



J. Edgar Hoover
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RELEASED

Report On
Statements Made Concerning
The [Veterans Administration's
Method Of Awarding Federal
Supply Schedule Contracts For
Chemical Reagents] *B-171649* *Rev. GPL.*

BY THE COMPTROLLER GENERAL
OF THE UNITED STATES

911797 **089895**

JUNE 10, 1971



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-171649

Dear Mr. Galifianakis:

DLG 05944

In accordance with your request dated December 23, 1970, herewith is our report on statements made by Mr. Dan Broida, president of Sigma Chemical Company, concerning the Veterans Administration's (VA's) method of awarding supply contracts for chemical reagents.

Mr. Broida's statements, contained in the enclosure to your letter, concerned the awarding of Federal Supply Schedule (FSS) contracts. FSS contracts are effective for specified periods of time and provide for the purchases of indefinite quantities at definite prices. Contractors awarded FSS contracts are listed on an FSS, which is distributed to the various Federal agencies for use in fulfilling their supply requirements.

Mr. Broida stated that the prices offered by the Sigma Chemical Company were lower than the prices offered by FSS contractors but that his company had been refused an FSS contract because it would not offer the Government a discount on the prices that it offered its other customers. He stated also that, by not being awarded an FSS contract, potential Government users were precluded from purchasing Sigma Chemical Company reagents.

The basic procurement policy of the Government is to seek from a contractor an economic advantage over the prices offered to other customers before it awards an FSS contract. The General Services Administration (GSA), the agency responsible for developing an efficient and economic system of procurement for Federal agencies, established this procurement policy to obtain a benefit that would offset the cost incurred by the Government in awarding FSS contracts and to eliminate the use of FSS as a free medium of advertisement. Both GSA and VA officials expressed the view that, because of its Government-wide distribution, FSS was a type of advertising media for FSS contractors and that the sales potential of the contractors thereby was increased.

In a letter dated July 9, 1968, the Administrator of General Services advised the Subcommittee on Government Procurement that the Government would save an estimated \$40 million to \$60 million annually as a result of this discount policy. On May 5, 1971, the Commissioner

of the Federal Supply Service, GSA, informed us that the Government was obtaining substantial savings as a result of the discount policy and that the aforementioned \$40 million to \$60 million was probably a conservative estimate. We did not attempt to verify the reasonableness of the estimated savings made by GSA.

During discussions with officials of the Sigma Chemical Company, we were advised that the company would not offer the Government an economic advantage over the prices offered to other customers. The officials stated that to offer the Government an economic advantage would result in extra work for and added costs to the company.

On the basis of the Sigma Chemical Company's position and the aforementioned basic procurement policy of the Government, VA has not awarded Sigma Chemical Company an FSS contract.

The FSS contract is only one of several procurement methods used by VA. Other methods of procurement include competitive-bid contracts, negotiated contracts, and direct purchases from suppliers. Under the direct-purchasing method, VA hospitals may purchase, with adequate justification, directly from the Sigma Chemical Company or from any other supplier. Our examination at the Washington VA Hospital showed that Sigma Chemical Company products were being purchased and that the users were satisfied with the products.

We noted that, although some FSS contractors' prices were substantially higher than those offered by the Sigma Chemical Company for similar items, some FSS contractors' prices were lower than those offered by the Sigma Chemical Company.

We noted, however, that VA (1) had not established a definition of an economic advantage or criteria for measuring what constituted a reasonable economic advantage and (2) did not have any means for determining whether an offer to the Government was lower than the prices charged to other customers. We found that varying degrees of economic advantages were being offered to the Government by the FSS contractors. We found also that two of VA's 55 FSS contractors for chemical reagents were not providing the Government with any apparent economic advantage

over the prices offered to other customers. We brought these matters to the attention of VA officials who informed us that VA had increased its staff specifically for the purpose of monitoring contracts to determine whether the Government actually was obtaining the economic advantages offered by contractors.

The Director of VA's Supply Service, by letter dated April 23, 1971, informed us that VA was attempting to obtain from the two FSS suppliers an economic advantage over the prices offered other customers and that, if acceptable price agreements were not obtained, the contracts would be canceled. The Director agreed that VA needed criteria for determining whether the economic advantage offered by a contractor was reasonable. He stated that such criteria were being developed and that future FSS contracts would be negotiated on the basis of the criteria.

The results of our examination are discussed in more detail in this report. VA and Sigma Chemical Company officials were not provided with copies of this report for their review and comment.

Similar requests also were received from other members of Congress, and the same information is being furnished to them.

Sincerely yours,

A handwritten signature in cursive script that reads "James B. Roberts".

Comptroller General
of the United States

The Honorable Nick Galifianakis
House of Representatives

GENERAL ACCOUNTING OFFICE
REPORT ON STATEMENTS MADE CONCERNING
THE VETERANS ADMINISTRATION'S METHOD OF AWARDING
FEDERAL SUPPLY SCHEDULE CONTRACTS
FOR CHEMICAL REAGENTS

The Sigma Chemical Company, St. Louis, Missouri, is a manufacturer and distributor of research biochemicals and diagnostic reagents. In an open letter accompanying its 1971 catalog, Mr. Dan Broida, the president of Sigma Chemical Company, made several statements concerning the Veterans Administration's (VA's) procurement procedures. Mr Broida stated that (1) VA had denied Sigma a contract because it would not offer the Government a discount on the prices that it offered its other customers, (2) Sigma's net prices, as illustrated by four examples, were lower than the discounted prices of its competitors who had contracts with VA, and (3) Government chemical reagent users were precluded from purchasing Sigma reagents.

Our examination into these statements included discussions with the Director and other officials of VA's Supply Service, who informed us that Mr. Broida's statements concerned VA's procedures for awarding Federal Supply Schedule (FSS) contracts. We also held discussions with the president of Sigma; General Services Administration (GSA) officials; the VA procurement officer; and several research technicians at the Washington, D.C., VA Hospital. We reviewed the records of VA's Marketing Center, the unit responsible for awarding FSS contracts.

The Federal Property and Administrative Services Act of 1949 (40 U.S.C. 471) gave GSA the responsibility for providing an economical and efficient system for the procurement of personal property and nonpersonal services needed by Government agencies. GSA, on January 3, 1961, assigned to VA the responsibility for awarding FSS contracts to suppliers of pharmaceuticals and chemical reagents (Federal Supply Class 6505 and 6810) and for compiling an FSS which lists all the contracts. The FSS is a primary procurement

source for filling the supply requirements of all Federal agencies except the Department of Defense. The Department of Defense has its own procurement system but may use the FSS contracts if it deems it advantageous to do so.

The FSS contracts awarded by VA are effective for specified periods of time and provide for the purchases of indefinite quantities at definite prices. FSS contracts for similar products are awarded to numerous contractors because there are no product standards and because specifications cannot be prepared for the products. Such numerous contract awards also enable the Government to choose from similar items. FSS contracts are awarded to contractors offering the Government an economic advantage, in regard to price and/or service offered, over other customers for the same items or groups of items. These contracts are for 1-year periods and, by mutual agreement of the Government and the contractor, may be renewed, in whole or in part, for additional periods not to exceed 2 years.

INFORMATION OBTAINED AT
SIGMA CHEMICAL COMPANY

Sigma was last awarded an FSS contract by VA in calendar year 1968. In accordance with GSA's policy, VA, in March 1969, began requiring that a contractor provide the Government with an economic advantage over prices offered to other customers in order to be awarded an FSS contract. Sigma refused to offer the Government such an economic advantage and therefore was not awarded an FSS contract.

The president of Sigma advised us that the reasons for not offering an economic advantage to the Government were that (1) Sigma's net prices were sufficiently low and (2) Sigma did not offer other customers, except dealers, any reduction in its established prices. He also stated that giving an economic advantage to the Government would result in extra work for and added costs to Sigma. He contended that the purchasing agents of VA hospitals could not buy Sigma's products because it did not have an FSS contract; therefore, Sigma was losing annual sales of approximately \$1 million.

The president of Sigma would not furnish us with any data to show how he had computed the company's estimated loss of Government sales, nor would he provide us with information concerning sales to VA hospitals.

Included in correspondence provided to us by the president of Sigma was a letter dated April 13, 1970, in which he advised the VA Marketing Center that he was aware of two contractors having FSS contracts who were not providing the Government with an economic advantage over prices offered to other customers. He stated that one contractor was charging the Government and retailers the same prices for the same items. He also pointed out that the other contractor required the purchase of five times the largest unit quantity of an item before allowing a price discount to the purchaser. (See p. 8 for our follow-up on these matters.) In bringing these matters to the attention of VA officials, the president of Sigma stated that, because Sigma lacked an FSS contract, the Government was purchasing inferior products at fantastically high prices.

VA'S POSITION REGARDING
ECONOMIC ADVANTAGE POLICY

The Director of VA's Supply Service informed us that Sigma was correct in stating that, unless it offered the Government an economic advantage over other customers, it could not obtain an FSS contract. He stated that VA's pharmaceutical and chemical reagent FSS contracts were agreements to purchase indefinite quantities of items at definite prices and were not awarded on a competitive-bid basis. He stated also that this policy had been established by GSA and that VA was administering its FSS contracts in accordance with this policy.

We discussed the FSS contracting policy with GSA officials who informed us that VA was administering its FSS contracts in accordance with GSA's policy of requiring an economic advantage over other customers.

Both GSA and VA officials expressed the view that, because of its Government-wide distribution, FSS was a type of advertising media for FSS contractors and that the sales potential of the contractors thereby was increased. The VA Supply Service Director stated that the policy of not awarding a contract to a company that did not offer the Government an economic advantage over the prices offered to other customers had been established to offset certain cost incurred by the Government in awarding FSS contracts and to reduce the large number of suppliers utilizing the FSS as a free medium of advertisement.

We noted that, in a letter dated July 9, 1968, the Administrator of General Services advised the Subcommittee on Government Procurement, Select Committee on Small Business, that the Government would save an estimated \$40 million to \$60 million annually as a result of this discount policy. On May 5, 1971, the Commissioner of the Federal Supply Service, GSA, informed us that the Government was obtaining substantial savings as a result of the discount policy and that the aforementioned \$40 million to \$60 million was probably a conservative estimate. We did not attempt to verify the reasonableness of the estimated savings made by GSA.

PROCUREMENT METHODS AVAILABLE TO VA

The awarding of FSS contracts is not VA's only method of procurement. Several other procurement methods are used, such as competitive-bid contracts, negotiated contracts, and direct purchases from suppliers. Consequently, purchases can be made from Sigma without its having an FSS contract.

During our examination at the Washington VA Hospital, we found that, if there was adequate justification, a VA research technician could request a specific product that was not provided by an FSS contractor. Research technicians at the Washington VA Hospital informed us that each manufacturer did not purify similar chemical reagents to the same degree or extent and that the interchanging of similar products during a research project might adversely affect the results of the project.

Therefore a researcher who had initiated a project with a particular product would have adequate justification for requesting continued use of that product for the duration of the project, even though it might not be provided by an FSS contractor or even though it was one of the higher priced products provided by an FSS contractor. The research technicians further stated that other reasons for use of a specific product might be the special or particular attributes of the product, the accessibility (fast delivery) of the product, or the personal preference of the user.

We observed that several Washington VA Hospital research technicians were using Sigma's products. They informed us that they were satisfied with the products. Our examination of several purchase orders showed that the technicians had made specific requests for and had received Sigma's products.

PRICE COMPARISONS

VA Marketing Center records showed that the FSS contractors' prices for comparable items varied considerably. In comparison with Sigma's prices, some FSS contractors' prices were higher and some were equivalent or lower. The quality of a product has a bearing on price; however, there is no standard grading or classification system for chemical reagents. Therefore we were unable to equate the quality of Sigma's products with those provided by FSS contractors.

The following table includes a price comparison for the same four items that Sigma included in its open letter. Because the open letter showed a comparison of Sigma's 1971 prices with an FSS contractor's 1970 prices, we have included in the table selected 1971 prices offered by FSS contractors for the same four items.

Comparison of Prices for Items Listed in Sigma's Open Letter

<u>Item</u>	<u>Unit</u>	<u>Schedule as shown in Sigma's open letter</u>		<u>Sample of 1971 prices available from FSS contractors (notes a and b)</u>	
		<u>FSS contractor's 1970 prices</u>	<u>Sigma's 1971 prices</u>		
L-Glutamine	1 kg.	\$600 ^c	\$ 71.50	\$100	\$ 67.50
L-Proline	1 kg.	395	219.00	240	200.00
L-Tryptophan	100 g.	70	29.50	70	30.15
Pyridoxal	250 mg. ^d	55	-	-	9.93
Phosphate	1 g.	-	5.00	32	5.25

^aThese prices do not include applicable discounts which would lower the prices per unit.

^bThe scheduled prices are not necessarily the highest or lowest prices available. We chose a high and a low price specifically for the purpose of illustrating price differences among the contractors.

^cThe contractor advised the VA Central Office that it did not sell this package size to any of its customers.

^d250 mg. equals 1/4 g.

Although there is a wide variance of prices available from FSS contractors, as shown by the above table, the

Government's policy is to purchase from the FSS contractor offering the lowest delivered price for an item of acceptable quality. Any deviation from this policy must be fully justified by the ordering office.

ECONOMIC ADVANTAGES OFFERED
BY FSS CONTRACTORS

VA records indicated that, as of March 12, 1971, there were 55 FSS contractors for chemical reagents. As previously discussed, the Government's policy is to seek from a contractor an economic advantage over the prices offered to other customers before it awards an FSS contract. Our examination of contract files showed, however, that two of the 55 contractors were not providing the Government with any apparent economic advantage over other customers.

VA does not have any means for determining whether a price offered to the Government is lower than prices charged to other customers. Also VA has not established a definition of economic advantage or criteria for measuring what constitutes a reasonable economic advantage. VA cited price discounts, time discounts, free transportation costs to the location of the ordering office (f.o.b. destination), and acceptance of small orders as some of the types of economic advantages that it had accepted from potential FSS contractors.

Our review showed that FSS contractors offered varying degrees of economic advantages. We found that one contractor offered f.o.b. destination as an economic advantage whereas another contractor offered a price and time discount, f.o.b. destination, and the acceptance of small orders as economic advantages to the Government. Both contractors were awarded FSS contracts because of their compliance with the Government's economic advantage policy.

We discussed these findings with VA officials who informed us that VA had increased its Marketing Center staff specifically for the purpose of monitoring contracts to determine whether the Government actually was obtaining the economic advantages included in the contracts.

The Director of VA's Supply Service, by letter dated April 23, 1971, informed us that VA was attempting to obtain from the two aforementioned FSS contractors an economic advantage over the prices offered to other customers and that, if acceptable price agreements were not obtained, the contracts would be canceled. The Director agreed that VA needed criteria for determining whether the economic advantage offered by a contractor was reasonable. He stated that VA was developing such criteria and that future FSS contracts would be negotiated on the basis of the criteria.

FOLLOW-UP OF STATEMENTS
CONCERNING TWO FSS CONTRACTORS

In a letter dated April 13, 1970, the president of Sigma informed VA officials that a 20-percent discount offered to the Government by one FSS contractor was not applicable unless there was a purchase of five times the largest unit quantity of an item. Our examination of VA's file for this FSS contractor showed that the statement was correct. Other data in the file, however, indicated that the contractor also had offered the Government free transportation to the location of the ordering office, a benefit not offered to the contractor's other customers, and that f.o.b. destination was the economic advantage upon which the contract had been awarded.

The president of Sigma also stated that another FSS contractor had been overcharging the Government by selling certain items to both the Government and retailers at the same prices. Our examination of VA's file for this FSS contractor showed that in 1970 the contractor had not given the Government the agreed-upon discounted price on certain catalog items. After receiving the letter from the president of Sigma, VA, on the basis of the contractor's estimate of the overcharges, recovered about \$5,700 from the contractor. Because it was too difficult to reconstruct the sales data necessary to calculate the actual overcharges, VA considered the contractor's estimate to be reasonable.

CONCLUSION

The president of Sigma was correct in his statement that Sigma had been denied an FSS contract because it had refused to provide the Government with a discount on prices that it offered to other customers. This denial was based on GSA's policy of obtaining an economic advantage to (1) offset the costs incurred in awarding these contracts and (2) preclude the contractors from using the FSS as a free medium of advertisement without providing an economic advantage to the Government.

With regard to the statement that the Government is paying significantly higher prices because it has not given Sigma an FSS contract, our examination has shown that some FSS contract prices are higher and others are lower than those offered by Sigma for similar items. Further, it is the Government's policy to purchase from the FSS contractor offering the lowest delivered price for an item of acceptable quality unless deviation from this policy is adequately justified.

The FSS contract is only one of the procurement methods used by VA. Other methods used include competitive-bid contracts, negotiated contracts, and direct purchases from suppliers. Consequently, VA hospitals may purchase, with adequate justification, directly from Sigma. Our examination showed that the Washington VA Hospital was purchasing some items directly from Sigma.

VA has not established a definition of economic advantage or criteria for measuring what constitutes a reasonable economic advantage when considering a proposal for an FSS contract. We noted that, as a result, FSS contractors offered the Government varying degrees of economic advantages. For instance, a supplier may be awarded an FSS contract by offering the Government free transportation to the ordering point whereas another contractor may be awarded an FSS contract by offering the Government a price, time, or other discount. Also VA does not have any means for determining whether a contractor's price offered to the Government is lower than the prices charged other customers.

We brought these findings to the attention of VA officials who informed us that contracts would be monitored to determine whether economic advantages actually were being obtained by the Government and that criteria were being developed for determining whether the economic advantage offered by a contractor was reasonable.

We plan to keep abreast of VA's progress in implementing the proposed actions.