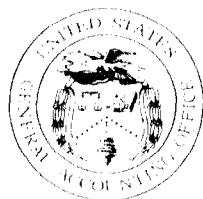
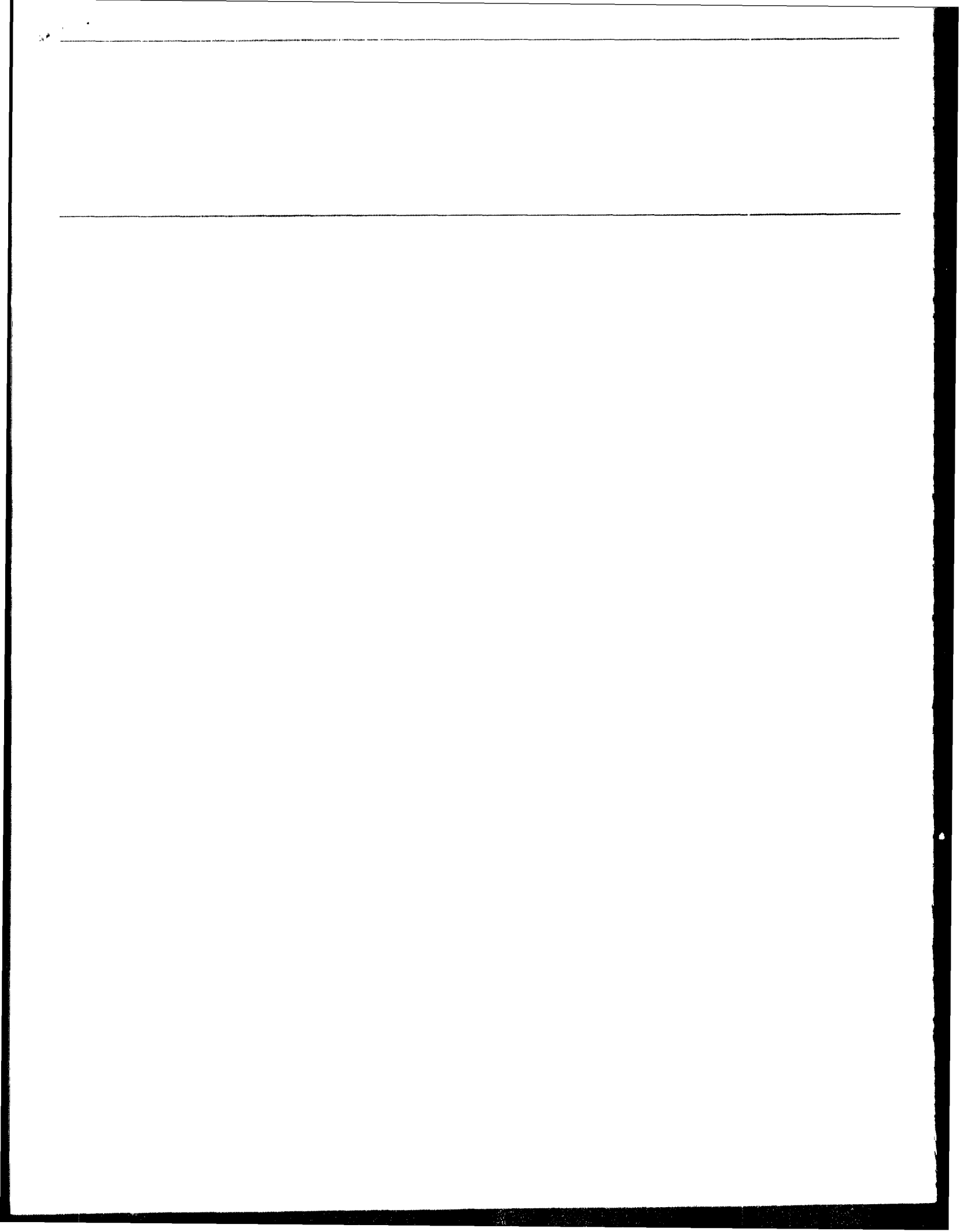


October 1991

SUPERFUND

EPA Has Not Corrected Long- Standing Contract Management Problems







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

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

B-246279

October 24, 1991

Congressional Requesters

This report responds to your requests for a review of contract management in the Environmental Protection Agency's (EPA) Superfund program. The report is also a part of our special audit effort to review areas vulnerable to fraud, waste, and abuse and to ensure that appropriate corrective actions are taken. The Superfund program was 1 of 16 areas we identified for review.

The report mainly discusses EPA's response to recommendations in prior GAO reports that EPA strengthen its management of Superfund contracts by adequately controlling contractor costs, setting contractor indemnification and conflict-of-interest policy, and developing a plan to reduce its backlog of unaudited Superfund contracts. The report contains several recommendations to the Administrator, EPA, to improve Superfund contract management.

Unless you publicly release its contents earlier, we plan no further distribution of this report until 30 days from the date of this letter. At that time, we will send copies of this report to the appropriate congressional committees and the Administrator, EPA. We will also make copies available to others upon request.

This work was performed under the direction of Richard L. Hembra, Director, Environmental Protection Issues, (202) 275-6111. Major contributors are listed in appendix I.

A handwritten signature in cursive script that reads 'J. Dexter Peach'.

J. Dexter Peach
Assistant Comptroller General

B-246279

List of Requesters

The Honorable Frank R. Lautenberg
Chairman, Subcommittee on Superfund, Ocean and Water
Protection
Committee on Environment and Public Works
United States Senate

The Honorable David H. Pryor
Chairman, Subcommittee on Federal Services, Post Office and
Civil Service
Committee on Governmental Affairs
United States Senate

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

Executive Summary

Purpose

Superfund, the Environmental Protection Agency's (EPA) \$15 billion effort to clean up the nation's most dangerous hazardous waste sites, is 1 of 16 federal programs GAO has identified as being most vulnerable to fraud, waste, and abuse. The program is vulnerable because of its large size—one quarter of EPA's budget—and its extensive use of cost-reimbursable contracts with potential values of almost \$10 billion. Although appropriate for some work, cost-reimbursable contracts can expose the government to excessive costs and give contractors little incentive to control costs if adequate safeguards are not imposed.

Reports by GAO over the last several years have disclosed weaknesses in EPA's management of Superfund contracts and oversight of contractors that make the program vulnerable to abuse and excessive costs. Several Subcommittee Chairmen requested that GAO review what EPA had done to correct these problems.

Background

The largest group of cost-reimbursable Superfund contracts are 45 contracts, collectively valued at \$6.6 billion. These 10-year contracts were awarded to 23 prime contractors to conduct cleanup studies, design remedies, and oversee construction at sites. The administration of these contracts has been largely delegated to EPA's regional offices. The contracts reimburse contractors for all allowable costs and offer an award fee, or incentive payment, for good performance. Allowable costs fall into two categories: (1) costs related to specific sites and (2) program management costs, which are expenses attributable to the general administration of the program.

Cost-reimbursable contracts require special oversight to protect against abuses. In 1988, GAO reported that EPA's contract oversight was inadequate. Specifically, EPA was not adequately reviewing contractor cost proposals for cleanup studies, which are the basis of budgets developed for work at each site, and contractor invoices, bills the contractor submits monthly as work at sites progresses. Because EPA was not estimating what cleanup studies should cost, it had to rely too much on contractor estimates. Moreover, it paid contractors for their work without sufficient examination of their incurred costs.

In 1989, GAO reported that EPA had indemnified contractors too liberally, thus putting Superfund assets at excessive risk. The Superfund law authorized EPA to indemnify contractors, that is, to pay for any damages that their negligent work at Superfund sites caused. This indemnification was to be granted only up to a limit to be specified by EPA and only

to contractors who could not obtain private insurance. GAO found, however, that EPA had not established an indemnification limit or required contractors to apply for insurance before being indemnified.

In 1989, GAO also reported that Superfund was vulnerable to contractor conflicts of interest because the same contractors who helped EPA to choose cleanup remedies could also work for the parties responsible for paying for the remedies. Yet, EPA had not (1) clearly instructed contractors and EPA personnel on what activities constituted conflicts, (2) documented the resolution of potential conflicts, or (3) checked contractors' compliance with conflict-of-interest rules.

Finally, in 1990 congressional testimony, GAO said that one of the most important controls over contractor costs—audits of contractor records that backed up their reported costs—had been neglected. Large audit backlogs had developed, and audits of contractor costs had been delayed for years.

GAO followed up on each of these issues to see if the conditions GAO described had been corrected. GAO interviewed EPA officials and reviewed records at EPA headquarters and 4 of its 10 regional offices.

Results in Brief

Despite several years of GAO's reporting on deficiencies in EPA's Superfund contract management, EPA has not adequately addressed most of GAO's recommendations to reduce the program's vulnerability to fraud, waste, and abuse. Controls over contractor costs, such as critical reviews of contractor cost proposals and invoices, are still not being fully used. In addition, contractor program management costs are excessive because EPA hired more contractors than it needed and then moved slowly to reduce the excess capacity. Superfund's exposure to indemnification losses is still unlimited because regulations to limit coverage have yet to be issued. Moreover, Superfund remains vulnerable to contractors' conflicts of interests because EPA contracting officials still need better guidance, and field checks of contractors' compliance with conflict-of-interest rules have not yet been performed.

EPA management has made some effort to correct the problems we reported previously but failed to follow through on planned improvements. The persistence of problems is largely the result of EPA's lack of sustained attention to Superfund contract management and EPA's delegation of contract management authority to the regions without sufficient oversight. After this report was drafted, the EPA Administrator

announced the findings of a high-level task force on Superfund contract management that confirmed many of the problems discussed in this report and made recommendations that, if implemented, would help solve many of these long-standing problems.

Principal Findings

Control Over Contractor Costs

EPA still does not require its regional offices to prepare cost estimates of cleanup studies, which were budgeted for \$342 million in fiscal years 1988 through 1990. As a result, the regions are still too dependent on the contractors' own cost proposals. The EPA regions GAO visited had prepared cost estimates, independent from the contractors', for only 4 of 30 sampled cleanup studies. When prepared, they were used to decrease the contractors' proposal—in one case, from \$3 million to \$1.6 million. In the absence of adequate cost control, contractors' studies have been getting more expensive. An EPA consultant found that the doubling of these studies' costs that occurred between 1985 and 1988 was, in part, caused by a lack of adequate cost control.

EPA does require Superfund project managers to review contractor invoices for reasonableness, but compliance continues to be inconsistent. Contracting officials in two of the four regions estimated that project managers were conducting invoice reviews for only about half of their contractors' invoices.

Because EPA hired too many contractors, program management costs, which are generally fixed costs, have been excessive. They totaled \$64 million through May 1991, about one-third of all costs. Following recent press reports of high program management costs, the EPA administrator set up a task force to study these costs. GAO is also reviewing the costs in a separate effort.

Contractor Indemnification

EPA has not corrected the problem of excessive contractor indemnification that GAO reported 2 years ago. While EPA has worked on a new indemnification policy, it has continued to grant unlimited indemnification to almost all of its Superfund contractors. It has also not tested contractors' willingness to do Superfund work without indemnification, as

GAO recommended, or set a limit on indemnification. Moreover, EPA is still not tracking contractors' efforts to obtain private insurance.

Contractor Conflicts of Interests

Since GAO's 1989 conflict-of-interest report, EPA established a four-person conflict-of-interest unit at headquarters to develop agency policy and guidance and advise EPA personnel on conflict-of-interest issues. Although the unit has made limited attempts to improve guidance and increase contractor oversight and has drafted new regulations, most of the problems GAO reported 2 years ago continue to exist. Specifically, contract officials are still complaining about insufficient guidance to determine when conflicts exist. In addition, EPA is not sufficiently verifying contractors' compliance with conflict-of-interest rules or adequately documenting conflict resolution.

Contractor Auditing

GAO reported in 1990 that audits of contractors' costs had disclosed problems, such as overcharges and understaffing by contractors. Nevertheless, the EPA Inspector General and the Defense Contract Audit Agency (DCAA), the two main responsible audit agencies, were not doing timely contract audits. For example, as of November 1990, there were 273 outstanding incurred-cost audit requests by EPA's contracting office, about 40 percent of which were over 2 years old. At present, the EPA Inspector General is developing a plan and has requested increased funding to reduce this backlog. The ability of DCAA to increase its coverage is in doubt, however, because of proposed staffing and budget cuts.

Underlying Cause

EPA has acknowledged many of the problems GAO has reported in the past, but until recently, it had not addressed GAO's recommendations. A pattern is apparent in EPA's response to reported contract management deficiencies—extended study of the problems, sometimes leading to revised plans or procedures, but with insufficient follow-through to actually get the problems corrected. The underlying causes of this pattern seem to have been a lack of high-level attention to contract management and delegation of contract management to the regions without sufficient oversight and accountability.

Recommendations to the Administrator, EPA

GAO's past reports on Superfund contract management made recommendations to the Administrator, EPA, to improve cost control, limit indemnification, and improve contractor conflict-of-interest controls, which GAO continues to believe are needed to reduce the program's vulnerability to fraud, waste, and abuse. This report adds new recommendations for improvements in these areas, the most important of which are intended to bring top management attention to bear on these persistent contract management problems and improve oversight of regional office contract management.

Agency Comments

As requested, GAO did not obtain written agency comments on a draft of this report. However, GAO discussed the report's contents with responsible EPA officials and included their comments where appropriate. Also, as indicated earlier, the EPA Administrator's Task Force corroborated the findings contained in GAO's report and proposed corrective actions that, if implemented, would improve Superfund contract management.

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Abbreviations

ARCS	Alternative Remedial Contracts Strategy
CERCLA	Comprehensive Environmental Response, Compensation, and Liability Act
CORAS	Contracts Operations Review and Assessment Staff
DCAA	Defense Contract Audit Agency
DOD	Department of Defense
DOE	Department of Energy
EPA	Environmental Protection Agency
FAR	Federal Acquisition Regulations
GAO	General Accounting Office
OIG	Office of Inspector General
OSWER	Office of Solid Waste and Emergency Response
PCMD	Procurement and Contracts Management Division
SARA	Superfund Amendments and Reauthorization Act

Introduction

Superfund, the Environmental Protection Agency's (EPA) program to clean up the nation's most dangerous hazardous waste sites, is 1 of 16 federal programs we have identified as being most vulnerable to fraud, waste, and abuse. A principal reason for highlighting the program's vulnerability is its dependence on contractors working under cost-reimbursable contracts. These contracts are authorized by federal regulations and are appropriate in some circumstances. But unlike fixed-price contracts, cost-reimbursable contracts do not limit the government's exposure to excessive costs by giving contractors incentives to control costs. EPA has awarded cost-reimbursable contracts with potential values near \$10 billion, and additional amounts are likely in the future. Since 1988, our reports have disclosed numerous weaknesses in EPA's contract management that put the government's Superfund investment at risk. This report mainly discusses what EPA has done to correct these previously reported problems.

The Superfund Program

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA) authorized EPA to compel those parties responsible for contaminating hazardous waste disposal sites, such as industrial generators of hazardous wastes and landfill operators, to clean up the sites or reimburse the government for cleanup costs. The act also created Superfund to finance cleanups when responsible parties able to pay for cleanups could not be found. Since CERCLA's enactment, Superfund has been extended twice, with spending authorizations totaling \$15 billion. Currently, there are about 1,200 sites in Superfund. EPA expects to spend \$40 billion cleaning up these sites and to add about 900 sites to Superfund during the 1990s. EPA has not estimated the costs of cleaning up the sites to be added, but it says that the costs of implementing cleanup remedies are currently running at about \$25 million per site and are expected to rise.

Once sites are selected for Superfund, EPA or the parties responsible for the contamination begin remedial investigations and feasibility studies to determine how to clean them up. The remedial investigation assesses the type and extent of contamination at the site and its health and environmental risks. The feasibility study uses data developed in the remedial investigation to evaluate various cleanup alternatives and assess their cost effectiveness. These studies are typically conducted as one project and referred to as "remedial investigation/feasibility studies" or "remedial studies."

Following a remedial study, EPA selects the final remedy and documents it in a Record of Decision. The remedy selected, which can include removing or covering contaminated soil and building water treatment facilities, is then designed and implemented. The remedial design documents the site conditions and outlines specifications for the remedy, while the remedial action is the actual construction work necessary to implement the selected remedy. Table 1.1 shows the number of Superfund sites in each of the cleanup phases as of September 23, 1991.

Table 1.1: Status of Superfund Sites as of September 23, 1991

Cleanup phase	Number of sites
Remedial study underway	488
Remedy selected	108
Design underway	169
Cleanup underway	310
Cleanup completed	63
Other ^a	107
Total	1,245

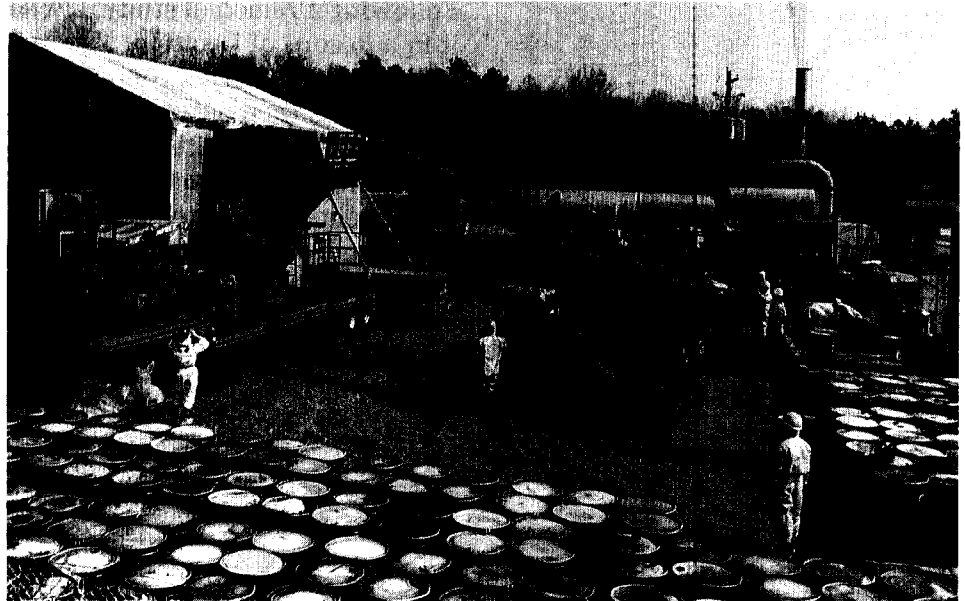
^aIncludes sites where no work has begun, an immediate threat assessment has been completed, or emergency action has been taken.

Source: EPA.

The Role of Contractors in the Superfund Process

EPA uses private contractors or the U.S. Army Corps of Engineers to perform most of the Superfund cleanup work paid for by the government. The private contractors perform remedial studies, design remedies, and manage the construction of the less expensive remedies. The Corps of Engineers designs and manages the construction of remedies in excess of \$5 million. (See fig. 1.1.)

Figure 1.1: Implementing a Superfund Remedy

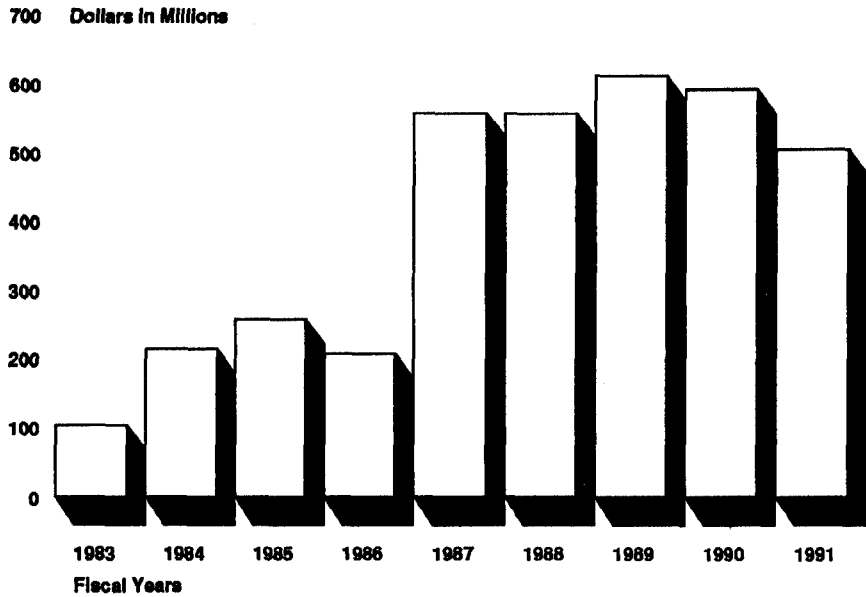


Note: Workers wearing protective gear feed drums containing dioxin-contaminated soil and other material into a shredder before incineration.

Source: The U.S. Army Toxic and Hazardous Materials Agency, Corps of Engineers.

Contractors generally work under two primary types of contracts: fixed-price and cost-reimbursable. Fixed-price contracts require a contractor to assume responsibility to perform the agreed-upon work within an established price. Cost-reimbursable contracts are used because they offer agency managers flexibility in responding to emergencies and are appropriate when the scope and nature of the work to be performed are uncertain or subject to change. However, because they promise to reimburse contractors for all allowable costs, these contracts (1) place maximum risk on the government and minimum risk on the contractor; (2) provide the contractor with little incentive to control costs; and (3) place a large administrative burden on both the government and the contractor to oversee, control, and identify contract costs. As figure 1.2 shows, EPA's obligations for cost-reimbursable contracts increased from \$103 million in fiscal year 1983 to \$612 million in fiscal year 1989 and decreased to approximately \$506 million in fiscal year 1991.

Figure 1.2: EPA's Obligations for Superfund Cost-Reimbursable Contracts, Fiscal Years 1983-91



Note: Data exclude Contract Lab Program (CLP) contracts. As of October 16, 1991, EPA had 61 CLP contracts valued at \$113.6 million.

Fiscal Year 1991 data are estimates.

Source: EPA's Procurement and Contracts Management Division, as of March 31, 1991.

EPA began its present Superfund remedial contracting system in 1988. By July 1989, EPA had awarded 45 contracts across the country to 23 architect/engineering firms to implement this system, called the Alternative Remedial Contracts Strategy (ARCS). The strategy decentralized remedial contract management to the EPA regions and was intended to improve competition for cleanup work and improve contractor performance. Between five and eight contracts were awarded in each region or zone.¹ The 45 contracts replaced 3 large contracts, called Remedial Engineering Management contracts, under which contractors conducted cleanup studies and investigations under 1 nationwide contract and 2 large-zone contracts—each zone covering one-half of the United States.

An ARCS contract is a form of cost-reimbursable contract called a “cost-plus-award-fee contract,” under which EPA reimburses the contractor for all allowable costs incurred. In addition, the contractor earns a base fee of about 3 percent of allowable costs and is eligible for an award fee, or

¹EPA placed contracts in each of its five eastern regions (Regions I-V) and in two zones that cover its five western regions (Regions VI-X). Zone 1 comprises Regions VI-VIII, and Zone 2 covers Regions IX and X.

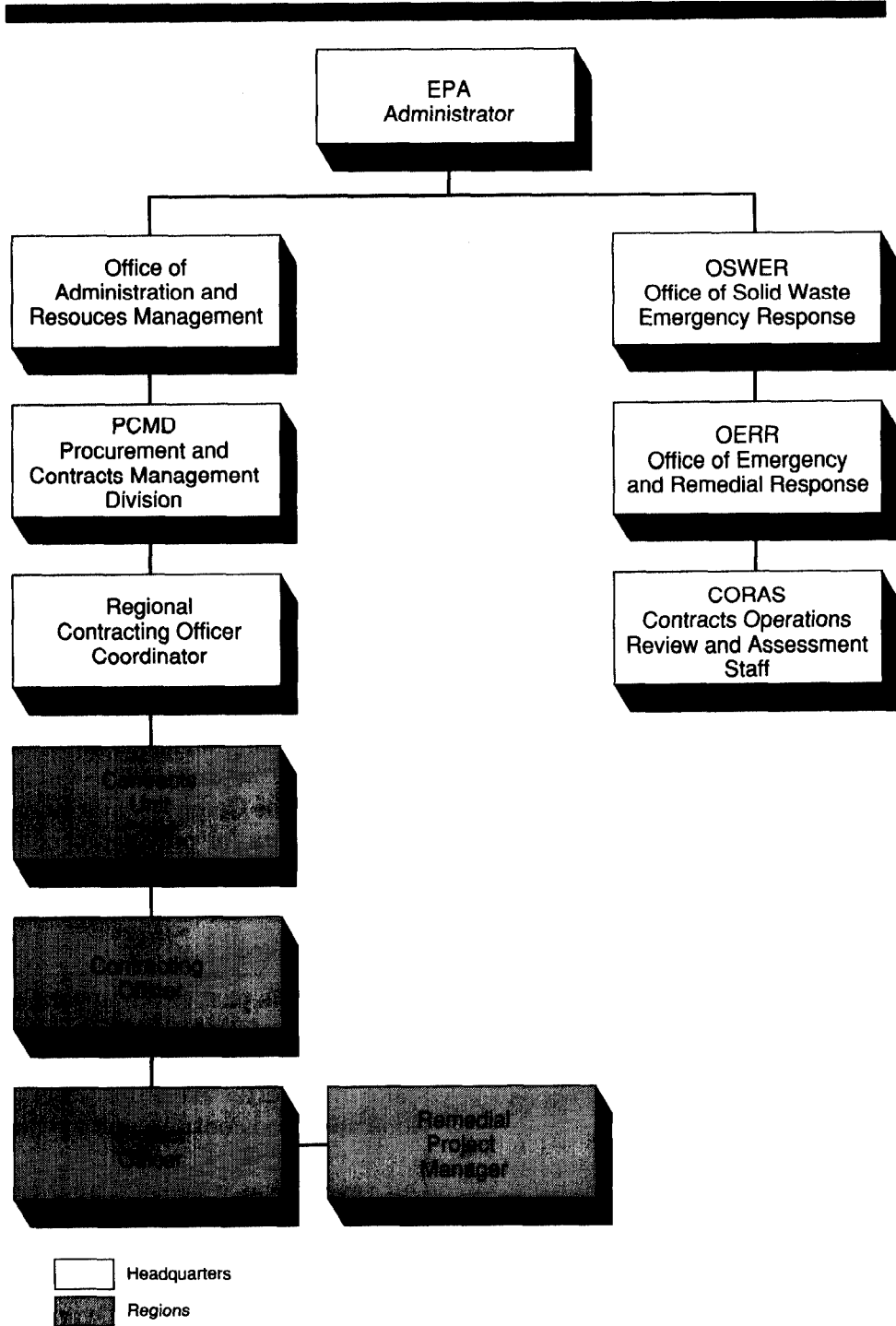
incentive payment, of up to 7 percent of allowable costs, on the basis of EPA's evaluation of the contractor's performance. Under contracts with potential values totaling about \$6.6 billion, ARCS contractors are responsible for cleaning up Superfund sites to be assigned by EPA over a 10-year period, from 1988 to 1998. Contractors are assigned work under "work assignments" approved by EPA before work is begun at each site.

Key Roles in Managing Superfund's Remedial Contracts

EPA's Procurement and Contracts Management Division (PCMD) (EPA's agencywide contracting unit), the Office of Emergency and Remedial Response (the Superfund program office), and regional contracting personnel are responsible for managing Superfund contracts. (See fig. 1.3.) The Office of Emergency and Remedial Response created the Contracts Operations Review and Assessment Staff (CORAS) to assess Superfund contract management.

The management of ARCS contracts is very decentralized. EPA regional offices assign work to contractors, approve work assignment budgets, approve contractor bills for payment, and evaluate their work. Contracting officers and their technical assistants in the regions are responsible for the day-to-day management of contracts to ensure contractors' compliance with their provisions and the agency's contract policies and procedures. The technical assistants include a project officer and a remedial project manager. However, the contract officer is the only official authorized to commit the government to a contract and to modify contract terms. A project officer provides technical direction and oversees the contractor's work at all sites assigned under a contract. The remedial project manager is responsible for managing and overseeing cleanup work at individual sites and provides feedback to the contracting officers on contractor cost, performance, and scheduling.

Figure 1.3: EPA's Superfund Contract Management Structure



Past GAO Reports on EPA's Contract Management

Over the past 3 years, we reported that some of the most important controls over EPA contractor costs had been neglected. These controls are intended to give some assurance that the government pays cost-reimbursed contractors only for allowable and reasonable costs. The controls include the preparation of government estimates of what contractors' work should cost (which is essential for evaluating contractors' cost proposals), a review of the reasonableness of contractors' invoices (which is the basis for their reimbursement claims), and audits of contractor records supporting their claimed costs. Deficiencies in these controls were reported in our report to the Subcommittee on Oversight and Investigations, House Committee on Energy and Commerce, entitled Superfund Contracts: EPA Needs to Control Contractor Costs (GAO/RCED-88-182, July 29, 1988) and in testimony before this Subcommittee entitled EPA's Contract Management: Audit Backlogs and Audit Follow-up Problems Undermine EPA's Contract Management (GAO/T-RCED-91-5, Dec. 11, 1990).

In addition, we have reported other contract management problems which have exposed Superfund to fraud, waste, and abuse. In a 1989 report to the Congress entitled Superfund: Contractors Are Being Too Liberally Indemnified by the Government (GAO/RCED-89-160, Sept. 26, 1989), we stated that EPA had put Superfund at unnecessary risk by providing contractors with excessive indemnification (guarantees by EPA to hold contractors harmless for damages caused by their negligence). Also, in 1989 we reported to the Subcommittee on Oversight and Investigations, House Committee on Energy and Commerce, about weaknesses in EPA's system for preventing conflicts of interest among its Superfund contractors (Superfund Contracts: EPA's Procedures for Preventing Conflicts of Interest Need Strengthening, GAO/RCED-89-57, Feb. 17, 1989).

Objective, Scope, and Methodology

This review is part of our special effort to examine federal programs vulnerable to fraud, waste, and abuse. We identified Superfund as one of these programs because of its high cost and the large federal financial stake in the effective enforcement of responsible party cleanup obligations and good contract management.

Our review was requested by the Chairmen of the Subcommittee on Superfund, Ocean and Water Protection, Senate Committee on Environment and Public Works; the Subcommittee on Federal Services, Post Office and Civil Service, Senate Committee on Governmental Affairs; and the Subcommittee on Oversight and Investigations, House Committee on Energy and Commerce. Our objective was to determine what

action EPA had taken to correct contract management problems we reported on over the last 3 years. To accomplish our objective, we examined records and interviewed EPA officials at EPA headquarters in Washington, D.C., and in four EPA regional offices—Boston (Region I), Chicago (Region V), New York (Region II), and Philadelphia (Region III). The regional offices selected are among the regions with the largest Superfund workload.

To follow up on our 1988 report on contractor cost control (GAO/RCED-88-182), we interviewed officials in EPA's procurement and Superfund offices about EPA's response to our recommendations for improving reviews of contractors' cost proposals and invoices and preventing contractors from receiving undeserved incentive payments. We examined files for the 30 highest value ARCS work assignments for remedial studies in the 4 regional offices for evidence of any improvements. All of these work assignments had been obligated for at least \$510,000, as of June 30, 1990. We also conducted structured interviews on evaluating contractor cost proposals and invoice reviews with the 12 contracting officers, 10 project officers, and 30 remedial project managers responsible for the work assignments. We interviewed officials in EPA headquarters and examined studies on a Superfund cost control issue that emerged since our 1988 report—excessive contractor program management costs.

To determine EPA's response to our conflict-of-interest report (GAO/RCED-89-57), we discussed policy and organizational changes with EPA headquarters officials and used a structured interview to obtain the views of 12 contracting officers in the 4 regions on how helpful these changes had been in preventing conflicts. We also examined records in EPA's Conflict of Interest Unit in headquarters. To determine what EPA had done to better control contractor indemnification risks, which we reported on in 1989 (GAO/RCED-89-160), we interviewed EPA headquarters officials responsible for making and implementing indemnification policy and regional contracting officials responsible for determining contractors' eligibility for indemnification. We also examined files in the regions to see if required indemnification procedures had been followed. We discussed the status of EPA's response to our contract audit coverage testimony (GAO/T-RCED-91-5) with officials of EPA's Office of Inspector General and examined Inspector General records.

We conducted our review between July 1990 and October 1991 in accordance with generally accepted government auditing standards. As directed, we did not obtain written agency comments on our report but

did discuss its findings with EPA Superfund and procurement officials at the management level. These officials generally agreed with the facts presented in this report. Their comments are included in the report as appropriate.

In addition, in October 1991, after this report had been drafted, an EPA Administrator's task force on ARCS contracting issued a report confirming many of the problems we discuss in our report. We have included some highlights of the task force's findings and recommendations at appropriate places in our report.

EPA Still Lacks Sufficient Controls Over Contractor Costs

In July 1988, we reported that EPA had not adequately controlled the cost of Superfund remedial study contractors.¹ This continues to be the case. EPA has not satisfactorily (1) evaluated contractor cost proposals, (2) recorded the results of price negotiations with contractors, (3) reviewed contractors' claimed costs, or (4) safeguarded against undeserved incentive payments. Although EPA made some changes in policies and procedures since our earlier review, most of the problems have persisted. Moreover, EPA has been slow to deal with a serious contract management problem that has developed since that report: excessive costs resulting from having too many contractors to perform the available work. The continued lack of controls over contractor costs can be directly attributed to EPA's failure to follow through on recommended corrective action.

Cost Estimation for Remedial Studies Is Inadequate

EPA does not prepare independent cost estimates to evaluate the reasonableness of contractor-proposed budgets for remedial studies even though such independent estimates can help prevent overcharging. This problem has continued since we first reported it in 1988. EPA has taken some tentative steps since then to correct this deficiency by beginning to develop cost-estimating models. But the utility of these models has not been proven, and they were not widely available or used in the regions we visited. In addition, some EPA regions, concerned about their limited ability to evaluate contractor costs, began to take steps to improve cost estimation, but their efforts have been piecemeal and incomplete.

Government Cost Estimates Not Prepared in the Past

Before authorizing a contractor to start a remedial study work assignment, EPA requires the contractor to submit a work plan and a budget estimate for regional office review and approval. Independent government cost estimates can be valuable aids in reviewing the contractor's budget estimate because they provide a basis for evaluating, negotiating, and controlling contractor costs.

The Federal Acquisition Regulations (FAR) state that federal agencies should prepare an independent estimate of the cost of architect-engineer services before negotiations on each proposed contract or contract modification expected to exceed more than \$25,000. The FAR stipulates that the analysis supporting the estimate should be prepared as thoroughly as though the government were submitting a proposal. Superfund officials agreed that it made good business sense to develop these estimates

¹GAO/RCED-88-182.

for work assignments under ARCS contracts, which are for architect-engineering services and which can have values well in excess of \$25,000.

In 1988, we reported that EPA regional staff were not developing such estimates because they were not required to do so by EPA headquarters. Even if they had been required, regions had little cost information at that time with which to prepare these estimates. Instead, EPA regional staff were using budgets and work plans from previously completed contractor studies to evaluate proposed contractor costs. This approach has serious limitations since these previous studies were not subjected to adequate cost control. An EPA consultant attributed the doubling of the cost of remedial study costs between fiscal years 1985 and 1988 to a need for better cost control.²

We concluded in our 1988 report that EPA had insufficient controls over remedial study costs. This deficiency is particularly significant because EPA budgeted approximately \$342 million for remedial studies in fiscal years 1988 through 1990. We said that in effect, EPA was allowing its contractors, working under cost-reimbursable contracts, to establish the cost parameters for these studies. To remedy this deficiency, we recommended that EPA (1) develop remedial study cost estimates and (2) require that this information be used to assess the reasonableness of contractor cost proposals and subsequent cost increases.

EPA Has Not Corrected Previously Reported Cost- Estimating Problems

EPA still has not instructed its regional staff to develop independent cost estimates for remedial studies. The regions we visited rarely prepared such estimates. When independent estimates were prepared, however, regional staff were able to reduce the contractors' proposed budgets. EPA officials recognize that the limited use of independent government estimates is a weakness in the management of these contracts and agree that developing such estimates would be a good business practice. However, EPA headquarters officials have not required estimates because they said they had not gotten around to focusing on the problem. In the interim, EPA has tested some cost-estimating models to assist its regional staff in developing independent government estimates. But the use of these models is not mandatory, they do not cover all types of Superfund sites, and they were not being used in the four regions reviewed.

²Booz, Allen & Hamilton Inc., The RI/FS Cost Study, Final Report, Volumes I and II (Oct. 28, 1988).

Independent Government Estimates Rarely Developed

We found that regional staff had developed independent government estimates for only 4 of the 30 remedial studies reviewed. The original value of these 30 studies ranged from \$510,000 to almost \$3 million. As they had 3 years ago, regional staff said they were not usually preparing independent government estimates because they lacked experience, knowledge, and adequate cost data bases.

However, where cost estimates were prepared, they were effective in reducing contractor costs. For example, a Region II project officer prepared four estimates by adapting a contractor's cost-estimating model. The region successfully used three of the four estimates to reduce contractors' proposed budgets by between \$60,000 and \$1.4 million. (See table 2.1.)

Table 2.1: Effectiveness of Independent Government Estimates in Region II

Site name	Contractor proposed budget	Independent government estimate	Final approved budget	Amount proposed budget was reduced
Ciba-Geigy	\$2,340,019	\$1,679,641	\$2,340,019	\$0 ^a
Higgins Farm	1,806,037	1,137,373	1,167,967	638,070
U.S. Radium	2,992,816	1,613,143	1,613,143 ^b	1,379,673
Action Anodizing	643,615	494,308	584,310	59,305

^aThe contractor was able to show that the independent government estimate prepared was unrealistic.

^bEPA had approved only a partial budget of \$998,571 at the time of our review. However, officials said the final budget will not exceed the independent government estimate.

Regional staff repeatedly told us that they needed more guidance on evaluating costs. Some said that they did not feel qualified to make the evaluations because they lacked knowledge in estimating and challenging ARCS costs. Most often they said they compared contractor-proposed costs with the costs of previously completed contractor studies. However, as we discussed in our 1988 report, such comparisons are not good substitutes for independent government estimates, since controls over the costs of these previous studies were not adequate.

Incomplete Efforts Toward Improving Cost Estimates

Headquarters and regional EPA officials acknowledged a need to improve EPA's ability to evaluate contractors' costs and have taken some initial steps toward solving the problem. However, in the absence of a clear requirement from headquarters for independent estimates and national guidance for preparing such estimates, these actions have been fragmented and uncoordinated.

In 1990, EPA's Office of Solid Waste and Emergency Response (OSWER), which oversees the Superfund program, began distributing two cost-estimating tools to regional staff. The first tool, the Superfund Cost Estimating Expert System, is a computer model that uses site-specific data to develop independent government estimates and to suggest ways to minimize the costs of remedial studies. EPA began working on this model in 1986 and approved it for distribution in August 1990. The model is currently usable for about two-thirds of the Superfund sites. However, as of February 1991, it was installed in only 1 of the agency's 10 regions. EPA does not intend to require the use of the model until further assessment because it is not certain about its effectiveness.

The second model is a general cost guide to be used for developing ballpark cost estimates. While EPA distributed this guide in September 1990, 29 of the 30 remedial project managers we interviewed in the fall of 1990 either had not received the guide or rarely used it. EPA planned to assess the distribution and use of this cost-estimating guide, but as of October 1991 had not started the assessment because headquarters managers did not make this a priority, citing lack of time and staff resources.

In addition to these headquarters initiatives, three of the four regions we visited have attempted to improve their cost-estimating systems. In 1987, a Region II project officer adopted a major Superfund contractor's software program for producing work plan cost estimates. Although, as discussed earlier, the model was used successfully, the project officer was the only one in the region who could operate the model. In 1990, Region V hired an engineer to help its staff develop cost estimates and review contractors' cost proposals. After the completion of our fieldwork, Region V began drafting guidelines and procedures for independent estimates. By taking these actions, the regions are acknowledging the need to improve controls over contractor costs. But since better cost control is a national need, the initiative in this area should not be left entirely to the regions.

Documentation of Price Negotiations Is Inadequate

The FAR requires that records be kept on contract price negotiations. The Comptroller General's internal control standards require that the documentation of significant events and expenditures of resources be accurate and complete and facilitate the tracing of actions after events have occurred. Our 1988 report noted incomplete documentation in contract files. In the regions we visited during our current review, we found that price negotiation records were not prepared for work assignments. For

much the same reason that we agreed with Superfund officials that it makes good business sense to prepare independent government cost estimates for work assignments, we also believe that documentation of price negotiations for work assignments should be prepared.

Adequate records of price negotiations can serve a number of important uses. They can force contract negotiators to justify their approval of agreed-upon costs, help in future negotiations involving similar issues, and give EPA management and outside reviewers a basis for evaluating the negotiations. The absence of adequate negotiations records makes it difficult to judge how well contractor prices were controlled.

At the end of contract price negotiations, the FAR requires contracting officers to promptly prepare a memorandum outlining the principal elements of a price negotiation. The memorandum is to be included in the contract file and contain such information as a summary of a contractor's proposal, the basis of the government's initial proposed price and the final price, and a discussion of any significant differences between the two. None of the 30 work assignment files reviewed for 30 remedial studies in the 4 regions contained documentation equivalent to what is required for contract negotiations. Region III's files contained negotiation memoranda, but did not explain significant differences between the government's proposed price and the agreed-upon price. Although EPA has a checklist for remedial project managers to use to document their evaluation of contractor price proposals, this form does not show the basis for final prices.

Contractor Invoices Still Not Being Reviewed

The review of contractors' monthly invoices—the basis for periodic contract payments—is another important control over contractor costs. Invoice reviews allow the government to foresee future problems, such as when contractor charges are going to exceed the established budget, and to avoid being charged a higher than reasonable amount. For example, remedial project managers can identify when a lower paid contractor employee would be qualified to perform technical work or when technical work could be done in less time than charged. These reviews, therefore, can reduce the risk of excessive charges. Similarly, a contracting officer can identify when a contractor's costs are not justified and request supporting documentation. Our 1988 report disclosed that remedial project managers were often failing to review invoices as required by EPA procedures, and needed more guidance from headquarters and information from contractors to make such reviews more meaningful.

Since our report, EPA has increased guidance and training to some extent. Nevertheless, most remedial project managers we interviewed during our current assignment were not aware of the new guidance and had not received the training. They continued to complain that contractors were not required to submit enough information justifying their charges. At half of the regions we visited, remedial project managers were not reviewing all invoices as required.

**Past Report Showed That
Project Managers Had Not
Reviewed Invoices**

Superfund remedial contractors submit monthly invoices of incurred costs for reimbursement. Project officers and remedial project managers are required to review the invoices and certify that they appear reasonable, appropriate, and within budget. The project manager's review is especially important because this official has the closest view of contractor work activities.

In 1988, we reported that about 55 percent of the remedial project managers we interviewed were not routinely reviewing invoices. Further, about half of the project managers did not find reviews of contractor invoices helpful because they needed additional guidance on performing reviews and better information in the invoices. According to one remedial project manager, the managers were reluctant to review contractor invoices because they considered themselves environmental specialists and not accountants. We concluded that EPA had not taken full advantage of this control to scrutinize contractors' costs and to disallow unreasonable costs. Therefore, we recommended that EPA ensure that remedial project managers review contractor invoices to determine the reasonableness of contractor costs, as required.

**Invoice Reviews Still Not
Being Adequately Done**

We found that remedial project managers in the regions we visited during our current review were still not consistently reviewing contractor invoices and that project managers want additional training on invoice review. CORAS officials acknowledged the need for systematic training on invoice reviews, but have yet to adequately meet this need.

**Contractor Invoices Not
Reviewed**

Remedial project managers in half of the regions we visited still were not reviewing all contract invoices, and contracting officials at three of the four regions we visited were not enforcing the requirements for these reviews. Project officers in Regions II and III estimated that remedial project managers reviewed about half of the site-specific invoices for their contracts. Many of the project managers we interviewed said

that they do not consistently review invoices because they have difficulty reading and understanding the invoices and lack the guidance and training to do reviews well. Region V was allowing its remedial project managers to certify the reasonableness of contractor charges on the basis of a review of progress reports rather than invoices, even though progress reports may contain incomplete cost information. To illustrate, one Region V remedial project manager could not determine what comprised \$1,100 of "other direct costs" billed by a contractor over a 2-month period, since the progress reports he used did not provide a detailed breakdown of the charges and he had not reviewed the monthly invoices.

In contrast to these regions, we found that Region I had one staff person responsible for following up with remedial project managers to verify that they reviewed all site-specific invoices. In one instance, a review of a contractor's invoice resulted in denial of payment of about \$50,000 in costs in part because the contractor did not submit documentation supporting its claim. According to a regional contracting officer, "It was necessary to deny payment of the entire invoice to get [the contractor's] attention in this matter." In another instance, after review, another invoice from this same contractor was rejected because of errors and inconsistencies. Because the contractor did not provide information adequately and promptly, EPA denied this contractor an award fee.

Guidance and Training Not Widely Available

Since our 1988 report, EPA has developed some invoice review guidance and training—consisting mainly of CORAS bulletins and a training module on how to review invoices. The guidance and training, however, were not reaching all remedial project managers.

At the time of our review, the first CORAS bulletin had been issued. The bulletin discusses primarily the project officers' and contracting officers' roles, information available to review invoices, and specific areas to check when reviewing invoices. It also provides a checklist to assist staff in reviewing cost reasonableness. However, 25 of the 30 remedial project managers we interviewed said they had not used this bulletin. Most of the 25 who offered an explanation said they were not aware of the bulletin or had not received a copy. According to the then CORAS Chief, remedial project managers may not have received the bulletin because it was distributed to project officers, rather than to remedial project managers.

In 1989, EPA offered a new Superfund contract management course that includes an invoice review module. The agency now requires this course for all newly hired remedial project managers. The majority of remedial project managers we interviewed—not being recently hired—said that they had not received the training. Many said that they had difficulty in understanding the ARCS invoices and needed training to better analyze invoices, estimate the costs of tasks, evaluate cost increases, and challenge questionable expenditures. In March 1991, CORAS began a survey of project managers to determine training needs.

Inadequate Information for Invoice Reviews

In addition to limited guidance and training, remedial project managers told us that their ability to analyze vouchers is hampered by insufficient detail in these vouchers. Invoice contents and formats are negotiated at the time of contract award. Project managers said they have difficulty in reviewing some contractors' invoices because some charges were reported in lump-sum totals and other charges were not adequately explained because of a lack of sufficient detail. For example, remedial project managers in Regions II and III said that they needed a better break out of the charges for subcontractor costs and for the hours and pay rates of contractor employees. Five of 11 contractors in Regions II and III billed these two types of charges in lump-sum totals, limiting remedial project managers' ability to assess the reasonableness of these charges. With only aggregate figures, the remedial project managers cannot readily determine what each subcontractor is billing and whether such charges appear reasonable. In 1989, EPA headquarters drafted a standardized format for ARCS contractors to report their monthly costs. The format was not officially adopted however because not all regions agreed it was appropriate.

Superfund Contracts Still Permit Undeserved Incentive Payments

Superfund remedial action contractors are eligible for an award fee—an incentive payment based on their performance. The award fee is granted in two phases—during the contract period (after assessments of the contractor's interim performance) and at the completion of work (after an assessment of the contractor's overall performance).

In 1988, we reported that EPA had granted award fees to contractors whose performance was rated less than satisfactory at the end of the contract. We recommended that EPA amend its award fee structure to prevent these contractors from receiving sizeable award fees. After our report was issued, EPA revised its award fee policy in conformance with

this recommendation, but its regional offices did not attempt to negotiate changes to some contracts to implement the policy. Headquarters officials did not check on contract revisions until we inquired about them during our review.

Poorly Performing Contractors Received Award Fee

Our 1988 report disclosed that 6 contractors in our sample of 11 that received a less than satisfactory overall performance rating earned between 29 and 45 percent of the available award fees. The fees had been received as a result of the first-phase award fee decisions. Similarly, in a 1990 review, EPA's Inspector General found that the agency rewarded Superfund contractor performance that was less than satisfactory. During our current review, we found no work assignments with less than satisfactory performance, but few work assignments had been completed and evaluated.

Contracts Not Modified to Prevent Unearned Awards

In June 1990—almost 2 years after we recommended action—EPA revised its award fee policy to (1) deny award fees to contractors who receive unsatisfactory performance ratings and (2) make the retention of an initial award fee contingent on satisfactory performance throughout the contract period. EPA requested that its regional contracting personnel negotiate changes to the ARCS contracts to permit recovery of initial award fees. But not until December 1990, during our current review, did PCMD follow up with regional contracting personnel to determine the status of their modifications to ARCS contracts. PCMD found that of the 45 ARCS contracts, 28 had been modified and 17 remained unmodified. As of September 1991, PCMD was drafting an instruction to the regions to complete contract changes.

EPA Has Not Acted Quickly to Deal With High Program Management Costs

For the last 2 years, EPA has had data showing that its ARCS contracts have high program management costs, but the agency has moved slowly to correct the problem. Further, EPA does not have data showing that its principal solution to the problem—supplementing ARCS' regular work with duties not planned for when the ARCS contracts were awarded—is a cost-effective approach.

A principal reason for high program management costs has been a lower than expected contractor workload, resulting in a high ratio of contractor management costs to site cleanup costs. Until very recently, EPA headquarters had not encouraged regional offices to terminate unneeded

contracts—and thereby reduce program management costs. This reluctance arose from concerns that a future increase in workload would leave the agency without sufficient contracting capacity. Superfund officials now acknowledge that an increase in remedial planning workload is unlikely. The problem of high program management costs developed after our 1988 report on controlling contractor costs. We are currently conducting a detailed review of ARCS contractor program management costs and expect to issue a report in the summer of 1992.

Remedial Contracts Are More Costly Than Expected

Beginning in 1988, EPA replaced a few large remedial action contracts with 45 ARCS contracts, largely to increase competition for cleanup work and improve contractor performance. Soon after the contracts were awarded, however, higher than expected program management costs developed. According to EPA reviews of ARCS costs in 1989 and 1990, program management expenditures appeared too high. These costs are administrative and technical costs, including expenses related to equipment, preparation of quality assurance and employee health plans, and pollution liability insurance. The costs are related to general administration of the Superfund program rather than site-specific work.

Interestingly, a 1989 study commissioned by EPA reported that the ARCS program management cost rate was about 2-1/2 times higher than the rate for the cleanup contractors that ARCS replaced.³ The report attributed some of the higher ARCS rate to start-up costs and expected the difference to diminish over time. However, it said that

“the ratio of [program management] costs to remedial hours used will probably remain relatively high because the remedial workload that is being assigned is substantially less than what was anticipated when the ARCS program was designed. The study found that a substantial proportion of [program management] costs, possibly more than 50 percent, could be defined as either fixed or non-recurring costs that did not vary in direct proportion to the remedial hours used. With a low remedial workload these non-variable costs that are incurred regardless of the amount of remedial work, will be spread over a smaller base, increasing the ratio of [program management] costs to remedial hours used.”

The report said that an ARCS workload increase was unlikely in the immediate future and that EPA might not be getting the full value from program management expenditures. It recommended better data on program management costs, better guidance to regional officials on acceptable costs, and possible restructuring of the ARCS program. Since the

³Booz, Allen & Hamilton Inc., *Analysis of ARCS Program Management Operations* (Oct. 28, 1989).

report, EPA has continued to monitor program management costs, but officials admit that they still need better data on the costs and have not provided better guidance to the regions.

A second EPA review of the program management cost issue was made in conjunction with an August 1990 briefing by Superfund officials to the Director of the Office of Emergency and Remedial Response. The briefing papers state that the low workload "in some regions has resulted in higher program management costs." As of March 1991, program management costs accounted for about 30 percent, or \$64 million, of the \$213.6 million of cumulative expenditures for the 45 ARCS contracts. The average monthly program management cost was about \$53,500, and ranged from about \$11,000 to \$119,000.

Excess Contract Capacity Has Contributed to High Program Management Costs

EPA expected to provide its remedial contractors with a base level of work⁴ in the first 2 years of the contracts' performance period, but was unable to supply the expected work. As of March 1991, 32 of the 45 contracts were between 24 and 39 months old. Yet only 18 of these 32 contracts had utilized their base number of remedial planning hours. For the remaining 14 contracts, 6 were expected to reach their base hours within 1 year, 5 within 2 years, and 3 other contracts are expected to take from over 2 to 8 years to use their base level of hours. For the other 13 contracts less than 24 months old, none had met their base level of work. EPA expected that it would take between several months to over 7 years to provide those contractors with the base level of work.

EPA officials we interviewed cited several reasons for the underutilization of these contracts. First, EPA deliberately awarded more contracts than it expected to need in the long run because it wanted to foster price and quality competition between the contractors and intended to drop some of the poorer performing contractors after they reached their base level of work. However, as of June 1991, EPA had not identified any contractors whose performance warranted termination. Second, responsible parties are performing a larger number of remedial studies and cleanups than in the past because of the agency's stronger enforcement efforts. Third, the Congress has denied some requested funds. The agency planned to start 40 remedial studies a year, but instead, it is now projecting that it will be able to start approximately 15 studies a year.

⁴A minimum number of hours of remedial planning work that a contractor could expect to receive under these contracts.

Fourth, EPA has shifted some of the cleanup work that could have been done under ARCS contracts to the Army Corps of Engineers.

In yet another internal study, EPA, in its September 1990 Long Term Contracting Strategy, analyzed the Superfund program's contracting needs through the year 2000. The study recommended using only 15 to 20 remedial contracts to accomplish projected response action work after the phase-out of the ARCS contracts. As a result of the study, EPA decided to expand the ARCS contractors' responsibilities by assigning to them responsibility for evaluating sites for inclusion in Superfund and assisting with the enforcement of responsible party cleanup obligations—work previously done by other contractors. However, Superfund officials did not have data showing how much this change would affect the program management cost rate or whether it was more cost effective than terminating ARCS contracts and leaving the extra work outside the ARCS program.

After allegations of excessive program management costs appeared in the press,⁵ the EPA Administrator established another task force to review the ARCS program in June 1991. The task force, comprising senior management from across the agency and regions, is now considering whether adjustments to the program's size are necessary. In addition, EPA's Region IV announced in July 1991 that it had begun termination actions against two of its ARCS contractors. EPA estimates that the terminations could save up to \$510,000 annually.

Conclusions

EPA's extensive use of cost-reimbursable contracts in the Superfund program imposes on it a special responsibility for effective cost control. Among the control techniques EPA can use to prevent excessive costs are reviews of proposed contractor costs in advance of work and claimed costs as work proceeds. However, EPA has made limited use of such controls. EPA regions we visited did not usually prepare independent cost estimates and so were not fully evaluating contractor cost proposals for remedial studies. The regions had not justified in written records agreed-upon prices for remedial studies, even though these records would promote more effective bargaining and be useful in future negotiations.

⁵"Administrative Costs Drain Superfund," the Washington Post, June 19, 1991.

The current Superfund contracting strategy delegates most contract management to the regional offices. But many regional officials we contacted did not believe they had the knowledge or experience to critique contractor cost proposals or review claimed costs. In effect, they lacked confidence in their ability to control contractor costs. They wanted more training in these areas, better guidance from EPA headquarters, and more detail from contractors to support claimed costs. Since our 1988 report on contractor cost control, EPA has provided some additional help to regions in carrying out their responsibilities, but not enough. A need for closer EPA headquarters oversight of regional contract management is also indicated by the failure of some regions to negotiate amendments to ARCS contracts in conformance with EPA's policy of denying award fees to poorly performing contractors. EPA began to reduce excessive costs resulting from contractor overcapacity only after press reports disclosed the problem. It has not justified its proposed main solution to the problem—assigning work to contractors that was not intended when they were hired—on the basis of cost effectiveness.

Recommendations to the Administrator, EPA

Our 1988 report on EPA contractor cost control recommended that the EPA Administrator direct Superfund and procurement officials to develop cost information for remedial studies and require remedial project managers to use it to assess the reasonableness of contractor cost proposals. We continue to believe that this recommendation should be implemented.

In addition, we recommend that the EPA Administrator

- establish controls to ensure that remedial project managers review contract invoices, develop more complete written guidance on remedial project managers' responsibilities for invoice review, and provide training to all project managers on how to meet these responsibilities;
- develop minimum standards for the information that contractors should submit to justify their invoiced charges;
- require contracting officials to document negotiations with contractors on the price of remedial studies, explaining the basis of the agreed-upon price and any significant deviations from the government's estimate; and
- require that all regions attempt to negotiate amendments to ARCS contracts to implement EPA's policy of denying award fees to contractors with less than satisfactory performance ratings.

With respect to ARCS contractors' program management costs, we specifically recommend that the EPA Administrator

- determine the cost effectiveness of assigning additional work to ARCS contractors and
- terminate or reduce the scope of any ARCS contracts with excessive program management costs.

Recent EPA Report

After this report was drafted, the EPA Administrator's Task Force on the ARCS program released an executive summary of its report. The executive summary concluded that

"... EPA is not conducting effective contract administration and oversight. This report documents weaknesses in the way EPA assigns work to contractors, monitors contractor performance and costs, prepares independent cost estimates, and conducts audits."

Furthermore, it said that "Administrative weaknesses in the areas of work assignment management, invoice review, technical performance management, and independent government cost estimates provide inadequate safeguards against waste and mismanagement."

The task force recommended a series of actions to correct the problems it had identified. These included

- immediate action to establish a regional capacity for providing independent government cost estimates to ARCS contract managers;
- immediate steps to strengthen ARCS administrative controls such as the invoice review process and the independent government cost estimates;
- the negotiation of an approximately \$2 billion reduction in the construction capacity of ARCS contracts to reflect the reduction in current projected needs; and
- the establishment of 20 percent or less as the ratio of program management expenditures to total ARCS contract expenditures, better data on program management expenditures, and other changes to the control of these costs.

Full implementation of the task force recommendations would help correct the problems discussed in this chapter.

Superfund Remains Vulnerable Because of Uncorrected Weaknesses in Other Contract Management Areas

In addition to not bringing contractor costs under adequate control as discussed in chapter 2, EPA has not resolved other previously reported contract management weaknesses that continue to expose Superfund to unnecessary costs and potential waste, fraud, and abuse. Specifically, EPA

- has placed Superfund resources at risk through excessive contractor indemnification, i.e., federal guarantees to pay damages resulting from negligent cleanup work;
- has not adequately safeguarded against the potential conflicts of interest that arise when Superfund contractors also work for parties responsible for cleaning up Superfund sites; and
- has not done timely audits of contractors' claimed costs.

EPA Is Still Granting Superfund Contractors Excessive Indemnification

Superfund contractors can be sued for damages by individuals, such as adjacent landowners, who might sustain injuries resulting from the negligence of a contractor performing cleanup at a Superfund site. During congressional deliberation over SARA, environmental liability insurance for contractors was virtually nonexistent. To ensure that a limited availability of insurance would not deter contractors from working in the Superfund program, section 119 of SARA authorized the federal government to indemnify Superfund contractors, that is, hold them harmless from liability for injuries, costs, and damages stemming from the negligent performance of cleanup work at a Superfund site.¹ SARA also established Superfund as the source of funding for third-party liability claims, such as death or illness, against indemnified contractors. EPA has used SARA to indemnify almost all Superfund contractors and subcontractors.

Our 1989 report on contractor indemnification² discussed three main problems. First, EPA had not adequately determined contractors' needs for indemnification—that is, the minimum indemnification necessary to ensure an adequate supply of contractor services. This occurred even though considerable evidence showed that contractors would be willing to participate in Superfund at lower indemnification levels than were being granted. Furthermore, EPA had not established a ceiling on indemnification per contract as SARA directed. Second, EPA had not ensured that indemnification was provided only after contractors proved they

¹SARA section 119 does not exempt response action contractors from liability arising from gross negligence or intentional misconduct.

²GAO/RCED-89-160, Sept. 26, 1989.

were unable to purchase private insurance, another SARA requirement. Third, other federal agencies were indemnifying their Superfund contractors under general procurement regulations even though SARA's indemnification rules establish specific statutory authority for indemnifying Superfund contractors. EPA was the only federal agency relying on SARA section 119 to indemnify Superfund response action contractors.

Our recent work shows that none of these problems have been resolved. EPA put off establishing indemnification limits until it issued its new indemnification guidelines and then was unable to reach a consensus on the guidelines within the agency. In addition, contractors continue to be indemnified without proof of uninsurability. EPA has also not advised other federal agencies to use SARA's indemnification provisions over those found in general procurement regulations.

EPA Has Not Determined Contractors' Need for Indemnification

As required by SARA, our 1989 report assessed Superfund contractors' need for indemnification. We identified only three insurers who provided pollution insurance for cleanup contractors and found that they provided only limited coverage. The rest of the insurance industry regarded pollution risks as generally uninsurable, believing that an accurate assessment of risk was not possible. Given the general unavailability of insurance, several contractors told us that they would not perform, or were reluctant to perform, Superfund work without federal indemnification. However, we found that some of these contractors were, in fact, performing hazardous waste cleanup work for states and responsible parties without indemnification. Because federal indemnification costs a contractor nothing, there was no incentive for a contractor to limit the amount of indemnification it requested. We reported that if indemnification requests were made an element of competition in the federal contract award process, the marketplace could serve to define the need for indemnification and its appropriate amounts. We went on to recommend that EPA identify and test procurement options which would determine the lowest indemnification levels that ensured an adequate supply of contractors for Superfund work.

Two years have passed since our report, but EPA has not yet set up procedures to determine contractors' minimum indemnification requirements. Policy guidelines have been delayed because of disagreements between top EPA managers over the appropriate level of indemnification.

EPA Has Not Enforced SARA's Conditions for Providing Indemnification

SARA requires that indemnification be provided on a discretionary, case-by-case basis after a contractor demonstrates its inability to obtain insurance and mandates that federal agencies set a limit on the amount of indemnification provided to a contractor. In our 1989 review, we found that EPA had not fully complied with SARA's requirements. Assuming that little or no insurance was available, EPA had indemnified contractors across-the-board instead of on a case-by-case basis and had not required contractors to document their efforts to seek insurance prior to receiving indemnification. Also, although required by SARA, EPA had not set limits on the indemnification amounts.

Proof of Uninsurability Not Required

Our 1989 report noted that SARA and EPA's own interim guidance required contractors to make diligent efforts to obtain insurance before seeking indemnification. The guidance requires a contractor to try to obtain insurance within 30 days of the contract's award and, in the case of a multi-site contract, each time before the contractor begins work at each new site under the contract. After the first effort to obtain insurance, the guidelines require a contractor to continue to monitor the insurance market and seek pollution liability coverage every 12 months and submit documentation of its unsuccessful insurance applications to EPA each time.

However, in our 1989 review, we found that EPA had not monitored regional office efforts to enforce SARA (and interim guidance) requirements. The regional offices were generally not requiring that contractors make and document diligent efforts to obtain insurance before granting indemnification. While our work confirmed the limited availability of insurance, we said that EPA's compliance with SARA's insurance requirements could stimulate the pollution liability insurance market by increasing the demand for such insurance. We recommended that EPA implement management controls to ensure that indemnification decisions be made on a discretionary case-by-case basis following proof of uninsurability, as SARA requires.

During our recent work in four EPA regional offices, we found that the regions are still not enforcing the SARA insurance requirements or the agency's interim guidance requiring contractors to document efforts to obtain insurance. EPA regional officials told us that they instruct contractors to make and document their efforts to obtain insurance at least once a year. However, the officials do not know how often, if at all, contractors actually look for insurance because they have not been monitoring compliance with the requirements. Contracting officials told us

that requiring proof of uninsurability has been a low priority, EPA management had not emphasized compliance, contractors have not been successful in obtaining insurance, and the regions have high workloads. EPA headquarters officials said that they had received some documentation of contractors' efforts to obtain insurance but regarded the monitoring of contractor compliance as a regional office responsibility.

No Limit Set on Indemnification

SARA also requires that each indemnification agreement be limited to a maximum dollar amount of coverage. But in our 1989 review, we found that EPA's interim guidance did not establish a limit on indemnification because according to EPA, the agency did not want to arbitrarily establish limits on indemnity levels without thoroughly researching the issue. EPA planned to set limits in the final guidance, but as indicated above, EPA has not issued this guidance. Meanwhile, each contractor continues to be indemnified up to the unobligated balance of Superfund, that is, all the uncommitted money appropriated by the Congress to Superfund. As of the beginning of fiscal year 1991, the unobligated amount of Superfund was about \$1.75 billion.

The longer EPA delays in setting a limit on indemnification agreements, the longer Superfund remains exposed to liability not intended by SARA. As of September 1991, about 30 cleanup contracts with unlimited indemnification have expired. With their expiration, EPA has lost the opportunity to limit its liability risk on these contracts. We continue to believe that EPA needs to immediately negotiate specific limits on its indemnification agreements with contractors rather than wait for the agency's final policy guidelines to be issued.

EPA Has Not Advised Other Federal Agencies of SARA's Indemnification Requirements

Our 1989 report also stated that SARA's requirements superseded, for Superfund contractors, any previously existing indemnification authority in general procurement regulations. We said that in SARA, the Congress had established specific terms for indemnifying these contractors, such as advance proof of uninsurability, and that section 119 must be used by other federal agencies in place of general procurement regulations. However, we found that EPA was the only federal agency using SARA's requirements to indemnify Superfund response action contractors. Other federal agencies, namely, the Departments of Defense (DOD) and Energy (DOE) were using the general provisions found in the FAR,

which do not contain all of SARA's requirements.³ We recommended that EPA advise federal agencies to use SARA's indemnification authority over general procurement regulation authority when indemnifying Superfund contractors. EPA officials concurred, stating that absent any express statutory authority, SARA section 119 is the exclusive Superfund indemnification authority and said that it planned to clarify its position on the use of section 119 by other federal agencies in its final guidance.

Our current review showed that DOD and DOE continue to indemnify certain of their response action contractors using general procurement authorities; the Department of the Interior continues to successfully award response action contracts without indemnification. Officials from DOD, DOE, and Interior told us that they are awaiting EPA's final guidelines before changing their indemnification policies.

Problems in Superfund Conflict-of-Interest Controls Continue

Potential contractor conflicts of interest can arise in the Superfund program because many of the contractors that help EPA select and implement cleanup remedies can also work for the parties responsible for paying for cleanups. Contractors' work for these parties could impair contractors' objectivity when performing work for EPA. Also, contractors could have access to sensitive EPA enforcement information advantageous to the responsible parties for whom they work. In 1989, we reported problems in EPA's conflict-of-interest system that still exist today: inadequate guidance, failure to consistently document conflict resolution, and insufficient verification of compliance with conflict-of-interest rules.

EPA Has Not Provided Sufficient Conflict-of- Interest Guidance

In our 1989 report, we said that contracting officers and contractors needed additional guidance to help recognize and avoid conflicts. Contracting officers told us they needed more guidance on what EPA considered a conflict, especially in reviewing contractors' requests to perform work for private companies at hazardous waste sites. In addition, EPA had not provided contractors with guidance regarding the information they should include in their requests for work to be performed for private parties. For example, one contractor told us that the firm was uncertain of whether prior approval was needed to perform work for other federal agencies. Another contractor was unclear as to whether it needed to get EPA's approval for work to be performed at non-Superfund

³DOE was also indemnifying nuclear contractors under the Price-Anderson Amendments Act of 1988. SARA did not override this authority.

sites. We recommended that EPA provide contracting officers and contractors with additional guidance for avoiding conflicts.

To its credit, EPA has taken some actions to improve its conflict-of-interest system.

- In September 1989, EPA's Procurement and Contracts Management Division established a four-person conflict-of-interest unit to develop agency policy and guidance for identifying and resolving conflicts and to advise EPA personnel of conflict issues. The unit developed three, one-page case studies to provide contracting personnel with specific illustrations of conflicts and presented these case studies at two regional conferences.
- In 1990, EPA began requiring that firms submit conflict-of-interest plans when responding to contract solicitations for work involving significant conflicts. The plans must describe contractors' systems for identifying and reporting conflicts. According to EPA officials, a contractor will be awarded a contract only if its plan is determined to be technically acceptable.
- In 1989, EPA adopted a policy of preventing cleanup contractors from obtaining contracts to help develop EPA cleanup policies. For example, according to an EPA official, Superfund cleanup contractors would generally be ineligible for Superfund policy development contracts if the policy could affect their cleanup activities. This policy has been used to deny contracts to two companies.
- EPA drafted a revised conflict-of-interest regulation to better protect against conflicts. If issued, the revised regulation would (1) require contractors to immediately report any conflict before beginning work at each site (not just at and "after" contract award), (2) require a contractor to notify EPA of employees' conflicts prior to incurring costs for those employees and prohibit employees from disclosing sensitive information obtained during their government work, and (3) require contractors to obtain approval for certain responsible party work for specified times after the completion of a Superfund contract or work assignment.

The above changes, if fully implemented, should give EPA contracting officials more information about contractor activities but only limited help in deciding what activities actually constitute conflicts.

A January 1990 memorandum from PCMD's Quality Assurance Staff to Superfund contracting officials says that "Often, there are no 'black and white' answers to [conflict of interest] issues that come up daily under our Superfund contracts and Contracting Officers are called upon to make difficult judgement calls about real or apparent conflicts in the

absence of definitive guidance or case history.” But since our 1989 report, EPA has provided little new guidance on contractor activities that could constitute a conflict, and contracting officials continue to complain about the lack of guidance. Ten out of 12 of the contracting officers we interviewed during our current assignment said that additional guidance and examples of what constitutes a conflict of interest would be helpful in their evaluation and resolution of conflicts. Eight out of 12 of the officers also said that recent EPA guidance on conflicts of interest was only moderately helpful in identifying potential and actual conflicts; one-third said the guidance was of little to no help. None said that it was greatly helpful. A senior procurement analyst of the Conflict of Interest Unit said that the agency recognizes the need for additional guidance to and training of regional contracting personnel in identifying conflicts but resource limitations had prevented a larger effort.

EPA Does Not Ensure That Conflicts Are Documented Consistently

Documentation of how potential conflicts of interests are resolved would promote consistency in the treatment of conflict-of-interest issues. In addition, a historical record of decisions could serve as guidance for future conflict resolutions, which is especially important because of the high turnover of Superfund contract management personnel. In our 1989 report, we found two cases where EPA had been informed of or had identified actual conflicts after contractors had accepted work assignments. In neither case, however, had contracting officers documented the actions they took to resolve the conflicts as EPA’s procurement regulations required. In addition, contracting officers did not always document actions to show their approval or denial of contractors’ requests to compete for or perform work for private companies at Superfund sites. We recommended that EPA direct contracting officers to follow requirements for documenting actions taken to resolve potential conflicts and actions taken on contractors’ requests to perform work for private companies at hazardous waste sites.

Following these recommendations, EPA began assembling information for its conflict-of-interest data base in January 1990 by instructing contracting officers and contractors to provide the Conflict of Interest Unit with copies of documentation on the identification and resolution of conflicts. EPA then designed a computerized system to store data from these records that would be accessible by both headquarters and field personnel. However, development of a fully effective system has been slowed for two reasons. First, according to a senior procurement analyst in the Conflict of Interest Unit, field offices have not submitted much of the required documentation explaining the basis of their conflict-of-

interest decisions. The analyst attributed this noncompliance to the newness of the requirement. Contracting officers in three regional offices we visited acknowledged that their regions were not consistently complying with the EPA procurement regulation on documenting conflict resolutions. Second, development of the data base has been delayed by staff shortages in the Conflict of Interest Unit. Of the approximately 500 cases that the unit had received from the regions, only 36 had been entered into the data base as of August 1991. According to the senior procurement analyst, the agency gave first priority to the development of the conflict-of-interest regulations and lower priority to the design of the conflict-of-interest data base. Also, the unit's activities were constrained by restrictions on travel funds and a reduction in staff.

EPA's Effort to Review Contractors' Conflict-of-Interest Systems Moves Slowly

EPA's conflict-of-interest control system relies heavily on self-disclosure by contractors of their potential conflicts. In our view, this system can be credible only if sufficient oversight of contractors is maintained. In our past review, however, we found that EPA had not done independent checks to verify contractors' compliance with conflict-of-interest policies. EPA's oversight was generally limited to discussions with contractors about conflict issues. EPA periodically conducted reviews of contractors' performance, such as purchasing system and management reviews; however, none of the reviews included checks to verify that contractors were complying with EPA's conflict-of-interest requirements. We recommended that the agency check conflict-of-interest compliance as part of its contractor performance reviews. Similarly, a 1989 EPA study recommended that EPA procurement teams should examine Superfund contractors' conflict-of-interest prevention systems.

Following our report and the EPA study, EPA created the Conflict of Interest Unit, one of whose functions was to visit contractors to examine their conflict-of-interest policies and procedures. Although unit officials acknowledged the value of the visits, EPA has not given the effort a high priority, and its reviews have moved slowly.

During our current review, we found that the Conflict of Interest Unit had conducted only 2 reviews through fiscal year 1991, although there are 23 ARCS contractors. It planned to conduct three more during fiscal year 1991 but was unable to do them because of other program priorities and a lack of resources. In fiscal year 1991, the staff available for conducting reviews was decreased from four to two because of assignments to other EPA activities.

The need to review conflict-of-interest compliance at contractor facilities and avoid total reliance on contractor self-disclosure is illustrated by a recent case documented in the Conflict of Interest Unit's files. This case involved a firm which had two contracts with EPA. Under the earlier of these contracts, the firm had done studies for EPA on the health threats of a Superfund site in Florida. The second contract was for long-term services in Region IV at a number of possible sites. No work was done at the Florida site under this second contract. After completing work on the first contract, the contractor began working at the Florida site for a private party responsible for the cleanup of the site. The contractor notified EPA of this engagement under the terms of the second contract but did not disclose that it had also worked for EPA at the Florida site under the first contract. Nothing in the file indicated that the potential conflict with the first contract was considered by EPA. Two years after beginning work for the responsible party, the contractor gave notice to EPA about the possible conflict, saying that its system for detecting conflicts of interest had improved.

Improvements in EPA Contract Audit Coverage Depend on Whether Resources Are Provided

One of the most important controls over the costs of contractor work done under cost-reimbursable contracts is an audit of contractor records supporting claimed costs. However, our December 1990 testimony on audit coverage of EPA contractors and other subjects disclosed large audit backlogs, with audits of funds paid to contractors being delayed for years.⁴ As a general rule, audits of EPA's contractors are the responsibility of audit groups in the federal agencies doing the most business with the contractors, mainly EPA's Office of Inspector General (OIG) and the Department of Defense's Defense Contract Audit Agency (DCAA). Delays in audits of EPA contractor costs resulted from decisions by DCAA and the OIG to use their limited resources for other types of audits. We recommended that the OIG develop a plan for reducing the backlog of audits of contractors for which it had audit responsibility and report its progress to the Congress. We also recommended that EPA work with other federal agencies (including DCAA) to develop ways to expedite audits of EPA contractors for which these agencies had responsibility. At present, EPA's OIG is developing a plan for reducing the contract audits backlog and has requested increased funding for contract audit coverage. The OIG has not, however, begun full reporting to the Congress on the status of the contract audit backlog.

⁴GAO/T-RCED-91-5.

Chapter 3
Superfund Remains Vulnerable Because of
Uncorrected Weaknesses in Other Contract
Management Areas

Our 1990 testimony noted that cost audits for 6 of EPA's 10 largest contractors were backlogged. These contractors collectively received over \$1 billion in EPA contract payments in fiscal years 1983 through 1990, most of which remained unaudited. We also said that cost audits for EPA's contractors overall were backlogged. As of November 30, 1990, PCMD data showed 273 outstanding requests for incurred cost audits, about 40 percent of them being over 2 years old.

When audits were done, our review showed that they uncovered significant problems. For example, audits of one contractor over several years revealed ongoing timekeeping problems:

- A 1990 audit by DCAA questioned approximately \$180,000 in labor costs from fiscal years 1986 to 1989 because the contractor charged EPA for about 11,000 hours of employee time off in excess of earned time off and holidays. This time off was in addition to time provided for in the contractor's policy, and according to the audit report, the contractor could not adequately explain why the government should pay for these costs.
- During a "floor check" to verify that employees were actually working on the projects assigned, which DCAA conducted as part of a special interim 1989 audit, the contractor was unable to locate over half of the employees selected for checking.

The majority of PCMD's audit requests were to DCAA and were part of a backlog of defense and other contracts that had grown from about \$33 billion worth of contracts in fiscal year 1981 to nearly \$170 billion worth in fiscal year 1989. According to EPA's OIG, adequate resources had not been available to perform all essential audits. At DCAA, increasing workloads and a hiring freeze had produced an increasingly unmet audit demand.

Since our December 1990 testimony, the OIG has taken some preliminary steps toward increasing contractor audit coverage. It has informed DCAA that it is assuming audit responsibility for 12 more Superfund contractors, increased its headquarters staff working on contract audit issues by 3, and made plans to award 6 additional contracts to certified public accounting firms for contract audits. It has written DCAA to inquire about whether it could increase coverage of EPA contractors and is working on a plan to define the unmet audit need and propose ways to address the need. As of October 8, 1991, the OIG had not received a response from DCAA.

According to an OIG official, progress toward reducing the audit backlog depends on the approval of additional funding the OIG has requested for fiscal years 1992 and 1993. The Administrator of EPA has requested that the Congress increase the OIG resources for auditing ARCS contractors by \$4 million. The 1993 budget was under review at the completion of our assignment. DCAA's ability to increase its coverage is in doubt, however, because of proposed staffing and budget cuts.

The OIG has not fully implemented another recommendation from our December 1990 testimony—that the OIG semiannual reports to the Congress include information on the status of the contract audit backlog. The March 1991 report describes actions the OIG was taking to improve contract audits but did not disclose the size of the backlog. OIG officials said that they did not have full data on the size of the backlog in time for the March 1991 report but are developing information on this problem.

Conclusions

EPA's response to our numerous recommendations on contractor indemnification and conflict-of-interest control has been generally inadequate. EPA has not issued a new policy to better control grants of indemnification. In the 2 years since our report, EPA has continued to indemnify contractors without limit and without proof of uninsurability, despite SARA requirements to the contrary, and has not advised federal agencies to use SARA over general procurement authority if they indemnify their Superfund contractors.

EPA started to remedy some of the problems in its contractor conflict-of-interest system that we reported in 1989. It drafted a new conflict-of-interest regulation, set up the Conflict of Interest Unit, and provided some new guidance and training. But the conflict-of-interest rule has not been issued, and the other efforts have been insufficient because of the low priority assigned to them. Conflict-of-interest decisions are still not being documented, and regional personnel need more clarification about how to identify and resolve conflicts.

Despite its value, audit coverage of EPA contractors continues to be inadequate. How much it improves will depend in part on budget decisions still being made.

Recommendations to the Administrator, EPA

In our 1989 report on contractor indemnification, we recommended that the Administrator, EPA, limit the potential exposure facing Superfund by (1) placing a dollar limit on new indemnification agreements and attempting to negotiate limits on existing agreements, (2) identifying and testing options for providing indemnification that include incentives making it competitively unattractive to obtain more indemnification than is needed, and (3) enforcing SARA's requirements for proof of uninsurability to obtain and retain indemnification. We continue to believe that these recommendations should be implemented.

Our 1989 report on preventing contractor conflicts of interest recommended that EPA

- check compliance with EPA's requirements for avoiding, neutralizing, and mitigating conflicts of interest as part of its reviews of contractors' performance;
- direct contracting officers to follow requirements for documenting actions taken to resolve conflicts and actions taken on contractors' requests to work for private parties; and
- provide contractors and contracting officers with additional written guidance for avoiding conflicts. This should include guidance on the information that contractors should include in their requests for private party work and the importance that contracting officers should place on this information when evaluating these requests.

We continue to believe that these recommendations should also be implemented.

Recent EPA Action

After this report was drafted, EPA's Assistant Administrators agreed on the terms of new policy guidelines for contractor indemnification. The details of the proposed guidelines were not released by EPA but, generally, they would define when and on what terms indemnification would be granted to Superfund contractors.

Management Inattention and Insufficient Oversight Have Caused Problems to Persist

Earlier in this report, we described numerous long-standing problems with the management of EPA's high-value Superfund contracts. In prior reports, we made recommendations to correct these problems, many of which EPA acknowledged, but the recommendations were largely not implemented. A pattern is apparent in EPA's response to reported contract management deficiencies—extended study of the problems, sometimes leading to revised plans or procedures, with insufficient follow through to actually get the problems corrected. The underlying causes of this pattern seem to be a lack of high-level attention to contract management and delegation of contract management to the regions without sufficient oversight and accountability.

Lack of Management Attention

In our 1988 report on contractor cost control, we said that EPA management's focus was on expeditiously cleaning up Superfund sites and that insufficient attention was being paid to cost control. This priority was reflected in the attitudes of remedial project managers, who generally rated quality and timeliness over costs as considerations in managing their projects. Several said that costs were a minor consideration.

Since our 1988 report, contract management issues have continued to be secondary to other Superfund issues. Public attention on Superfund has been mainly directed at the speed of cleanups. The principal EPA review of Superfund since our 1989 report was a management study of Superfund commissioned by EPA's Administrator when he took office. As we pointed out in congressional testimony, this study did not focus sufficiently on contract management.¹ Instead, it emphasized the speed and quality of cleanups and the enforcement of responsible party cleanup obligations. The EPA review had high priority in the agency because of the Administrator's sponsorship, was backed up with a detailed plan to implement recommendations, and was followed by program improvements, especially in enforcement. The main Superfund contracting review EPA made since our 1988 report dealt with how to structure a contracting program for the 1990s to replace expiring contracts and supplement the ARCS contractors' workload. The review, however, did not make recommendations to deal with issues discussed in our 1988 report. As discussed in chapter 2, only when press reports of excessive program management costs appeared did EPA set up a high-level task force to examine issues of Superfund contractor costs.

¹Making Superfund Work Better: A Challenge for the New Administration (GAO/T-RCED-89-48, June 15, 1989).

The persistence of contract management problems described in this and the preceding chapter and the inattention to contractor audits indicate a need for top agency managers to intervene, raise the level of concern throughout the agency with contractor cost control and other contract issues, and see issues through to resolution.

Decentralization Without Oversight

Another underlying cause of the failure to correct the deficiencies discussed in our previous reports has been EPA headquarters' delegation of management responsibility to the regions without sufficient oversight and accountability. Our current review showed that the regions have not received enough advice or training from headquarters on estimating contractor costs, reviewing claimed costs, controlling program management costs, and dealing with contractors' potential conflicts of interest. Also, the regions have not fully adhered to headquarters' policy in the areas of invoice review, indemnification, and conflict-of-interest controls. While a decentralized approach to contract administration can be effective, it should be accompanied with headquarters' assistance when regions need it; accountability in the regions for performance; and enough oversight to ensure that national priorities, such as cost control, are observed.

Recommendations to the Administrator, EPA

To ensure that the contract management problems discussed in this report are given top management attention and our recommendations are fully implemented, we recommend that the EPA Administrator

- develop an action plan with goals, specified regional and headquarters' accountability, and follow up to implement our recommendations and
- report Superfund contract management as a material weakness under the Federal Managers' Financial Integrity Act until the recommendations are implemented.

Furthermore, to ensure that regional offices effectively administer Superfund contracts and adhere to contract management policy, we recommend that the EPA Administrator increase headquarters' monitoring of regional office contract management.

Recent EPA Report

The executive summary of the EPA Administrator's Task Force referred to at the end of chapter 2 of this report, while endorsing a decentralized contracting process, also concluded that "ARCS contracting activities are

not viewed systematically within EPA." It said that "ineffective information flows, inadequate coordination, and the need for improved staff training and development characterize EPA's management of ARCS contracts." It recommended the creation of a Superfund Acquisition Program Manager to assume responsibility for acquisition decisions and activities and address ARCS contract management problems. The executive summary also made other recommendations for headquarters' oversight of regional contract management. Also, the summary recommended that ARCS contract management be reported as a material weakness in EPA's fiscal year 1991 Federal Managers' Financial Integrity Act report and that a tracking system for corrective actions be established with quarterly reporting to EPA's Senior Council on Management Controls. At the same time that the task force's executive summary was released, the EPA Administrator announced the creation of a 20- to 30-person team of "troubleshooters" to provide information on regional office activities and improve management and accountability in the program.

If these recommendations are effectively carried out, they should help correct problems specifically discussed in this chapter.

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