

December 8, 2005



Defense Infrastructure

Public-Private Competition for
Environmental Services at the Navy
Public Works Center, San Diego,
California
(D-2006-036)

This special version of the report has been revised to omit
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Acronyms

FAR	Federal Acquisition Regulation
IDIQ	Indefinite-Delivery, Indefinite-Quantity
MEO	Most Efficient Organization
NAVFAC	Navy Facilities Engineering Command
OMB	Office of Management and Budget



INSPECTOR GENERAL
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December 8, 2005

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION,
TECHNOLOGY, AND LOGISTICS
NAVAL INSPECTOR GENERAL

SUBJECT: Report on Public-Private Competition for Environmental Services at the
Navy Public Works Center, San Diego, California (Report No. D-2006-036)

We are providing this report for information and use. We performed the audit in response to a congressional request. No written response to this report was required, and none was received. Therefore, we are publishing this report in final form.

We appreciate the courtesies extended to the staff. Questions should be directed to Mr. Henry F. Kleinknecht at (703) 604-9324 (DSN 664-9324) or Ms. Anella J. Oliva at (703) 604-9323 (DSN 664-9323). See Appendix C for the report distribution. The team members are listed inside the back cover.

By direction of the Deputy Inspector General for Auditing:

A handwritten signature in black ink that reads "Richard B. Jolliffe".

Richard B. Jolliffe
Director
Contract Management Directorate

Special Warning

This special version of the report has been revised to omit source selection information.

Department of Defense Office of Inspector General

Report No. D-2006-036

December 8, 2005

(Project No. D2005-D000CH-0123.000)

Public-Private Competition for Environmental Services at the Navy Public Works Center, San Diego, California

Executive Summary

Who Should Read This Report and Why? Defense officials responsible for the Office of Management and Budget (OMB) Circular No. A-76 public-private competitions should read this report because it addresses certain technical and procedural issues related to the public-private competition process.

Background. On June 17, 2002, the Department of the Navy announced the decision to perform a cost comparison of the environmental services function at the Public Works Center, San Diego, California. The cost comparison is a public-private competition process required by OMB Circular No. A-76 to compare the cost of Government performance with contractor performance. One private contractor, Shaw Infrastructure, Inc., (Shaw) submitted a proposal to compete with the Government most efficient organization (MEO). On August 16, 2004, the contracting officer conducted the cost comparison and announced the tentative decision to select the Government MEO to perform the environmental services at the Navy Public Works Center, San Diego. The adjusted total cost to contract with Shaw, about \$72 million, was approximately \$12 million more than the Government's adjusted in-house cost of about \$60 million. Shaw appealed the tentative decision, and the Administrative Appeal Authority sustained three of the five appealed items. On December 3, 2004, the Administrative Appeal Authority recomputed the cost comparison, and determined the adjusted total in-house cost should have been about \$77 million, approximately \$4 million more than Shaw's adjusted total contract cost of about \$73 million.¹ The Administrative Appeal Authority reversed the tentative decision and ruled in favor of Shaw as the winner of the cost comparison. The Navy awarded the contract for performance of the environmental services at the Public Works Center, San Diego, to Shaw on January 12, 2005.

We performed this audit in response to a request from Congresswoman Susan A. Davis that we review allegations from the employees of the environmental department at the Navy Public Works Center, San Diego. The employees made ten allegations of procedural and technical violations during the OMB Circular No. A-76 public-private competition for the environmental services. The allegations related to the solicitation for the public-private competition for environmental services and the associated amendments to the solicitation; the public review period during the administrative appeals process and the withholding of contractor bid information from the MEO; contract funding; the timeframe of the competition; the integrity of the study; and the technical evaluation of Shaw's proposal. The employees also alleged three potential adverse impacts as a result

¹ Shaw's adjusted total contract cost increased because it includes the one-time conversion cost and the minimum conversion differential. These costs are calculated based on a percentage of the in-house personnel costs, which were increased by the appeal.

of the contract award to a private contractor. The potential adverse impacts related to disruptions of Navy services, an increase in notices of violations, and job loss for the environmental services employees.

Results. The allegation regarding the amendments to the solicitation was substantiated; however, it had minimal effect on the MEO and the decision to award performance to a private contractor. Seven of the allegations were not substantiated, and two were indeterminable. Although the Navy awarded the contract for environmental services to Shaw on January 12, 2005, the Government continued to provide service during the 79-day transition period. Shaw assumed operations of the environmental department on April 1, 2005, and the first performance period of the contract was a 6-month period, which ended on September 30, 2005. We were unable to substantiate the potential adverse impacts based on a 6-month period of contractor performance. However, since Shaw assumed operations, the Navy Public Works Center, San Diego, is responsible for monitoring Shaw's performance and taking appropriate action if Shaw does not meet the performance requirements of the contract. We plan to issue a second report discussing the importance of monitoring Shaw's performance to manage any potential adverse impacts.

Management Comments. We provided a draft of this report on November 18, 2005. No written response to this report was required, and none was received. Therefore, we are publishing this report in final form.

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Background

We performed this audit in response to a request from Congresswoman Susan A. Davis that we review allegations from the employees of the Environmental Department at the Navy Public Works Center, San Diego, California. The employees alleged several procedural and technical violations during the Office of Management and Budget (OMB) Circular No. A-76 public-private competition for environmental services. The employees also alleged potential adverse impacts as a result of the competition decision to award the environmental services function to a private sector provider, Shaw Infrastructure, Inc., (Shaw). We also received a similar complaint through the Defense Hotline, which included an additional allegation.

Public-Private Competition for Environmental Services. On June 17, 2002, the Department of the Navy announced the decision to perform a cost comparison of the environmental services function at the Public Works Center in San Diego, California. The cost comparison is a public-private competition process required by OMB Circular No. A-76 to compare the cost of Government performance with contract performance. About 103 positions were included in the public-private competition process. The Navy Public Works Center, San Diego, environmental business line falls under the chain of command of Naval Facilities Engineering Command (NAVFAC) and is responsible for providing a wide range of environmental services to customers throughout the Commander Navy Region Southwest area of cognizance. These services included laboratory analysis and testing, industrial waste and oily waste treatment, hazardous waste handling and treatment, site assessment and remediation, and special projects.

On October 16, 2003, the Navy issued a solicitation on the NAVFAC E-Solicitation Web site for the OMB Circular No. A-76 cost comparison study to provide environmental services. The performance work statement was based on a standard template to ensure Navy-wide consistency, and included firm-fixed-price requirements, which represent ongoing, recurring work; and indefinite-delivery, indefinite-quantity (IDIQ) requirements, which represent one-time, nonrecurring work. The solicitation set up a three-step source selection process. Step 1 of the process included an analysis of each proposing firm's written statement of qualifications. Step 2 of the process involved the submission of written proposals detailing each firm's technical approach and price, and included submission of the Government's most efficient organization (MEO). Step 3 of the process involved evaluation of the technical and price proposals, selection of a best value offeror, and a cost comparison of the best value offeror and the MEO to determine the successful offeror.

The technical and price proposals for the environmental services were due February 13, 2004. Shaw was the only offeror to submit a technical and price proposal. After four rounds of discussions with the technical and price evaluation boards, Shaw submitted its final technical and price proposals on July 6, 2004. On July 12, 2004, the source selection board recommended Shaw as the best value contractor, and the source selection authority selected Shaw as the best value contractor to compete with the Government MEO in the cost comparison. The MEO certified and submitted its in-house cost estimate on July 29, 2004.

On August 16, 2004, the contracting officer conducted the cost comparison and announced the tentative decision to select the Government MEO to perform the environmental services at the Navy Public Works Center, San Diego. The adjusted total cost to contract with Shaw for the services was about \$72 million, approximately \$12 million more than the MEO's adjusted total in-house cost of approximately \$60 million. Shaw subsequently appealed the tentative decision on September 7, 2004. The MEO did not submit an appeal during the eligible period.

Administrative Appeal. Shaw alleged that the in-house cost estimate did not include all costs required by the solicitation. Shaw identified five items that it stated were not properly accounted for in the in-house cost estimate. On December 3, 2004, the Administrative Appeal Authority sustained three of the five appealed items and increased the in-house cost estimate accordingly. The three sustained items were as follows.

- The in-house cost estimate did not include the specified IDIQ material “plug” amount of \$3 million per year. The MEO stated that IDIQ materials were included elsewhere in its cost estimate, but the Appeal Authority stated that the MEO could not support this claim.
- The in-house cost estimate prorated the costs for IDIQ personnel and associated contract costs instead of including the full workload required in the base year as required by the solicitation. This error was automatically computed by the software used to prepare the in-house cost estimate.
- The in-house cost estimate excluded the cost of a Quality Control Manager, which was required by the solicitation to execute the quality control program.

The Administrative Appeal Authority recomputed the cost comparison and determined the adjusted total in-house cost should have been about \$77 million, approximately \$4 million more than Shaw's adjusted total contract cost of approximately \$73 million.¹ The Administrative Appeal Authority's final decision reversed the tentative decision and ruled in favor of Shaw as the winner of the cost comparison.

Contract for Environmental Services. On January 12, 2005, the Department of the Navy awarded a contract for performance of the environmental services to Shaw. During a 79-day transition period, the Government employees were still responsible for performance of the environmental services. Shaw fully assumed operations of the environmental services department on April 1, 2005. The first performance period of the contract ended on September 30, 2005.

OMB Circular No. A-76 Guidance. The OMB Circular No. A-76 (Revised), “Performance of Commercial Activities,” May 29, 2003, (revised circular)

¹ Shaw's adjusted total contract cost increased because it includes the one-time conversion cost and the minimum conversion differential. These costs are calculated based on a percentage of the in-house personnel costs, which were increased by the appeal.

establishes Federal policy regarding the competition of commercial activities. The guidance sets forth policy for implementing OMB Circular No. A-76, including instructions for using a standard or streamlined competition to determine if Government personnel should perform a commercial activity. The guidance also requires agencies to centralize oversight responsibility to facilitate fairness in competitions and promote trust in the process. The revised circular supersedes the previous OMB Circular No. A-76, "Performance of Commercial Activities," August 4, 1983, (Revised) and OMB Circular No. A-76 Revised Supplemental Handbook, March 1996 (Revised) (previous circular). The previous circular was in effect during the public-private competition for environmental services at the Navy Public Works Center, San Diego. All public-private competitions announced after May 29, 2003, are subject to the rules in the revised circular.

Objective

Our overall audit objective was to review selected portions of the OMB Circular No. A-76 process and the decision to award the environmental services function at the Navy Public Works Center, San Diego, California, to a private contractor. Specifically, we reviewed the allegations made to Congresswoman Davis to determine whether the Navy decision to award the contract to Shaw Infrastructure, Inc., was in accordance with appropriate policies and procedures. See Appendix A for a discussion of the scope and methodology. See Appendix B for the congressional request. This report discusses the allegations; we plan to issue a second report discussing the Government offer in public-private competitions and the importance of monitoring contract performance.

Managers' Internal Control Program

Review of the managers' internal control program was not an announced objective of the audit and we did not complete a review of the program.

Summary of Allegations and Audit Results

The Navy Public Works Center, San Diego, California, environmental services employees made eight allegations of procedural violations and two allegations of technical violations during the OMB Circular No. A-76 public-private competition for environmental services. The employees also alleged three potential adverse impacts as a result of the contract award to Shaw Infrastructure, Inc. One allegation of a procedural violation was substantiated, but had minimal effect on the MEO and the decision to award performance to a private contractor. Seven allegations were not substantiated and two allegations were indeterminable. We were unable to make a determination on the results of the three alleged potential adverse impacts and plan to issue a second report discussing the importance of monitoring contractor performance.

Procedural Issues

The allegations of procedural violations related to the solicitation for the OMB Circular No. A-76 competition for environmental services and the associated amendments to the solicitation; the public review period during the administrative appeals process and the withholding of contractor bid information from the MEO; contract funding; the timeframe of the competition; and the integrity of the study. Of the eight procedural allegations, one was substantiated, but had minimal effect on the MEO, five were unsubstantiated, and two were indeterminable. A discussion of the allegations of procedural violations and our audit results follows.

Procedural Allegation 1. In violation of the Federal Acquisition Regulation (FAR), only 1 of 49 plan holders received complete bid information during this Web-based solicitation. Of 16 total amendments to the solicitation, only 11 were posted to the Web. It appears that the contractor had the benefit of timely access to this information and the in-house Government employees did not.

Audit Results. The allegation was substantiated, but had minimal effect on the MEO. There were 18 total amendments to the solicitation, but 2 were issued after the allegations were made. The contracting office distributed the amendments by posting them to the NAVFAC E-Solicitation Web site; however, amendments 12 through 15 were not posted or otherwise provided to the MEO at the same time they were provided to Shaw, as required by FAR Subpart 15.206. Amendment 16 corrected an administrative error in Section F, "Performance Period of the Contract," to make it agree with Section B, "Offeror Acceptance," and was provided to the MEO. Amendments 17 and 18 were issued after a final decision was reached as a result of the administrative appeal process.

Amendments Not Posted on the E-Solicitation Web Site.

Amendments 12 through 15 were not posted on the E-Solicitation Web site or otherwise provided to the MEO at the same time as they were provided to the

contractor. The contracting officer stated that she realized that the MEO did not have all amendments during the technical balancing process, which is the process of comparing the best value contractor proposal with the Government proposal to assess whether the same level of performance is proposed. According to the contracting officer, once she realized the error, she transmitted amendments 12 through 15 to the MEO on July 23, 2004. The MEO's responses to technical balancing questions were due on July 26, 2004, however, the contracting officer extended the date to July 28, 2004.

The contracting officer agreed that it was an error that the MEO did not receive amendments 12 through 15 at the same time as Shaw. According to the contracting officer, the amendments did not materially alter the requirements of the performance work statement and were more clarification in nature, and we agree with that assessment. Amendments 14 and 15 were administrative. Although Amendments 12 and 13 clarified portions of the performance work statement, added four pieces of Government-furnished equipment, and added some workload data to one of the exhibits, they do not appear to be significant changes.

- Amendment 12, May 28, 2004, extended the date for receipt of the technical and price proposals from June 1, 2004, to June 4, 2004, and included a page of notes (expectations and interpretations) to the standard schedule for pickups of containerized solid waste services.
- Amendment 13, June 24, 2004, informed offerors that as a result of the fourth round of discussions, revised proposals were due on June 28, 2004. The amendment also added two washing machines and two dryers as additional Government-furnished equipment, and added workload data to the textile recycling technical exhibit.
- Amendment 14, July 2, 2004, formally closed discussions and informed offerors that final proposal revisions were due July 6, 2004.
- Amendment 15, July 14, 2004, revised FAR clause 52.207-2, "Notice of Cost Comparison," in the solicitation to change the public review period from 30 working days to 15 working days.

It is important that the contracting officer communicate with the MEO as if they were another offeror from industry and ensure that they are sent solicitation amendments concurrently with industry. However, we do not believe that because the MEO received amendments 12 through 15 later than Shaw, the in-house offer was adversely impacted.

Procedural Allegation 2. The solicitation date was extended to accommodate one contractor. While the extension of the solicitation date was communicated to this contractor, this information was not available to the in-house Government employees. This action was in further violation of the FAR.

Audit Results. The allegation was unsubstantiated. The solicitation date was not extended; however Amendment 7 opened discussions with the offeror and stated that the date of receipt for revised proposals was April 7, 2004. As a result of

discussions between Shaw and the Government, Amendments 8 through 14 extended the date for receipt of revised proposals. These discussions were held at the discretion of the contracting officer. Although amendments 12, 13, and 14 were not provided to the MEO in a timely manner, the extension of the due date for receipt of proposals did not affect the MEO.

Discussions Between Shaw and the Government. FAR Subpart 15.306, “Exchanges With Offerors After Receipt of Proposals,” states that discussions, or negotiations, are exchanges between the Government and offerors that are undertaken with the intent of allowing the offeror to revise its proposal. The primary objective of discussions is to maximize the Government’s ability to obtain best value, based on the requirements and evaluation factors set forth in the solicitation. The scope and extent of discussions are a matter of contracting officer judgment.

Shaw submitted technical and price proposals during Step 2 of the solicitation process. The members of the technical and price evaluation boards reviewed Shaw’s technical and price proposals and briefed their initial findings to the source selection board on March 9, 2004. After the initial reviews, the source selection board recommended that the technical and price evaluation boards conduct discussions with Shaw to resolve the outstanding issues identified during the initial reviews. On March 16, 2004, the source selection authority approved the source selection board recommendation that discussions be held with Shaw.

Discussions were officially opened on March 24, 2004, via amendment 7. During each round of discussions, the members of the technical and price evaluation boards reviewed Shaw’s proposal submissions and response to prior questions, and asked further questions or for clarifications. Four rounds of discussions were held, from April 19 through July 1, 2004, before the technical and price evaluation board members rated Shaw’s proposals as acceptable. Each time the boards requested clarification or asked additional questions, the contracting officer extended the due date to allow Shaw to respond and revise its proposal. The contracting officer and legal representative on the source selection board stated that four discussions were not unusual and that it was in the Government’s best interest to continue discussions, as allowed by the FAR.

Procedural Allegation 3. All information related to the contractor bid was withheld from the in-house Government employees in violation of procedural guidance. All documents related to the Government’s bid were available and provided to the contractor in full detail, while the contractor bid was redacted and unavailable to the Employee Appeal Committee during the public review and administrative appeal period. The employees requested this information, and the contract specialist overseeing the study denied the request. The result of this decision, with full transparency of the Government bid to the contractor while contractor bid information was withheld, was a decision biased in the contractor’s favor.

Audit Results. The allegation was unsubstantiated. The contracting officer followed FAR guidance and did not release contractor bid information to the MEO. We are concerned, however, with the fairness of a process that allows the contractor access to all information related to the MEO bid during the appeal

period, while the MEO cannot review the contractor's proposal because it is considered proprietary. This competition was held under the previous circular, which had an administrative appeal process. Under the revised circular, the appeal process is eliminated, and the agency tender official, the inherently Governmental agency official responsible for the MEO, will have the same rights as the contractor—including the ability to protest the final decision.

Administrative Appeal Process. The previous circular states that as part of the administrative appeals process, agencies shall make all relevant documents available for review. The detailed documentation shall include, at a minimum, the in-house cost estimate, with detailed supporting data, the completed cost comparison form, and the management plan.

The employees requested contractor bid information because they were relying on draft DoD Handbook 4100.XX-H, "A-76 Cost Comparison Handbook #7, Public Review and the A-76 Administrative Appeal Process," October 2000, which included "the selected contract offeror's cost proposal" in a list of documentation generally made available to the affected parties during the public review period. However, FAR Subpart 3.104-3 does not allow the release of contractor proposal information before the award of the contract. FAR clause 52.207-2 does allow the release of the in-house cost estimate when the tentative decision favors the MEO.

- FAR Subpart 3.104-3, "Statutory and Related Prohibitions, Restrictions, and Requirements," states that a person must not, other than as provided by law, knowingly obtain contractor bid or proposal information or source selection information before the award of a Federal agency procurement contract to which the information relates.
- FAR clause 52.207-2, "Notice of Cost Comparison (Negotiated)," which was included in the solicitation, states that if the result of the cost comparison favors Government performance, the contracting officer will publicly disclose this result, the completed cost comparison form and its detailed supporting data, and the price of the offer most advantageous to the Government.

We asked the DoD Assistant Director of Housing and Competitive Sourcing why "the selected contract offeror's cost proposal" was included in a list of information generally available for review. She stated that the appeal process was designed to review the bid the Government developed, not the contractor's proposal. The Assistant Director stated that the entire handbook series was in no way designed to provide DoD policy, procedure, or guidance, but was developed as best practice guidelines. The handbooks were marked as "draft" and were not finalized. Although the goal was to finalize the handbooks, she stated they were not able to because OMB started working on the revised circular.

Procedural Allegation 4. Public review period was reduced from 30 days to 15 days to allow a single contractor time to resubmit their bid. During this time, eligible appellants requested contractor bid information in accordance with Administrative Appeal Process guidelines (DoD "A-76 Cost Comparison

Handbook,” October 2000). This information was withheld from Government employees.

Audit Results. The allegation was unsubstantiated. Although the public review period was reduced from 30 working days to 15 working days, the reduced time period was established prior to the appeals period and was consistent with applicable guidance. The public review period did not allow a single contractor time to resubmit their bid, as the allegation states, but was a specific time frame during which an eligible appellant could submit a cost comparison appeal for consideration during the administrative appeals period. Additionally, as we stated in the audit results to Procedural Allegation 3, contractor bid information was withheld in accordance with the FAR.

Public Review Period. The FAR states that if the result of the cost comparison favors Government performance, the contracting officer shall inform interested parties that the completed cost comparison form and detailed supporting data relative to the Government cost estimate are available for public review. The FAR provides for contracting officer discretion on the number of days allowed for the public review period. Specifically, FAR Subpart 7.306(b)(3) states:

The public review period shall begin with the contracting officer’s announcement of the cost comparison result and availability of the cost comparison forms and detailed supporting data to interested parties. The review period shall last for the period specified in the solicitation (at least 15 working days, up to a maximum of 30 working days if the contracting officer considers the action to be complex).

As noted in our response to Procedural Allegation 3, the solicitation included FAR clause 52.207-2, “Notice of Cost Comparison (Negotiated),” which states that the award is conditioned on the offer remaining the more economical alternative after completing a public review period of 30 working days and resolving any requests for review under the agency appeals procedure. According to the contracting officer, the 30 working day review period included in the solicitation was an administrative error. Amendment 15 was issued on July 14, 2004, to correct the error and revised the public review period to 15 working days (22 calendar days). The contracting officer announced the tentative decision to select the Government to perform the environmental services on August 16, 2004, and established a 22 calendar day public review period beginning on August 17, 2004, and ending on September 7, 2004.

Procedural Allegation 5. Prior to contract signing, the Government must have funds appropriated to pay for the contract. It is in direct violation of the FAR to sign a contract in which funding has not been appropriated. Navy Public Works Center is a Navy working capital fund organization rather than operations and maintenance funded. It appears that the contract will be awarded without first appropriating funding and relying on the commodity income to fund the contract costs.

Audit Results. The allegation was unsubstantiated. The firm-fixed-price portion of the contract was funded prior to contract signing, and IDIQ work was not

guaranteed by the contract. The contracting officer included the appropriate clauses in the contract and the minimum guarantee of the contract was funded.

Contract Funding. FAR Subpart 32.7, “Contract Funding,” describes basic requirements for contract funding and procedures for using limitation of cost or limitation of funds clauses. Specifically, FAR Subpart 32.7 states that no officer or employee of the Government may create or authorize an obligation in excess of the funds available, or in advance of appropriations, unless otherwise authorized by law. Before executing any contract, the contracting officer shall expressly condition the contract on availability of funds in accordance with FAR Subpart 32.703-2.

FAR Subpart 32.703-2 states that the contracting officer may initiate a contract action properly chargeable to funds of the new fiscal year before these funds are available, provided that the contract includes the clause at 52.232-18, “Availability of Funds.” It also states that a 1-year indefinite-quantity or requirements contract for services that is funded by annual appropriations may extend beyond the fiscal year in which it begins, provided that any specified minimum quantities are certain to be ordered in the initial fiscal year and the contract includes the clause at 52.232-19, “Availability of Funds for the Next Fiscal Year.” Both FAR clause 52.232-18 and FAR clause 52.232-19 were included in the contract.

Firm-Fixed-Price Requirements. On January 12, 2005, the Navy awarded contract no. N68711-03-D-4302 to Shaw for approximately \$8.09 million. The firm-fixed-price portion of the contract with Shaw was about \$4.26 million, which included the base year firm-fixed-price requirements and the requirements of the phase-in period. The firm-fixed-price portion of the contract was funded prior to contract signing. On December 28, 2004, the Navy Public Works Center, San Diego, Commanding Officer authorized \$4.26 million in funds expiring September 30, 2005, to complete the phase-in period and the firm-fixed-price portion of the contract for environmental services for the Navy Public Works Center, San Diego.

Indefinite-Delivery, Indefinite-Quantity Requirements. The IDIQ portion of the contract was about \$3.83 million, which included the base year IDIQ requirements. The Navy Public Works Center, San Diego, is a Navy working capital fund organization. A working capital fund organization must operate much like a business receiving funding from customers rather than through direct appropriation. Although funding was authorized for the firm-fixed-price portion of the contract, funding was not authorized for the IDIQ portion of the contract prior to contract signing. However, the contract included clause 5252.216-9310, “Combination Firm Fixed Price/Indefinite Quantity Contract,” from the Navy Facilities Acquisition Supplement, March 2002, also known as the NAVFAC Contracting Manual. This clause states that the quantities specified as indefinite quantity are estimates only and may be ordered by issuance of separate task orders, and that the minimum guarantee of work is the firm-fixed-price portion of the contract. Additionally, the contract included FAR clause 52.216-22, “Indefinite Quantity,” which states that the contract is an indefinite-quantity contract for the supplies or services specified and effective for the period stated in the schedule. The quantities of supplies and services specified

in the schedule are estimates only and are not purchased by this contract. Delivery or performance shall be made only as authorized by orders issued in accordance with the ordering clause.

Procedural Allegation 6. The commercial activity competition rules dictated that the final decision be reached no later than September 30, 2004. The final decision date exceeded the schedule established in the “Application of the Deviation to Initiatives in the Department of Defense Transition Plan.” On this basis, the competition should have been cancelled.

Audit Results. The allegation was unsubstantiated. A tentative decision was made on August 16, 2004. The final decision was not made until December 3, 2004, because the Administrative Appeal Authority needed additional time to complete the appeal process.

OMB Circular No. A-76 Transition. When OMB issued the revised circular, DoD had 216 competitive sourcing initiatives in progress. The 216 competitive sourcing initiatives had to meet the transition requirements of the revised circular, or the DoD competitive sourcing official had to request a deviation from OMB to continue under the previous circular. Of the 216 competitive sourcing initiatives, 150 required a deviation from OMB to continue under the previous circular, 55 met the transition requirements of the revised circular permitting them to continue under the previous circular, and 11 were expected to transition to the revised circular. The environmental services competition at the Navy Public Works Center, San Diego, was one of the 150 initiatives that required a deviation to continue under the previous circular.

On October 24, 2003, the DoD competitive sourcing official requested a deviation from OMB for the 150 competitive sourcing initiatives. On November 17, 2003, OMB authorized DoD to proceed under a deviation for the limited purpose of completing the 216 competitive sourcing initiatives in the DoD transition plan. OMB expected DoD to make final decisions for the cost comparisons no later than September 30, 2004, the completion date projected by the DoD competitive sourcing official.

Competition Decision. The contracting officer announced the tentative decision to select the Government as the provider of the environmental services on August 16, 2004, and established the administrative appeals public review period ending on September 7, 2004. The DoD Commercial Activities Management Information System user guide states that once the tentative decision is reached, the initiative status changes from in-progress to completed. Shaw appealed the tentative decision by the established public review deadline. The Administrative Appeal Authority was required to review the appeal and make a decision within 30 days. The Appeal Authority was, however, granted two extensions because of complexities in the appeal. The final decision was made December 3, 2004.

If the contractor had not appealed the tentative decision, the final decision would have been made after the public review period ended on September 7, 2004, well within the September 30, 2004, deadline. Although the contractor appealed and the final decision was not made until December 3, 2004, it would

not have made business sense to cancel the competition. A tentative decision had been made within the deadline and the competition was nearly complete at that time. On this basis, we do not believe the competition should have been cancelled.

Procedural Allegation 7. The Navy Public Works Center competition was conducted as a pilot with a compressed 18-month schedule, following a draft protocol reliant upon support from internal Department of Navy resources in Washington, D.C. This support was withdrawn when new commercial activity guidelines were issued in 2003, leaving Public Works Center the only fast-tracked pilot competition to progress to final decision. The pilot competition protocol was a misguided attempt to mimic the new A-76 rules, which were the subject of Congressional scrutiny in September 2004.

Audit Results. The allegation was indeterminable based on the information available. A memorandum was issued establishing the environmental services competition as a pilot program; however, it did not establish a limited timeframe to complete the competition. We were unable to support or refute the claim that support was withdrawn. In addition, while the pilot program did implement rules similar to those in the revised circular, we were unable to support that it was a “misguided attempt to mimic the new rules.”

Pilot Program. The environmental services competition was announced as a multifunction competition on June 17, 2002. The OMB Circular No. A-76, Revised Supplemental Handbook, states that cost comparisons of multiple activities should be completed within 36 months from the date of public notification; therefore, the environmental services competition should have been completed no later than June 2005. On August 15, 2002, the Assistant Secretary of the Navy (Installations and Environment) signed a memorandum which establishes the competitive sourcing process improvement pilot at the Navy Public Works Center, San Diego, California. Although the memorandum does not specifically identify the environmental services competition, it does identify competitions announced in FY 2002 as part of the pilot program. The pilot program memorandum does not establish a completion timeframe; however, various e-mails state the competition was to be completed in 20 months. The competition took approximately 26 months to complete.

The pilot program memorandum states that the performance work statement and MEO teams would have a support contractor and funding for contractor support would be provided by the Office of the Chief of Naval Operations. However, the memorandum does not reference any other reliance upon support from internal Department of Navy resources in Washington, D.C., as the allegation states. One of the e-mails the employee representative provided mentions that a host of advisors, including Washington, D.C., Hawaii, and the region, would provide support. According to the allegation, this support was withdrawn when new commercial activity guidelines were issued in 2003, leaving the Navy Public Works Center, San Diego, the only fast-tracked pilot competition to progress to final decision. We were verbally informed by multiple people, including the performance work statement team leader and the MEO team leader, that at the beginning of the environmental services competition, many people from the Headquarters level were involved. After the revised circular was issued

in May 2003, the support seemed to disappear. We were unable to support or refute this claim.

Procedural Allegation 8. The contractor at issue, Shaw Environmental and Infrastructure, has a history of manipulating the commercial activity contracting process. Their performance in this solicitation is consistent with their past practices, raising serious questions about the integrity of our public-private competition.

Audit Results. The allegation was indeterminable based on the information available. This allegation was based on a previous OMB Circular No. A-76 competition at Fort Sam Houston, Texas, where the contracting officer found the Shaw proposal unacceptable after multiple proposal revisions. During discussions and evaluations of Shaw's Fort Sam Houston proposal, the evaluators noted that Shaw had responded to agency concerns regarding staffing levels in particular areas by adding staffing in the areas identified but simultaneously decreasing staffing in other areas that had been previously determined to be adequately staffed. This approach required the agency to completely reevaluate the entire proposal, including all areas previously found acceptable, following proposal revisions. Shaw protested but the Comptroller General denied the protest in Comptroller General Decision B-291121, Matter of Shaw Infrastructure, Inc., November 19, 2002.

The technical evaluation board for the OMB Circular No. A-76 public-private competition for environmental services also documented concerns about Shaw's approach for addressing the board's comments on staffing deficiencies in the Shaw proposal. However, the technical evaluation board report states the board assumes that Shaw will complete the work because they stated they have adequately staffed the functions based on their expertise. In addition, the source selection board report states that the board deliberated extensively on these and other concerns and "agrees these are weaknesses, however, Shaw will be able to accommodate any fluctuations in workload, as it has stated in its responses to discussion items." *² We do not believe the instance of one Comptroller General decision involving the contractor proves a history of manipulating the commercial activity process or is a basis to question the integrity of the public-private competition.

Technical Issues

The allegations of technical violations related to the technical evaluation of Shaw's proposal and the final technical evaluation report. Both allegations were unsubstantiated.

Technical Allegation 1. The technical evaluation report assessing contractor capability was not certified. Two of the four technical evaluation board members refused to sign the technical evaluation report.

² This area of the report represents source selection information that was omitted.

Audit Results. The allegation was unsubstantiated. All four members of the technical evaluation board signed the technical evaluation report. However, two of the four members disagreed with the contractor's acceptable rating for Subfactor T1.2, capacity to accomplish the work, and attached letters of dissention to the final report. See Technical Allegation 2.

Technical Allegation 2. Two letters of dissention regarding contractor technical capability were placed in the file by members of the technical evaluation board. These concerns do not appear to have been given due consideration in the final decision.

Audit Results. The allegation was unsubstantiated. Two members of the technical evaluation board attached letters of dissention to the final report, but the concerns appear to have been given due consideration by the members of the source selection board.

Technical Evaluation. The source selection plan states that all technical evaluation board members must sign the technical evaluation report. If the board members are unable to reach unanimous agreement on the content of a report, the technical evaluation board chairperson should forward minority reports prepared by the dissenting members. The four technical evaluation board members signed the final report and submitted the report to the source selection board on July 1, 2004. The technical evaluation board rated Shaw as acceptable, which meant that the proposal met the stated requirements, with no deficiencies, but there may be weaknesses that present some risk of unsuccessful contract performance. However, two of the four members of the technical evaluation board attached letters of dissention regarding the contractor's acceptable rating for the Subfactor T1.2, capacity to accomplish the work, to the final technical evaluation report.

*³

Although not documented, the technical evaluation board members verbally stated that they felt pressured to rate Shaw as acceptable. The board members expressed frustration with the answers they were receiving from Shaw because Shaw did not provide adequate information on how they would accomplish the tasks. They also stated that they were unable to develop defensible metrics or establish a numerical rating system that would identify the contractor's inability to perform the work. According to the source selection board chairperson, she advised the technical evaluation board members that when identifying weaknesses within Shaw's proposal, the board must support its findings based upon the criteria established in the solicitation. She further stated that the weaknesses identified by the technical evaluation board did not support a rating of less than acceptable. The source selection board stated that the technical

³ This area of the report represents source selection information that was omitted.

evaluation board concerns were attributed to the board's unfamiliarity with the different process of how Shaw proposed to do the work, as opposed to how the Navy performed the work prior to the competition. The source selection board members stated that Shaw proposed the minimum bid based on the performance work statement requirements.

Source Selection Evaluation. The technical evaluation board chairperson briefed the source selection board on July 1, 2004. *⁴

The source selection board stated that after the briefings from the price and the technical evaluation boards, the source selection board members deliberated extensively on the overall findings of the evaluation boards. The source selection board's final report stated that the board acknowledged the concerns of the dissenting technical evaluation board members and the weaknesses identified in the technical evaluation board report, and agreed that Shaw's proposal had weaknesses. *⁴

Potential Adverse Impacts

The three allegations of potential adverse impacts related to disruption of Navy services, an increase in notices of violations, and job loss for the environmental services employees. Although the Navy awarded the contract to Shaw on January 12, 2005, during the 79-day transition period, the Government continued to provide service. Shaw assumed operations of the environmental department on April 1, 2005, and the first performance period of the contract was a 6-month

⁴ This area of the report represents source selection information that was omitted.

period that ended on September 30, 2005. We were unable to substantiate the potential adverse impacts based on a 6-month period of contractor performance. Since Shaw assumed operations, the Navy Public Works Center, San Diego, is responsible for monitoring Shaw's performance to determine whether they are in compliance with the contract. We plan to issue a second report discussing the importance of monitoring Shaw's performance to manage any potential adverse impacts.

Potential Adverse Impact 1. Adverse impacts to Navy fleet operations are expected as a result of disruption of hazardous waste pickup and disposal services and oily waste treatment operations.

Audit Results. According to the contracting officer and the regional compliance manager, service to the Navy Fleet Operations has not been disrupted as a result of the change in service. Although Shaw sometimes did not complete the work in the proposed amount of time, the regional compliance manager did not consider it a disruption and stated it was going to take time for everyone to adjust. We were unable to substantiate disruption of hazardous waste pickup and disposal services and oily waste treatment operations on a 6-month period of contractor performance. The Residual Organization, composed of Navy Public Work Center employees, is responsible for monitoring Shaw's performance and taking appropriate action, as necessary, to ensure Shaw performs the contract requirements.

Potential Adverse Impact 2. Notices of violation from regulatory agencies are expected to increase as a result of this decision, which will be costly and have an adverse impact on the Navy fleet.

Audit Results. The regional compliance manager stated that since Shaw began performance on April 1, 2005, ten notices of violation were received at facilities operated by Shaw or one of Shaw's subcontractors; however, five of the violations were the Government's responsibility because they were findings associated with issues prior to Shaw taking over operations. The regional compliance manager stated that the violations Shaw has received are similar in nature to those that the Navy Public Works Center, San Diego, received in the past. We do not have adequate data to determine whether the number of violations has increased. The Residual Organization needs to closely monitor and document Shaw's performance so that action can be taken if the number of violations increases.

Potential Adverse Impact 3. Approximately 100 constituents who have demonstrated commitment to the success of the department and protection of the environment now face job loss as a result of this flawed decision.

Audit Results. Regardless of the outcome of a public-private competition, job loss generally occurs. The Government Accountability Office report, "Effects of A-76 Studies on Federal Employees' Employment, Pay, and Benefits Vary," March 2001, states that personnel reductions are key to achieving reduced costs from A-76 competitions. In addition, the Center for Naval Analyses report, "Analysis of DFAS Military Retired and Annuitant Pay Sourcing Options," September 2003, states that "in any public-private competitions, even

competitions when the MEO prevails, jobs are put at risk, and there is generally a Reduction-In-Force as a result of jobs being eliminated and grades being reduced.” Therefore, it is true that the Government employees who performed this function were at risk of losing their jobs.

Reduction In Force. On December 3, 2004, the final decision was made to award the environmental services function to Shaw. Although 103 positions were affected when the Navy announced the public-private competition in June 2002, on December 10, 2004, there were 77 environmental services employees⁵ whose positions were scheduled to be eliminated. As a result of the reduction-in-force process, all 77 positions were eliminated and 25 environmental services employees were involuntarily separated from the Government. Ten of the 25 involuntarily separated employees were employed by Shaw as of July 26, 2005. The following table shows the status of the 77 affected environmental services employees.

Navy Public Works Center Affected Positions		
<u>Status</u>	<u>Number of Employees</u>	<u>Employed by Shaw</u>
Retained Government jobs		
Downgraded to lower grade level	6	-
Stayed at the same grade level	38	-
Subtotal	44	-
Retired from Government		
Regular	2	1
Early	3	0
Subtotal	5	1
Separated from Government		
Resigned	3	0
Involuntary separation	25	10
Subtotal	28	10
Total	77	11

⁵ The reduction in force announcement dated December 10, 2004, states that 78 employees would be affected; however, one employee listed onboard as of December 10, 2004, had already resigned from the Government on September 20, 2004.

Appendix A. Scope and Methodology

We performed this audit in response to a request from Congresswoman Davis to review the Navy Public Works Center, San Diego, environmental department employees' allegations concerning the public-private competition for environmental services at the Navy Public Works Center, San Diego, California. The allegations consisted of seven procedural issues, two technical issues, and three potential adverse impacts as a result of the contract award to Shaw Infrastructure, Inc. We received a similar complaint through the Defense Hotline. In addition to the allegations submitted through the congressional request, the Hotline complaint included an eighth procedural issue. We plan to issue a second report discussing the Government offer in public-private competitions and the importance of monitoring contract performance.

We met with Navy and NAVFAC strategic sourcing officials. We interviewed and obtained documentation from individuals involved in the public-private competition, including members of the source selection board and the technical evaluation board, the agency tender official, the MEO team leader, the performance work statement team leader, the contracting officers, the MEO legal advisor, and the employee representative. We met with the regional compliance manager to obtain information on violations and disruptions to Navy service. We reviewed additional letters from employees of the Navy Public Works Center, San Diego.

We reviewed the FAR, applicable OMB Circular No. A-76 guidance, and DoD directives and instructions related to the competitive sourcing program. We reviewed documentation from the public-private competition, including the solicitation, amendments, performance work statement, and Shaw's technical and price proposals. We reviewed reports from the price evaluation board, technical evaluation board, and source selection board. We also reviewed the Administrative Appeal Authority report. We reviewed the contract, modifications, and other documentation used in the public-private competition. We reviewed monthly performance reports from April through July 2005.

We performed this audit from February through November 2005 in accordance with generally accepted government auditing standards.

Use of Computer-Processed Data. We did not use computer-processed data to perform this audit.

Government Accountability Office High-Risk Area. The Government Accountability Office has identified several high-risk areas in DoD. This report provides coverage of the Defense Infrastructure Management and Defense Contract Management high-risk areas.

Prior Coverage

No prior coverage has been conducted on the subject during the last 5 years.

Appendix B. Congressional Request

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Congress of the United States
House of Representatives
Washington, DC 20515-0553

COMMITTEES:
ARMED SERVICES
SUBCOMMITTEES:
TERRORISM, UNCONVENTIONAL THREATS AND
CAPABILITIES
MILITARY READINESS
EDUCATION AND THE WORKFORCE
SUBCOMMITTEES:
EDUCATION REFORM
SELECT EDUCATION
VETERANS
SUBCOMMITTEE:
BENEFITS

December 17, 2004

The Honorable Joseph E. Schmitz
Office of the Inspector General
U.S. Department of Defense
The Pentagon
Washington, DC 20301-1900

VIA FACSIMILE: (703) 604-8567

Dear Mr. Schmitz:

I am writing to your office at the request of the civilian employees of the Environmental Department at the Navy Public Works Center, San Diego (PWC), many of who are my constituents.

These individuals have written to me with the significant concerns they share about the process that was used to outsource the services they currently provide to the Navy. I have enclosed a sampling of the letters I have received from PWC's employees detailing their concerns for your review. I understand that they have written to your office directly to bring this matter to your attention.

While the PWC's employees are asking for a stay of the contract's award, they are more interested in preserving the integrity of the Department of Defense's contracting process, which they believe was compromised in this specific instance. I hope that you and your staff will review the allegations made in the attached documents and, if substantiated, take appropriate action to ensure that the contract in question is compliant with current regulations and that similar errors are not repeated in future contracting awards.

With the specter of additional outsourcing of Defense Department functions to the private sector in the future, every reasonable effort must be made to certify that contract awards are in the very best interest of the U.S. Government. I share the PWC's employees desire to guarantee this process is above question. I would appreciate your office's efforts to make certain this is the case.

Sincerely,


SUSAN A. DAVIS
Member of Congress

cc: U.S. Navy, Office of Legislative Affairs

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Appendix C. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition, Technology, and Logistics
Deputy Under Secretary of Defense (Installations and Environment)
Under Secretary of Defense (Comptroller)/Chief Financial Officer
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)
Director, Program Analysis and Evaluation
Director, Defense Procurement and Acquisition Policy

Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy
Commanding Officer, Navy Public Works Center, San Diego

Department of the Air Force

Auditor General, Department of the Air Force

Combatant Command

Inspector General, U.S. Joint Forces Command

Non-Defense Federal Organization

Office of Management and Budget

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Homeland Security and Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Efficiency and Financial Management, Committee on Government Reform

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member (cont'd)

House Subcommittee on National Security, Emerging Threats, and International Relations, Committee on Government Reform

House Subcommittee on Technology, Information Policy, Intergovernmental Relations, and the Census, Committee on Government Reform

Honorable Susan A. Davis, U.S. House of Representatives

Team Members

The Department of Defense Office of the Deputy Inspector General for Auditing, Contract Management prepared this report. Personnel of the Department of Defense Office of Inspector General who contributed to the report are listed below.

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