2) specify that operational, management, and procedural issues may be resolved through the issues resolution process.

DOE and university officials told us they did not believe the issues resolution process would hamper DOE's ability to oversee the contracts. DOE said that its working relationship with the university has improved and that both sides are communicating more effectively. They noted that the university has been willing to meet with DOE to resolve disagreements to DOE's satisfaction. For example, the officials said that the university made changes to a voluntary separation program in response to objections raised by DOE. This issue was resolved informally without resorting to the issues resolution process. However, DOE officials did acknowledge that the lack of time limits for the process could result in lengthy disagreements.

[21]Government contracting policies encourage "alternate dispute resolution" techniques to avoid costly contract litigation.

The improved working relationship between the university and DOE is a noteworthy achievement considering the difficulties of the recent past. We have concerns, however, about what may happen if the university and DOE cannot readily resolve a dispute. For example, the lack of any time limits or mechanism for DOE to terminate negotiations could prolong disagreements, resulting in a delay in DOE's recovery of moneys that are disputed.

Other Contract Provisions Weaken DOE's Controls Over These Contracts

While some of the clauses added strengthen DOE's controls over the current contracts, several provisions provide DOE with less control over the university than the standard or previous contract clauses. These provisions affect core areas of contract oversight, including the management of laboratory projects, records, inspections, costs, and employment. These nonstandard clauses weaken DOE's ability to effectively oversee the contracts and protect the taxpayers' investment in these laboratories. DOE's official summary of the contract negotiations states that in every case in which DOE agreed to deviations from standard clauses, the basis was to "accommodate a strongly-held negotiating position of the University."

DOE's Authority to Direct Laboratory Projects Is Weakened

Although the current contracts contain a clause requiring DOE's approval for laboratory staff to work on projects for other federal agencies and private institutions, the university believes another nonstandard clause allows it to assign staff to its own projects at the laboratories without DOE's advance approval. The purpose of requiring such approval is, among other things, to ensure that DOE's own work requirements are met and are not inappropriately relegated to a lower priority than work done for other entities.[22]

In the university contracts, the contractual authority to perform work for other entities is set out in a clause entitled "work for others," which is a standard requirement in DOE's other M&O contracts. If the university had DOE-approved laboratory policies on work for others, it would not need approval on a case-by-case basis. This provision applies to work done for entities other than DOE. However, another clause in the contracts, termed "university-directed research and development," gives the university the right to direct and fund its own research at the laboratories. This clause

[22]As a further deviation from DOE policy, the contracts also provide that the case-by-case approval of work-for-others projects would not be needed if the university develops DOE-approved polices and procedures.

states only that the work will be within the contract's general scope of work and performed in accordance with the terms of the contract.

University officials told us that the university is entitled to fund any research project it wishes at the laboratories if the project falls within the scope of work of the contracts. In March of 1994, a university official said that while the university had not funded any research projects at the laboratories in either fiscal year 1993 or 1994, it did plan to begin some projects in the following months. The university does not believe the contract requires it to submit its projects to DOE for approval under the work-for-others clause and was not planning to do so.

During our review, DOE negotiators told us that under the work-for-others clause in the contracts, the university would have to obtain DOE's approval for its university-directed research. Nonetheless, in May 1994 DOE officials told us that (1) it was not DOE's intent to require the university to submit its research projects to DOE for approval and (2) management controls over project staffing in place at the laboratory would ensure that DOE's work would not be negatively affected by research projects sponsored by the university. However, it is not clear why the university alone would be exempt from evaluation to ensure, among other things, that DOE's own requirements will be met, when all other outside projects at the laboratories are subject to such scrutiny.

The potential to disrupt or delay DOE's own research efforts exists whether the party sponsoring the laboratory research is a corporation or small business, another federal agency, or the university. For example, a laboratory scientist working on the Human Genome Project, a major federal biological research project to identify all of the human genes—which is being carried out, in part, at the DOE laboratories managed by the University of California—could also work on a gene project for another entity, potentially at the expense of the government's research efforts.

As a result of our discussions with DOE on this issue, a DOE official subsequently told us that the agency has decided to develop a policy to ensure that the university reports its research projects to DOE before the work starts, similar to the work-for-others process followed by other contractors. In addition, DOE will require that the money for such projects be accounted for separately.

DOE's Access to Laboratory Records May Be Restricted

Although the previous and current contracts with the university contain standard access-to-records provisions allowing DOE to inspect and audit all records, access is limited by other nonstandard clauses. In the previous contracts, DOE's right to make copies of some administrative records was limited.[23] In the current contracts, DOE agreed to restrict the government's access to records by exempting some records created at the laboratories from government scrutiny.[24] For example, under the "contract records" clause, DOE may not examine privileged or confidential communications between university attorneys and laboratory attorneys related to the university's management and operation of the laboratories. As a result, communications between university and laboratory attorneys that DOE should be aware of may not be disclosed—for example, a legal opinion on compliance with DOE's requirements on such subjects as property management. DOE therefore would not be in a position to ensure that the university takes appropriate corrective actions, if warranted, in a timely manner.

According to one of DOE's chief negotiators, DOE had difficulty obtaining access to attorneys' documents under the previous contracts. He said the limits in the current contracts were the result of extensive negotiations with the university and were viewed as an acceptable compromise of the university's broad position that all legal documents should be protected. However, in our opinion, the terms of the current contracts do provide for broad protection of legal documents. By agreeing to this new limit, DOE ceded oversight authority that is part of a standard clause in its M&O contracts. In effect DOE agreed to restrict its access to documents that may relate directly to the management and operation of the laboratories—the task under contract. In addition, the restriction applies to documents prepared by laboratory attorneys, probably at the government's expense.

Other records that the university may restrict under the contract include personnel and medical records,[25] such as files pertaining to employees' qualifications, grievances, discipline, and charges of discrimination; investigations of employees' misconduct; compensation and benefits; and internal health and safety. For these, DOE must make written requests for specific records, identify the federal law that requires such disclosure, and provide the basis for the requested access. DOE also agreed that the

[23]The contracts cited records required to be kept confidential under state law or any written university policy that applied universitywide.

[24]This clause is at variance with GAO's statutory right of access to documents and therefore cannot be enforced against GAO.

[25]Records of personnel's radiation exposure are not restricted, however.

university would not release records relating to employee assistance programs, including alcohol and drug abuse programs and psychiatric evaluations, without a court order.

The contracts state that the university will reply to DOE's requests for records "within a reasonable time." The contracts also state that if the university's general counsel denies access to the requested records, the parties may pursue the request through the issues resolution process discussed earlier.

According to DOE, the process for requesting personnel records was developed to expedite decisions on access to records that may be subject to California's privacy law. Although this law allows the release of information to federal agencies when required by federal law, DOE agreed to abide by the university's judgment about whether or not it can provide a record and to resolve any dispute through the issues resolution process.

By agreeing to these limitations, DOE may have hampered its ability to meet its oversight responsibilities. For example, if DOE wanted to evaluate discrimination charges filed against the university at the laboratory to determine if systemic problems existed, it is not clear whether the university would grant DOE access to the appropriate records in a timely fashion if DOE had to invoke the issues resolution process to obtain access. Delays in receiving these records could occur even though another standard clause in the contracts, entitled "equal opportunity," states that the university will provide DOE with all necessary information to evaluate compliance with all applicable rules, regulations, and orders. Under the contracts, however, special clauses like the contract records clauses have priority over standard clauses.

DOE Agreed to Notify Laboratory Management in Advance of "Surprise" Inspections

Although the contracts contain the standard clause that permits inspection of all work at such time and in such a manner as DOE deems appropriate, this right is restricted by another clause covering research and development work. Specifically, DOE has agreed to conduct surprise inspections—referred to as "no-notice" inspections—only after it has notified laboratory management. This notification requirement, incorporated in the "inspection of research and development" clause, defeats the purpose of surprise inspections and could compromise the ability of auditors to certify that their work meets the requirements of generally accepted government auditing standards. Government auditing standards make an auditor responsible for designing steps and procedures to provide reasonable assurance that abuse or illegal acts will be detected. In some cases, surprise inspections may be the only way to ensure the detection of illegal acts or abuses. DOE's agreement with the university has thus removed an important oversight tool.

DOE's negotiators and university officials told us that they put this provision in place to prevent injuries to auditors during reviews of the laboratories' internal guard forces. The rationale is that laboratory guards are armed, and therefore an auditor on a surprise inspection could get hurt. However, under the contracts, the requirement for giving notice is not limited to inspections of the guard forces. Instead, the requirement is broadly defined, and all work at the facilities could potentially fall under the restriction. That is, if inspections of the guard force are considered to fall under the contracts' research and development provision, it is not clear what type of reviews, if any, would fall under the standard inspections clause that permits surprise inspections.

In subsequent discussions, one of DOE's chief negotiators said that he does not believe DOE would be prevented from conducting appropriate surprise inspections at the laboratories. However, he agreed that the contract terms could be interpreted broadly as limiting DOE's ability to conduct such inspections. He said that DOE could use the issues resolution process if it needed to resolve the issue.

DOE's Ability to Recover Funds From Improper Transactions Is Hindered

In the current contracts, DOE limited its authority to recover improper expenditures made by the university in a timely fashion or, in some cases, at all. DOE negotiators told us that in the earlier contracts, DOE had the authority to deduct from future payments to the university any money the government believed the university had spent improperly. This procedure enabled DOE to reduce (offset) new funding by amounts that were determined to be unallowable. For example, DOE used this authority to withhold $595,000 from the university's management fee to recover funds for unallowable costs. In response, the university filed a lawsuit against DOE in 1991 over the issue of withholding funds from the management allowance for disallowed costs.[26] According to DOE, the university viewed DOE's withholding of funds as a breach of faith, and this became a major issue during the negotiations. In response, DOE agreed to restrict its right "as part of the price of the contracts."

[26]According to DOE, the suit was dropped as a part of the settlement of a False Claims Act suit against the university.

A special clause in the current contracts requires DOE to notify the university of a questionable cost and give the university 60 days to respond in writing. DOE then has 60 days to decide whether it believes the cost is unallowable. If DOE determines the cost is unallowable, the university can either invoke the issues resolution process or reimburse the cost from its own funds. After the issues resolution process has been exhausted, if the parties still dispute the cost, DOE can then offset future funding by the disputed amount. This process could lengthen considerably the time it takes the government to recover money improperly spent by the university and also removes the university's incentive to settle such issues promptly.

Similarly, DOE has given up authority to recoup money under the Anti-Kickback Enforcement Act of 1986, as amended. The act provides the government with a series of remedies when a contractor or the contractor's employee has received improper compensation in return for doing business with the person providing the compensation (kickback). The act gives the government, in this case DOE, discretionary authority to offset the kickback against future payments to the contractor.

The current contracts with the university limit DOE's offset authority to those circumstances in which the university's regents or a laboratory director have made or received a kickback. In all other cases involving university employees, the government is limited to either seeking the money directly from the employee or requiring the university to obtain the money from the person who gave the kickback, rather than reducing future contract payments by the amount of the kickback. The university has effectively shifted the risk of its employees' misbehavior from the university to the employees or the parties offering kickbacks, such as subcontractors. However, an employee may not have the funds to pay the government and could declare bankruptcy. As a result, DOE's ability to recover any kickbacks that university employees may receive could be hindered.

Restriction of DOE's Authority Over Personnel Matters Continues

A standard DOE contract clause gives DOE the authority to require contractors to fire their employees for cause. However, this clause has not been included in the university contracts.[27] Consequently, DOE cannot require the university to remove incompetent or careless employees because the key oversight role for personnel administration resides with the university. According to DOE's negotiators, discussion about the

[27]The previous and current contracts only require that the laboratory directors and deputy directors be acceptable to DOE.

standard clause governing this issue did not even "make it to the table." Under the ground rules agreed to before formal negotiations were initiated, both parties agreed to allow the laboratories to manage personnel according to university policy and with sole discretion to hire and fire employees.

DOE agreed to this broad limit on personnel management despite a January 1991 internal DOE report prepared to support contract negotiations that noted major deficiencies in executive compensation and in overall compensation management at the laboratories managed by the university. DOE also was not successful in revising contract terms on pay policies, recommended by DOE's Director of Contractor Human Resource Management, that would have lowered contract costs.

DOE Can Propose Contract Modifications at Any Time

DOE does not need to wait until the current contracts with the University of California expire to implement policy or any other changes in the contracts. The contracts for the three DOE laboratories include a provision that either DOE or the University of California may propose contract modifications at any time during the term of the contracts and that such modifications will be negotiated in good faith.

Conclusions

By including more standard clauses, DOE has made some progress in obtaining better contract terms in its management and operating contracts with the University of California for the Los Alamos, Livermore, and Berkeley laboratories. The university has agreed to comply with specific standards and criteria in important business management areas such as property management, procurement, and accounting. These changes provide greater clarity about DOE's expectations of performance in these areas, which could result in better management of the DOE laboratories.

However, other nonstandard clauses in the contracts may constrict DOE's authority. For example, we are concerned with the new clause establishing an issues resolution process. We agree that some system for resolving disputes, in addition to the standard disputes clause, is an appropriate and worthy idea. In addition, we are encouraged that DOE and the university have made progress in improving their working relationship and in resolving disagreements. Nonetheless, we have some concerns about whether the issues resolution process will work as planned to overcome the serious communication problems and stalemates that occurred in the past. The process also may be unnecessarily lengthy and burdensome. In any event, success will require continued good faith and a strong commitment on the part of both parties. We are also concerned that DOE's plans to require the university to notify DOE of any university-sponsored research at the laboratories may not provide DOE with adequate controls to ensure that its own work is not jeopardized if DOE does not have the authority to approve such projects.

DOE did not adopt GAO's previous recommendation that deviations from standard clauses should provide DOE with authority at least equivalent to that provided in DOE's standard clauses. As a result, DOE's ability to ensure that adequate policies, procedures, and controls are in place to protect the government's interests is undermined. In addition, the University of California continues to be subject to fewer controls than DOE's other nonprofit contractors.

Recommendations

We recommend that the Secretary of Energy require the Department's Chief Financial Officer and Deputy Assistant Secretary for Procurement and Assistance Management to review the instances in which DOE has less authority under the University of California contracts than is provided in the standard clauses. The officials should determine whether the bases for allowing the deviations are sound and whether DOE should use its authority to propose contract modifications at any time to make the changes needed to better protect the government's interests.

To ensure that DOE maintains adequate controls over the work conducted at the laboratories, we also recommend that the Secretary of Energy require the University of California to obtain DOE's advance approval for any research projects the university sponsors at the laboratory.

Views of DOE and the University and Our Evaluation

Overall, when commenting on the facts presented in this chapter, DOE officials from the offices of General Counsel, Procurement, Laboratory Management, Field Management, and Defense Programs indicated a willingness to reexamine some of the contract terms and propose contract modifications to better protect the government's interests. However, the DOE officials, as well as the university official commenting on the facts, minimized the potential impacts of the nonstandard clauses on DOE's ability to effectively oversee the contracts. We do not know whether the nonstandard clauses will, in fact, cause or contribute to serious problems at the laboratories. Our view is that (1) the standard terms are designed to protect the government's interests, (2) the nonstandard terms affect important areas of contract oversight, and (3) the justifications for the deviations are weak.

Increased Fees May Not Be Cost-Effective for DOE and Are Based on Exceptions to DOE's Policies

Compensation provided to the University of California under the contracts for the three laboratories increased from $13 million a year to about $30 million a year under the current contracts. DOE justified the increase, in large part, on the basis of additional financial risks the university assumed under the contracts. However, the contracts continue to reflect DOE's historical contracting policies for nonprofit contractors and, as such, provide for only limited financial risks. Furthermore, DOE's program to improve contractors' operations by paying for-profit contractors higher fees to incur greater financial risk if they take inappropriate actions has not been cost-effective or improved the contractors' performance. This is in large measure because the financial risks borne by the contractors are still too limited to bring about improved performance.

DOE used its fee policy for nonprofit contractors for the University of California contracts rather than its policy for educational institutions, thus permitting higher fees without the restrictions that would normally apply. DOE agreed to waive its policies for educational institutions because the university would not agree to contract changes that increased its financial risk without higher fees for such risks. The university could continue to be exempted from DOE's contracting policies, even under the proposed contract reform policies that DOE announced in February 1994. The proposed contracting reforms—including paying fees to all contractors that assume increased levels of financial risk and opening the M&O contracts to competition periodically—provide for waivers that DOE may grant. Given the number of waivers from its policies that DOE has granted the university in the past, the extent to which these proposed policies will be applied to the university is unclear at this time.

DOE Is Paying the University New and Larger Fees

The current contracts increased the compensation DOE pays to the university by about $17 million a year, primarily by adding a new fee relating to financial risks borne by the university. The contracts also provided for substantial increases in lease payments—justified in part as compensation to the university for renewing the contracts.

Under the 5-year contracts in effect from 1987 to 1992, DOE paid the university an annual fee, called a management allowance, ranging from $12 million to $13 million. The largest component of the management allowance—$8 million—was for costs incurred by the university in support of the laboratories, called indirect costs. In addition, under agreements dating back to 1948, the government paid the university a nominal rental fee—generally $1 per lease—for the use of land for the

Lawrence Berkeley Laboratory, which is located on the University of California's Berkeley campus.

DOE provided the balance of the annual management allowance for "complementary and beneficial" activities, including university-funded special equipment and facilities to be used by visiting scientists and graduate students at the laboratories, and increased oversight by the university and Board of Regents of the operations of the laboratories. The amount provided for complementary and beneficial activities was initially $4 million, increasing each year by $250,000 up to $5 million in the fifth year of the contracts.

The 5-year contracts that took effect in 1992 provide for annual payments to the university of about $30 million a year for

- a new management fee (referred to as a risk fee in this report),[28] fixed at $14 million and justified on the basis of the additional financial risks the university agreed to assume under the new contracts;
- the university's indirect costs, fixed at $6 million;
- "ground lease" payments for the Lawrence Berkeley Laboratory, fixed at $5 million; and
- the establishment of a new University of California laboratory management oversight unit, at an estimated first-year cost of $5 million.

The fixed annual payments total $25 million, and the additional variable amount will cover the actual costs incurred by the university for the laboratory management oversight unit. According to the university, first-year expenditures for the management oversight unit were approximately $3.3 million.

[28]While the contracts call this a performance management fee, it is a fixed fee that does not vary with DOE's assessment of laboratory performance.

Experience With Other Contractors Indicates That the University's New Risk Fee May Not Be Cost-Beneficial for DOE

DOE has substantially increased the amount it pays in fees to its for-profit contractors, primarily on the basis of the additional financial risks the contractors must bear. The objective of these increases was to improve the performance of contractors by increasing their financial risk for any inappropriate actions they take, while providing the opportunity to earn increased fees. Similarly, DOE has substantially increased its compensation to the University of California, primarily on the basis of financial risks the university bears. However, recent reports by DOE and DOE's Inspector General concluded that increasing fees to compensate for the minimal risks the for-profit contractors assume was not achieving DOE's objective. For example, the February 1994 report of DOE's Contract Reform Team concluded that the risks borne by the contractors were still too limited to bring about improved performance.[29]

Nonetheless, the current University of California contracts include risk fees of $14 million a year, while continuing DOE's historical policy of indemnifying almost all the costs incurred by its nonprofit contractors. DOE officials said that, in negotiating the fee amount, they took into consideration that the university (1) had in previous contracts, but gave up, protection against incurring unallowable contract costs and (2) faced potential financial risk for some legal costs required by the Major Fraud Act of 1988. DOE officials said this was the first M&O contract to deal with the limitation on proceeding (legal) costs under the Major Fraud Act.

We note that, with the exception of the legal costs that all government contractors are now potentially responsible for because of the fraud statute, the new cost allowability criteria in the university contracts only brought these contracts more in line with DOE's contracting policies. Other nonprofit contractors, such as the University of Chicago, have not received additional fees for bearing the limited financial risks required by DOE's policies.[30] Furthermore, DOE did not attempt to quantify the increased financial risks under the University of California contracts during contract negotiations or develop criteria to evaluate the costs and benefits of risk fees paid to contractors to ensure that the policy will be cost-effective.

DOE's recent experience in paying for-profit M&O contractors higher fees to assume greater risk provides a perspective for evaluating the university's

[29]Making Contracting Work Better and Cost Less, Report of the Contract Reform Team, U.S. Department of Energy, advance copy (Feb. 1994).

[30]The University of Chicago's current contract for DOE's Argonne National Laboratory provides for about $4 million in compensation relating primarily to the university's indirect costs.

increased risk and the potential benefits to DOE. In 1991, DOE took steps to expand the risk and accountability of its profit-making M&O contractors in managing DOE facilities. Among other things, DOE promulgated a rule—termed the "accountability rule"—that revised the fee structure to compensate contractors for taking greater financial risk and to provide incentives for improved performance. Under the rule, DOE held contractors rather than the government responsible for costs that a prudent contractor could have avoided. The accountability rule added a new category of unallowable costs, called "avoidable costs." A contractor could be held liable for the following types of avoidable costs if they resulted from negligence or willful misconduct by contractors' or subcontractors' personnel: fines and penalties; unnecessary or excessive program costs; and damage, destruction, loss, and theft or unauthorized use of government property.

Recently, DOE's Inspector General examined the implementation of the accountability rule and found that DOE had paid higher fees but had not received any measurable benefits in return.[31] The report of DOE's Contract Reform Team agrees with the Inspector General that the accountability rule has had little measurable impact on the accountability or performance of for-profit contractors but has resulted in significant cost increases to DOE. The report of DOE's Inspector General concluded that the accountability rule did not appear to be meeting its objectives because DOE had not evaluated the potential costs and benefits of the rule before its implementation.[32] The report also noted that under six contracts with estimated costs of over $3.7 billion for fiscal year 1992, the for-profit contractors reported about $1 million in avoidable costs. However, DOE had paid increased fees of $22.8 million to the contractors for bearing increased risk for such costs and funded $2.5 million in annual expenses to administer the rule.

In comparing the university's risks and fees with DOE's experience with for-profit contracts under the accountability rule, it is important to consider that the potential risks that the profit-making contractors face are greater than the risks borne by the university under its current contracts. For example, the university's liability for property damage and fines and penalties is limited to instances that can be attributed to the bad faith or willful misconduct of six top-level University of California officials and the three laboratory directors. In contrast, for-profit contractors' liability for

[31] Audit of Implementation of the Accountability Rule (DOE/IG 0339, Jan. 21, 1994).

[32] While DOE did not agree with the Inspector General's recommendation to suspend application of the accountability rule to other contracts, it did agree to study the costs and benefits of the rule.

the same activities extends to all the contractors' employees, and the exposure to financial risks is therefore higher. In addition, the university contracts do not include the "avoidable cost" category of unallowable costs, which currently applies only to for-profit contractors. As a result, the university contracts are even less likely than DOE's approach with for-profit contractors to achieve the Department's objectives and be cost-beneficial.

In addition, fees paid to the for-profit contractors are linked to performance assessments, while the fees to the University of California are not. The university believes the fixed fee provides a significant incentive to comply with DOE's requirements because it plans to allocate a portion of the remaining balance of the risk fee, after paying unallowable costs, to the laboratories with the best management record in terms of unallowable costs. These funds are to be used for university-directed research. However, paying a fixed fee provides DOE with less control over the university than over the for-profit contractors whose fee amounts depend on DOE's performance ratings. The fixed-fee structure gives the university the incentive to avoid unallowable costs but does not give DOE the ability to pay the fee based on performance measures that reflect DOE's management priorities.

DOE Waived Its Policy and Paid Unrestricted Fees to the University

In the university contracts, DOE waived not only its fee policy for educational institutions but also the rules the agency would normally follow for such waivers. The policy states that fees are generally not paid for M&O contracts with educational institutions, but the policy does permit the payment of a management allowance "in special circumstances." In 1991, DOE clarified this policy by requiring that management allowances paid to educational institutions generally be provided only for costs that benefit DOE's operations. DOE clarified the policy in response to questions by DOE's Inspector General about the size of and increases in the management allowance in the university's 1987-92 contracts.[33]

DOE's fee policies do not state the rationale for treating nonprofit educational institutions differently from all other nonprofit entities. According to the Director of DOE's Office of Procurement, the fee policy for educational institutions reflects the view that universities would contract with DOE primarily as a public service, not because of a desire to raise revenues by conducting business operations. The primary educational mission of universities is funded through various means, such

[33]Compensation was 50 percent higher than provided for in the 1982-87 contracts.

as endowments, state funding, and grants. In contrast, the primary mission of other nonprofit entities can involve business operations, such as waste management, which need revenues to be sustained.

According to the Director of DOE's Office of Procurement, DOE followed its fee policy for nonprofit M&O contractors rather than its policy for educational institutions because the university would not agree to accept increased financial risks without higher fees for such risks. The university believes that the nature of the work conducted at the Livermore and Los Alamos laboratories—particularly the nuclear weapons design work—carries a greater potential for liability than the risks borne by other nonprofit M&O contractors. The nonprofit fee policy authorizes fees for, among other things, financial risk and does not place any restrictions on the use of the fees. As a result, DOE was able to negotiate contracts with the university that included risk fees and generally do not restrict the university's use of the contract fees.

The nature of the work conducted by some of DOE's other educational institution contractors may not involve the same level of financial risk as that borne by the University of California in its weapons work. However, because other educational institutions are generally not eligible for risk fees under DOE's policies, the special waiver of the fee policy for educational institutions granted to the University of California may put these other contractors at a disadvantage.[34] DOE's proposed contract reforms, discussed in the following section, include changes in fee policies that could eliminate such potential inequities in the payment of fees.

Finally, in addition to waiving its fee policy for educational institutions, DOE did not follow procedures designed to promote fee consistency and uniformity. DOE also used an alternative policy to pay the university's indirect costs. Following DOE's fee procedures would have required (1) more specific justification of the fee levels provided for in the contracts and (2) approval of fee amounts in excess of the maximum allowable fee by DOE's procurement executive.[35] Since DOE's top management was closely involved in these negotiations, following the procedures would not necessarily have resulted in the approval of lower fees. However, at a minimum, DOE's goal of achieving some degree of consistency and uniformity in fees is undermined when DOE negotiators do

[34]If other educational institutions were paid fees, DOE's policies state that the financial risks borne should be evaluated in determining the appropriate fees to be paid.

[35]DOE's policies include schedules that establish maximum allowable fees for its M&O contracts based on certain contract costs.

not follow the procedures designed for this purpose. We have included a more detailed explanation of the exceptions to DOE's standard policies and procedures in the university contracts in appendix II.

DOE's Proposed Contract Reforms Leave the Door Open for Continued Waivers for the University

The February 1994 report of DOE's Contract Reform Team acknowledges the numerous contracting problems identified by DOE's Inspector General and GAO and contains a number of recommendations to improve DOE's contracting practices for its M&O contracts. However, the contracting reforms may not be applied to all contracts, as the proposed policies include provisions that permit exemptions—for example, "in unusual circumstances." Among other things, the proposed changes would increase the financial risks to be borne by all contractors, both for-profit and nonprofit contractors, and would periodically subject these long-term contracts to competition. These changes could have a significant impact on future M&O contracts, including those between DOE and the University of California.

Specifically, DOE is proposing to establish more stringent cost reimbursement policies for its profit-making contractors and apply these same policies to its nonprofit contractors. Because the changes would call for contractors to assume increased levels of financial risk, DOE proposes to modify its official policy against paying fees to educational institutions. Doing so would eliminate the double standard DOE has created by waiving its policy for the University of California, its largest nonprofit educational M&O contractor. According to the Contract Reform Team's report, DOE is to develop the policies implementing these changes in 1994. As a result, fees for DOE's nonprofit educational contractors may become more prevalent.

DOE believes that the development of a fee and risk-sharing policy for nonprofit educational institutions should address the special concerns of nonprofits; for example, protecting university endowments and preserving limited assets. While DOE has already waived its fee policy for the university contracts, the proposed policy would generally allow the payment of fees only to nonprofit contractors that agree to accept the same cost reimbursement rules as for-profit organizations.

DOE's more stringent proposed changes in its cost reimbursement policies pertain to fines and penalties, third-party liabilities, and costs resulting from damage to or loss of government property. Now, DOE has the burden of proving that such costs are not allowable; under the proposed change, the contractor would have to show why a questioned cost should be allowable. For example, costs associated with losses of government property would be unallowable unless the contractor could show that the losses did not result from willful misconduct or a failure to exercise prudent business judgment.

Given the university's historical opposition to assuming risks and the substantial fee increases in the current contracts to compensate the university for assuming limited risks, it is unclear (1) whether the university would agree to accept the additional risks identified in DOE's proposals or (2) what fee level would be needed to convince the university to accept such risks. In this regard, the report of the Contract Reform Team also states that DOE could waive these new rules for nonprofit contractors if DOE needed to have nonprofit contractors compete for a contract and the rules made it unlikely that they would.

Other key policy proposals that could significantly affect the University of California contracts are (1) opening M&O contracts to competition after no more than one extension and (2) negotiating the terms of any extended contract before making the decision to extend the contracts. If DOE implements these changes across the board, the university contracts would be subject to competition for the first time since the laboratories were established more than 40 years ago, and DOE would be in a stronger negotiating position. In cases in which DOE plans to extend contracts, rather than opening them to competition, DOE would also gain negotiating leverage by requiring that the contract terms be agreed to before DOE commits to the contract extension. Currently, DOE decides initially whether to extend a contract or open it to competition. If DOE decides to extend the contract, it enters into contract negotiations on a "sole-source" basis, which reduces its negotiating leverage. Under the proposed policies, DOE would have leverage to respond if a contractor threatens not to renew a contract.

However, the report of the Contract Reform Team indicates the competition requirement would not be enforced "in unusual circumstances." Because the proposed policy acknowledges that DOE may grant waivers—and because it has historically granted a number of policy waivers for the university contracts—it is not clear at this time whether DOE will open the university contracts to competition.

Conclusions

The current university contracts will likely produce the same disappointing results as DOE's recent accountability program for profit-making organizations. The university bears even less risk than the for-profits because its contracts reflect DOE's historical policy of reimbursing nonprofit contractors for almost all costs. In addition, the substantial fees paid to the university to cover increased financial risks may provide an incentive for the university to avoid unallowable costs but may not provide an incentive to control costs overall and manage efficiently. Without criteria for determining whether the benefits of having the university assume such risks are offset by the fees paid, DOE is perpetuating a costly and ineffective approach.

In general, we support the recommendations of DOE's Contract Reform Team. However, the proposals will not achieve their intended purposes unless rigorous cost-benefit analyses are included in contract negotiations. Without such analyses, DOE may perpetuate the conditions under the present contracts, whereby it pays the university substantially higher fees than the risks appear to warrant.

Furthermore, because the University of California is the largest of DOE's M&O nonprofit contractors, imposing fewer requirements on the university could jeopardize successful implementation of the changes in policy for nonprofit organizations designed to improve the contractors' performance. For example, if the university would not agree to accept the same financial risks as for-profit contractors, DOE would have to ensure that (1) its other nonprofit educational contractors could receive waivers from the requirements and (2) all contractors that do not accept the same risks as for-profit contractors are subject to the same DOE fee criteria. Similarly, if DOE were to waive the competition requirements for the university under its proposed "unusual circumstances" criterion, the inconsistent application of these requirements would reduce DOE's potential negotiating gains, place at a disadvantage other current M&O contractors that must compete to renew their contracts, and preclude other qualified contractors from competing for the Los Alamos, Livermore, and Berkeley contracts.

Recommendations

We recommend that the Secretary of Energy require the Deputy Assistant Secretary for Procurement and Assistance Management to ensure that the (1) fees paid to contractors for incurring increased financial risks are cost-effective by developing criteria for measuring the costs and benefits to the government of this approach and (2) new policies for nonprofit M&O contractors apply to DOE's largest nonprofit contractors, such as the University of California.

Views of DOE and the University of California

The comments from both DOE and university officials on the facts presented in this chapter and appendix II generally provided suggestions for improving clarity and accuracy. We have incorporated their comments where appropriate.

Related Reports by DOE's Inspector General

Audit of Implementation of the Accountability Rule (DOE/IG-0339, Jan. 21, 1994).

Audit of Personal Property Management at Los Alamos National Laboratory (DOE/IG-0338, Dec. 7, 1993).

Financial Administration of Work for Nonfederal Sponsors—DOE Field Office, Albuquerque, New Mexico (WR-BC-91-02, Sept. 30, 1991).

Departmentwide Audit of the Visibility over the Status of Nuclear Materials (DOE/IG-0296, Aug. 30, 1991).

General Management Inspection of the Department of Energy's San Francisco Operations Office (DOE/IG-0290, Sept. 20, 1990).

Departmentwide Audit of Carrier Selection and Invoice Verification (DOE/IG-0278, Nov. 29, 1989).

Indemnification of the Department of Energy's Management and Operating Contractors (DOE/IG-0272, Sept. 22, 1989).

Waivers of DOE's Fee Policies and Procedures Reflected in the University of California Contracts

DOE's Fee Policies and Procedures

Because DOE waived its fee policy for educational institutions for the University of California contracts and chose to treat the university as a nonprofit entity, DOE's general fee policies for management and operating (M&O) contracts became applicable to these contracts. Under these policies, fees for M&O contracts include compensation for (1) contract management;[36] (2) use of the contractor's resources; (3) the financial risk that all contract costs may not be reimbursable; and (4) the home office's general and administrative expenses—that is, indirect costs. In addition, the fees agreed to under M&O contracts are to be commensurate with the difficulty of the work and the level of required skills, demonstrated excellence, and the contractors' contributions or use of their own facilities or investment capital. DOE's policies also state that, in determining the appropriate fee, negotiators can evaluate alternative investment opportunities available to a contractor if, for example, the contractor's resources could be used to make a profit in some other field.

DOE's policies recommend basing the fees for M&O contractors on significant factors, such as financial risk and use of the contractors' resources; these factors are to be evaluated and assigned appropriate values. To promote a reasonable degree of consistency and uniformity in the process for determining fees, the policies include fee schedules that establish maximum allowable fees for M&O contracts based upon certain contract costs. Any fees in excess of the allowable amounts are to be justified in writing and approved by DOE's procurement executive.

For the University of California contracts, DOE's negotiators did not follow a number of these policies and processes. Consequently, the negotiators did not have to justify amounts in excess of the fees allowed under DOE's policies and obtain the approval of DOE's procurement executive.

Lease Compensation

The negotiators did not include the $5 million annual compensation for leases covering university-owned land—the contractor's resource—as a component in the fees. DOE has rented land for the Lawrence Berkeley Laboratory from the University of California under long-term agreements with nominal fees.[37] For example, under four leases, the government paid a one-time fee of $1 for 50-year leases; under another lease, it paid $1 a year over the 50-year lease term. The first lease would have expired in

[36]The policies use the phrase "for the entrepreneurial function of organizing and managing resources."

[37]Unlike the Lawrence Livermore and Los Alamos national laboratories, which are government-owned facilities on government property, the Lawrence Berkeley Laboratory is located on the University of California's Berkeley campus.

1998, and all of the leases could have continued in effect for the term of the current contracts. DOE's negotiation record states that the $5 million annual payment is for (1) compensation to the university for agreeing to the contracts and (2) recognition that the university-owned land and facilities[38] have grown substantially in value since the agreements were initiated in 1948.

According to the university, the university's negotiators determined that the leases represented assets and that compensation for the use of these assets was appropriate, as DOE and the university were defining a more businesslike relationship under the new contracts.

DOE officials provided somewhat different, but not inconsistent, explanations as to why the lease payments were not viewed as fees. According to the Director of DOE's Office of Procurement, DOE's negotiators did not consider the university's request for compensation for the use of the land as a request for a fee—which in their view implies a profit. The Director said DOE negotiated in good faith in response to the university's request for substantial lease payments for the use of land that the university had been providing essentially free of charge to DOE for many years. Because of this perspective, the risk fee and lease payments were not lumped together and analyzed in terms of the maximum allowable fee that would be permissible.

Officials at DOE's Oakland office, with whom we discussed compensation, offered another perspective. They reported that the lease payments were viewed as contract costs, which may be reimbursed, rather than as a fee. However, they acknowledged that DOE's negotiators did not obtain any cost data from the university to support the $5 million annual fee on a cost-reimbursement basis. Instead, the fee amount was based on alternative investment opportunities. DOE officials used an estimate that the annual lease value of comparable land was about $36 million a year. On the basis of this estimate, the negotiators determined that the amount the university requested was fair and reasonable and agreed to an annual $5 million fixed payment in lieu of reimbursement of the actual cost.

Additionally, DOE's Procurement Director said the negotiators considered this lease payment to the University of California comparable to compensation paid to Princeton University for land used for DOE's Princeton Plasma Physics Laboratory. DOE also does not view the payment to Princeton as a fee. However, the cases are not comparable because

[38]DOE paid for and owns the facilities constructed for the federal laboratory on the university's land.

DOE's general fee policies do not apply to Princeton University. Princeton is treated as an educational institution and, unlike the University of California, does not receive a fee to cover items such as financial risk and the use of the contractor's resources.

If the lease payments to the University of California had been included as a component of the management risk fee, as outlined in DOE's fee policies, the negotiators would have compared $19 million in proposed fees with the maximum allowable fee of $15.8 million they computed,[39] instead of limiting the comparison to the $14 million risk fee. The procurement executive's specific approval would have been required to exceed the maximum allowable fee.

Indirect Costs

The negotiators did not follow DOE's standard fee policy, which assumes that the fees paid include compensation for contractors' indirect costs. Instead, using an alternative policy that allows indirect costs to be treated as reimbursable costs rather than as fees, the negotiators agreed to pay additional compensation of $6 million annually for the university's indirect costs. Specifically, DOE's fee policies state that in instances where the standard fee allowance may be insufficient to adequately recognize a contractor's indirect costs and such costs appear to have a directly benefiting relationship to the DOE program, they may be either (1) the basis for requesting fee amounts in excess of the maximum allowable fee or (2) approved by a contract official as a reimbursable contract cost if a fair and reasonable amount can be agreed upon. The negotiators chose to justify the costs as reimbursement for fair and reasonable indirect costs.[40] If the alternative policy had not been used, the negotiators would have had to ask the procurement executive to approve additional annual fees in excess of DOE's maximum allowable amount.

Computation of the Maximum Allowable Fee

The maximum allowable fee is a percentage of a fee base.[41] DOE's regulations define this base as the cost of the production or research and development work to be performed, excluding a number of contract costs, such as those for land, buildings, and facilities; those for subcontracts; and those that are reimbursed, for example, work for others.

[39]As discussed below, the negotiators did not use the proper methodology for computing the maximum fee.

[40]This justification was not included in DOE's record of negotiation. DOE provided us with the rationale in June 1994 in response to questions we raised throughout our review.

[41]The percentage applied depends upon the amount of the fee base.

For the University of California contracts, DOE's negotiators computed fees for cost categories such as the reimbursable costs of work for others. The negotiators used the total estimated expenditures in fiscal year 1993 as the base, including sizeable expenditures for reimbursable work. As a result of including reimbursable work in the fee base, the maximum fee the negotiators used as a basis for evaluating and justifying the university's risk fee may have been substantially higher than is appropriate.

Expenditure of Fees

Because DOE's negotiators used the fee policy for nonprofit organizations rather than the policy for educational institutions, the compensation criteria developed as a result of questions about the management allowance paid to the university under the previous contracts did not apply. For example, DOE's steering committee for the renewal of the University of California contracts, discussed in chapter 1, criticized the fact that previous contracts permitted the university to spend the management allowance for purposes of "mutual benefit" to DOE and the university rather than requiring the university to use the fee for laboratory operations. That is, the committee was concerned about the funding in the previous contracts for "complementary and beneficial" activities discussed in chapter 3. However, DOE's policy on nonprofit entities does not require that fees cover costs that benefit DOE's operations, and DOE gave the university the right to spend most of the fees at its discretion. The university stated that it would spend the $14 million annual risk fee, less unallowable costs, in support of the laboratory "to the extent that it is possible to do so." The university indicated it would use the fees for university-directed research at the laboratories as well as for complementary and beneficial activities. The university did not specify to DOE how it would spend the $5 million lease payments. Finally, while the contracts expressly state that the university has the absolute right to spend the $6 million annual payment in lieu of indirect costs at its sole discretion, the contracts also state the understanding of both parties that the university will pay $5.7 million of that annual payment to the state of California as compensation for its support of the university system.

Major Contributors to This Report

Resources, Community, and Economic Development Division, Washington, D.C.	Jim Wells, Associate Director Doris E.L. Cannon, Assistant Director Kathleen J. Turner, Assignment Manager Carol A. Ruchala, Evaluator-in-Charge Christine M.B. Fishkin, Senior Evaluator Sandra J. Eggart, Senior Evaluator Eileen Larence, Report Reviewer Phyllis Turner, Reports Analyst
Denver Regional Office	Peter Fernandez, Regional Assignment Manager
Office of the General Counsel	Michael Burros, Senior Attorney

Related GAO Products

Energy Management: Controls Over the Livermore Laboratory's Indirect Costs Are Inadequate (GAO/RCED-94-34, Nov. 16, 1993).

Energy Management: DOE Has Improved Oversight of Its Work for Others Program (GAO/RCED-93-111, Apr. 7, 1993).

Department of Energy Contract Management (GAO/HR-93-9. Dec. 1992).

Energy Management: DOE Has an Opportunity to Improve Its University of California Contracts (GAO/RCED-92-75, Dec. 26, 1991).

Energy Management: Tightening Fee Process and Contractor Accountability Will Challenge DOE (GAO/RCED-92-9, Oct. 30, 1991).

Energy Management: Contract Audit Problems Create the Potential for Fraud, Waste, and Abuse (GAO/RCED-92-41, Oct. 11, 1991).

Energy Management: DOE Actions to Improve Oversight of Contractors' Subcontracting Practices (GAO/RCED-92-28, Oct. 7, 1991).

DOE Management: Improvements Needed in Oversight of Procurement and Property Management Practices at the Lawrence Livermore National Laboratory (GAO/T-RCED-91-88, Aug. 20, 1991).

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

DOE Management: Management Problems at the Three DOE Laboratories Operated by the University of California (GAO/T-RCED-91-86, July 31, 1991).

Nuclear Security: Property Control Problems at DOE's Livermore Laboratory Continue (GAO/RCED-91-141, May 16, 1991).

Nuclear Nonproliferation: DOE Needs Better Controls to Identify Contractors Having Foreign Interests (GAO/RCED-91-83, Mar. 25, 1991).

Nuclear Security: Accountability for Livermore's Secret Classified Documents Is Inadequate (GAO/RCED-91-65, Feb. 8, 1991).

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

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

Nuclear Security: DOE Oversight of Livermore's Property Management System Is Inadequate (GAO/RCED-90-122, Apr. 18, 1990).

Energy Management: DOE Should Improve Its Controls Over Work for Other Federal Agencies (GAO/RCED-89-21, Feb. 9, 1989).

Ordering Information

The first copy of each GAO report and testimony is free. Additional copies are $2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

Orders by mail:

U.S. General Accounting Office
P.O. Box 6015
Gaithersburg, MD 20884-6015

or visit:

Room 1100
700 4th St. NW (corner of 4th and G Sts. NW)
U.S. General Accounting Office
Washington, DC

Orders may also be placed by calling (202) 512-6000
or by using fax number (301) 258-4066.

Each day, GAO issues a list of newly available reports and testimony. To receive facsimile copies of the daily list or any list from the past 30 days, please call (301) 258-4097 using a touchtone phone. A recorded menu will provide information on how to obtain these lists.

United States
General Accounting Office
Washington, D.C. 20548-0001

Official Business
Penalty for Private Use $300

Address Correction Requested

Bulk Mail
Postage & Fees Paid
GAO
Permit No. G100

[redacted]