Report No. D-2007-128 September 26, 2007

# Inspector General
## United States Department of Defense


# Hotline Allegations Concerning the Defense Threat Reduction Agency Advisory and Assistance Services Contract

**Additional Copies**

To obtain additional copies of this report, visit the Web site of the Department of Defense Inspector General at http://www.dodig.mil/audit/reports or contact the Secondary Reports Distribution Unit at (703) 604-8937 (DSN 664-8937) or fax (703) 604-8932.

**Suggestions for Future Audits**

To suggest ideas for or to request future audits, contact the Office of the Deputy Inspector General for Auditing at (703) 604-9142 (DSN 664-9142) or fax (703) 604-8932. Ideas and requests can also be mailed to:

ODIG-AUD (ATTN: Audit Suggestions)
Department of Defense Inspector General
400 Army Navy Drive (Room 801)
Arlington, VA 22202-4704


**Acronyms**

| | |
|---|---|
| A&AS | Advisory and Assistance Services |
| CB | Chemical and Biological |
| DCAA | Defense Contract Audit Agency |
| DTRA | Defense Threat Reduction Agency |
| FAR | Federal Acquisition Regulation |
| GAO | Government Accountability Office |
| IDIQ | Indefinite-Delivery, Indefinite-Quantity |
| IG | Inspector General |
| IT | Information Technology |
| NGIT | Northrop Grumman Information Technology |
| ODC | Other Direct Costs |
| RFP | Request for Proposal |
| WMD | Weapons of Mass Destruction |

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202–4704

September 26, 2007

MEMORANDUM FOR DIRECTOR, DEFENSE THREAT REDUCTION AGENCY

SUBJECT: Report on Hotline Allegations Concerning the Defense Threat Reduction Agency Advisory and Assistance Services Contract (Report No. D-2007-128)

We are providing this report for review and comment. The Director, Defense Threat Reduction Agency nonconcurred with the recommendations in the draft report. We considered management comments on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. We request that the Director, Defense Threat Reduction Agency reconsider his previous comments and provide revised comments on Recommendations 1. and 2. by October 26, 2007.

If possible, please send management comments in electronic format (Adobe Acrobat file only) to AudACM@dodig.mil. Copies of the management comments must contain the actual signature of the authorizing official. We cannot accept the / Signed / symbol in place of the actual signature. If you arrange to send classified comments electronically, they must be sent over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Questions should be directed to either Mr. Terry L. McKinney at (703) 604-9288 (DSN 664-9288) or Mr. Timothy E. Moore at (703) 604-9282 (DSN 664-9282). 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:

Richard B. Jolliffe
Assistant Inspector General
Acquisition and Contract Management

## Department of Defense Office of Inspector General

**Report No. D-2007-128** **September 26, 2007**
(Project No. D2006-D000CF-0262.000)

# Hotline Allegations Concerning the Defense Threat Reduction Agency Advisory and Assistance Services Contract

## Executive Summary

**Who Should Read This Report and Why?** Defense Threat Reduction Agency and DoD contracting officials should read this report. The report addresses issues dealing with competitive contract awards, proper use of integrated product teams in the negotiation of contracts, and profit rates in relation to contract performance risk.

**Background.** This audit was performed in response to allegations received by the Defense Hotline. Contract HDTRA1-05-D-0003 is a single-award, indefinite-delivery, indefinite-quantity task order contract to provide advisory and assistance services. The purpose of the Defense Threat Reduction Agency contract HDTRA1-05-0003 is to acquire advisory and assistance services for the Defense Threat Reduction Agency and its operational and related organizations, in support of research, planning, designing, developing, implementing, integrating, testing, applying, and evaluating emerging and mature technologies and developing and transitioning capabilities for the Defense Threat Reduction Agency and its customers. Overall, the Hotline received seven allegations. The allegations cover the solicitation, evaluation, and award of Defense Threat Reduction Agency contract HDTRA1-05-D-0003 and the eight* related task orders, valued at $62.7 million, awarded to date.

**Results.** Overall, we substantiated six of the seven allegations (see Appendix B for allegations). In FY 2006, Defense Threat Reduction Agency contracting officials awarded a $375 million single-source, indefinite-delivery, indefinite-quantity advisory and assistance service contract using flawed techniques that were in conflict with the Federal Acquisition Regulation. Defense Threat Reduction Agency officials negotiated contract prices and terms using the final revised proposal after informing the contractor that it was the only company in negotiations with the Defense Threat Reduction Agency. Officials based the contract award on a revised final proposal developed by the contractor with Defense Threat Reduction Agency assistance that was substantially different from requirements contained in the contract solicitation. Defense Threat Reduction Agency officials also accepted "other direct costs" in the revised final proposal that would have changed the competitive environment if those requirements had been included in the initial request for proposal. The Defense Threat Reduction Agency accepted abnormally high profit rates on the revised cost proposal, and certified that contract prices were fair and reasonable based on a competitive contract award although the contract was not competitively awarded. As a result, the Defense Threat Reduction Agency paid more than necessary for advisory and assistance service tasks, including $10.2 million to

*Of the eight task orders, four task orders were awarded within a month after the contract was signed. The other four task orders were awarded in and after February 2006.

procure dedicated facilities, and $792,372 to obtain initial information technology equipment.

The Director of Defense Threat Reduction Agency should not exercise additional options on contract HDTRA1-05-D-0003. He should compete a multiple-award, indefinite-delivery, indefinite-quantity contract for advisory and assistance services. (See the Finding section of the report for the detailed recommendations.)

The Defense Threat Reduction Agency internal controls were adequate. We identified no material internal control weaknesses in the award of the Advisory and Assistance Services contract. However, we reviewed only one contract at Defense Threat Reduction Agency. Therefore, we can not comment on all of the internal controls.

**Management Comments and Audit Response.** The Director, Defense Threat Reduction Agency nonconcurred with the recommendations and stated that the Defense Threat Reduction Agency complied with the Federal Acquisition Regulation, statutes, and regulations in the award of the contract. Knowledgeable senior level personnel made the acquisition decisions. The report failed to: recognize Government benefits the Defense Threat Reduction Agency obtained; appreciate the intolerable consequences on the mission; and recognize the impracticality of the time frames to execute a new competition.

The Director, Defense Threat Reduction Agency stated his agency complied with Federal Acquisition Regulation 16.504 in determining that a single award contract was in the best interest of the Government. Senior leaders within the Defense Threat Reduction Agency thoroughly reviewed the use of a single-award contract and determined that was the best approach, which the Federal Acquisition Regulation allows. The Defense Threat Reduction Agency uses advisory and assistance services contracts for highly technical expertise on a continuous basis to support staff with mission demands. The Director stated that it would be impractical, and also hurt the mission, to compete each task between multiple-award contracts. The Director stated that the report does not identify any procedures not followed.

Our review validated Hotline allegations that Defense Threat Reduction Agency contract HDTRA1-05-D-0003 was awarded based on a final revised proposal that was significantly different from requirements contained in the contract solicitation, that contracting officials did not award a competitive contract, and that the contracting officer certified that contract prices were fair and reasonable based on a competitive contract award. Also, the contracting officer did not negotiate fair and reasonable prices, nor adequately evaluate contract "other direct costs," and officials did not determine reasonable profit rates, awarding the contract with abnormally high profit rates.

In the contract documentation, Defense Threat Reduction Agency officials conceded that the Federal Acquisition Regulation has a preference for multiple awards for advisory and assistance contracts. However, Defense Threat Reduction Agency officials have yet to present a cogent argument that the Government is better served by a single-award indefinite-delivery, indefinite-quantity contract. Defense Threat Reduction Agency officials state that they complied with Federal Acquisition Regulation provisions because the required paragraph was included in the Acquisition Plan that was approved by senior officials. However, this paragraph does not explain why the Defense Threat Reduction Agency will be better served by a single contractor reimbursed for all advisory and assistance tasks on a cost-plus basis than they would be by competing tasks among

several responsible contractors. For this contract, Defense Threat Reduction Agency officials did issue a solicitation in a competitive environment. However, the Defense Threat Reduction Agency did not receive a responsive proposal from any contractor and cannot claim its advisory and assistance contract was awarded on a competitive basis. Rather than work on a new solicitation after receiving no responsive bids, Defense Threat Reduction Agency officials worked with the incumbent contractor to develop a contract that did not resemble the original solicitation, that was not competed, that reimbursed the contractor for unnecessary costs, that had abnormally high profit rates, and that did not contain verifiable fair and reasonable prices. The procedures by which the revised final proposal was developed are not in conformance with the Federal Acquisition Regulation. We request the Director, Defense Threat Reduction Agency reconsider his response and provide a plan by October 26, 2007, to terminate this contract and award a multiple-award contract for advisory and assistance services.

# Table of Contents

## Background

This audit was performed in response to allegations received by the Defense Hotline. Overall, the Hotline received seven specific allegations (see Appendix B). The allegations cover the solicitation, evaluation, and award of Defense Threat Reduction Agency (DTRA) contract HDTRA1-05-D-0003 and eight[1] related task orders, worth approximately $62.7 million, awarded to date. The contract is a single-award, indefinite-delivery, indefinite-quantity (IDIQ) task order contract for advisory and assistance services (A&AS). The purpose of DTRA contract HDTRA1-05-D-0003 is to acquire A&AS for DTRA and its operational and related organizations, in support of research, planning, designing, developing, implementing, integrating, testing, applying, and evaluating emerging and mature technologies and developing and transitioning capabilities to DTRA customers. DTRA awarded the contract to Northrop Grumman Information Technology (NGIT) with a minimum award amount of $25,000 and a maximum amount of $375 million.

On January 6, 2005, DTRA contracting officials issued the request for proposals (RFP) for HDTRA1-04-R-0013,[2] closing on February 22, 2005. The solicitation resulted in one proposal, from the incumbent contractor. On May 20, 2005, the DTRA contracting officer sent the contractor a letter opening negotiations regarding the solicitation. Instead of exploring other options to foster some form of competition, DTRA decided to enter into direct negotiations with the contractor using an integrated product team. The DTRA contracting officer notified the incumbent contractor that the source selection process was dissolved. DTRA awarded the contract effective October 27, 2005. Four task orders were awarded within a month of the signed contract. Each task order has a base year and three option years. The first option year was exercised during October 2006.

**Advisory and Assistance Services.** Federal Acquisition Regulation (FAR) Part 2, "Definition of Words and Terms," defines advisory and assistance services as:

> Those services provided under contract by nongovernmental sources to support or improve: Organizational policy development; decision-making; management and administration; program and/or project management and administration; or R&D [Research and Development] activities. It can also mean the furnishing of professional advice or assistance rendered to improve the effectiveness of Federal management processes or procedures (including those of an engineering or technical nature). In rendering the foregoing services, outputs may take the form of information, advice, opinions, alternatives, analyses, evaluations, recommendations, training and day-

[1] Of the eight task orders, four task orders were awarded within a month after the contract was signed. The other four task orders were awarded in and after February 2006.

[2] The request for proposal for the A&AS contract was HDTRA1-04-R-0013; DTRA awarded the contract HDTRA1-05-D-0003.

to-day aid of support personnel needed for the successful performance of ongoing Federal operations.

**Competitive Contract Awards of Service Contracts.** According to the Public Contract Law Journal, the best method for the Government to determine that prices paid for services are fair and reasonable is to award service contracts on a competitive basis. Full and open competition assures cost effectiveness as well as reduces the potential for favoritism and conflicts of interest.

The "Competition in Contracting Act" is implemented in section 2304, title 10, United States Code (10 U.S.C. 2304) and 10 U.S.C. 2305. When conducting a procurement for property or services, 10 U.S.C. 2304 states that the agency shall obtain full and open competition through the use of competitive procedures in accordance with the requirements of this chapter and the FAR.

## Objective

Our overall audit objective was to determine whether contract procedures for contract HDTRA1-05-D-0003 were in compliance with applicable laws and regulations. Specifically, we examined the solicitation, award, administration, and funding of the contract. The focus of our review was to determine whether the seven allegations to the DoD Hotline were substantiated. See Appendix A for a discussion of the scope and methodology of our review.

## Review of Internal Controls

The DTRA internal controls were adequate as they applied to the audit objectives. We identified no material internal control weaknesses in the award of the A&AS contract. However, we reviewed only one contract at DTRA. Therefore, we cannot comment on all of the internal controls within DTRA.

# Negotiation and Award of DTRA Contract HDTRA1-05-D-0003

In FY 2006, DTRA contracting officials awarded a $375 million single-source, IDIQ, A&AS contract using flawed techniques that were in conflict with the FAR. Specifically, DTRA officials:

- based the contract award on a revised final proposal developed by the contractor with DTRA assistance that was substantially different from requirements contained in the contract solicitation,
- negotiated contract prices and terms of the final revised proposal after informing the contractor that it was the only company in negotiations with DTRA,
- accepted "other direct costs" in the revised final proposal that would have changed the competitive environment if those requirements had been included in the initial RFP,
- accepted abnormally high profit rates on the revised cost proposal, and
- certified that contract prices were fair and reasonable based on a competitive contract award although the contract was not competitively awarded.

The contracting officer did not follow FAR guidance when soliciting, negotiating, and awarding the contract. Originally, the procurement was solicited as competitive; however, DTRA entered into direct negotiations with the only contractor that submitted a proposal even though the revised final proposal was significantly different from the solicited requirement. As a result, DTRA paid more than necessary for A&AS tasks including $10.2 million to procure dedicated facilities and $792,372 to obtain initial information technology (IT) equipment and replace that equipment within a 3-year period.

## Criteria

**FAR Competition Requirements.** FAR 6.101, "Full and Open Competition Policy," requires, "with certain limited exceptions . . . that contracting officers shall promote and provide for full and open competition in soliciting offers and awarding Government contracts." Competitive procedures to meet the requirement include sealed bids, competitive proposals, combination of competitive procedures, or other competitive procedures.

**Requests for Proposals.** FAR 15.203, "Request for Proposals," states that requests for proposals "for competitive acquisitions shall, at a minimum, describe

the (1) Government's requirement; (2) Anticipated terms and conditions that will apply to the contract; (3) Information required to be in the offeror's proposal; and (4) Factors that will be used to evaluate the proposal" and each factor's relative importance.

The Government must not favor one contractor over another. If substantial changes are made to the RFP, all potential contractors need to receive those changes to evaluate the RFP. Additionally, if the contracting officer changes the RFP, the time the RFP is due may be extended.

**Amending the Solicitation.** FAR 15.206(e), "Amending the Solicitation," states that:

> If, in the judgment of the contracting officer, based on market research or otherwise, an amendment proposed for issuance after offers have been received is so substantial as to exceed what prospective offerors reasonably could have anticipated, so that additional sources likely would have submitted offers had the substance of the amendment been known to them, the contracting officer shall cancel the original solicitation and issue a new one, regardless of the stage of the acquisition.

**Communications With Offerors.** FAR 15.306(b)(2), "Exchanges With Offerors After Receipt of Proposals," states that communications:

> May be conducted to enhance Government understanding of proposals; allow reasonable interpretation of the proposal; or facilitate the Government's evaluation process. Such communications shall not be used to cure proposal deficiencies or material omissions, materially alter the technical or cost elements of the proposal, and/or otherwise revise the proposal.

FAR 15.306 (d) states that "negotiations are exchanges, in either a competitive or sole-source environment, between the Government and offerors, that are undertaken with the intent of allowing the offeror to revise its proposal. . . . When negotiations are conducted in a competitive acquisition, they take place after establishment of the competitive range and are called discussions."

**Pricing Policy.** FAR 15.402, "Pricing Policy," requires contracting officers to "purchase supplies and services from responsible sources at fair and reasonable prices." If the price is based on adequate competition, no further documentation of the fair and reasonable price is required. However, in the absence of competition additional justification is required.

**Adequate Price Competition.** FAR 15.403-1(c)(1), "Prohibition on Obtaining Cost or Pricing Data," provides that a price is based on adequate price competition if

> There was a reasonable expectation, based on market research or other assessment, that two of more responsible offerors, competing independently, would submit priced offers in response to the solicitation's expressed requirement, even though only one offer is

> received from a responsible offeror and if – (A) Based on the offer received, the contracting officer can reasonably conclude that the offer was submitted with the expectation of competition, e.g., circumstances indicate that – (1) The offeror believed that at least one other offeror was capable of submitting a meaningful offer; and (2) The offeror had no reason to believe that other potential offerors did not intend to submit an offer . . .

**Indefinite-Quantity Contracts.** FAR 16.504(a) states that "an indefinite-quantity contract provides for an indefinite quantity, within stated limits, of supplies or services during a fixed period." FAR 16.504(c)(2) states that:

> (2) Contracts for advisory and assistance services.
>
> (i) Except as provided in paragraph (c)(2)(ii) of this section, if an indefinite-quantity contract for advisory and assistance services exceeds 3 years and $11.5 million, including all options, the contracting officer must make multiple awards unless— (A) The contracting officer or other official designated by the head of the agency determines in writing, as part of acquisition planning, that multiple awards are not practicable. The contracting officer or other official must determine that only one contractor can reasonably perform the work because either the scope of work is unique or highly specialized or the tasks so integrally related; (B) The contracting officer or other official designated by the head of the agency determines in writing, after the evaluation of offers, that only one offeror is capable of providing the services required at the level of quality required; or (C) Only one offer is received.
>
> (ii) The requirements of paragraph (c)(2)(i) of this section do not apply if the contracting officer or other official designated by the head of the agency determines that the advisory and assistance services are incidental and not a significant component of the contract.

# DTRA A&AS Contract

DTRA awarded contract HDTRA1-05-D-0003 on October 27, 2005. The contract was flawed because: DTRA negotiated contract terms and conditions that were significantly different from requirements in the RFP after informing the contractor that it was the only company in direct negotiations, the contract included other direct costs that were not in the RFP, and DTRA agreed to accept abnormally high profit rates. The contracting officer also incorrectly certified that prices were fair and reasonable based on a competitive contract award.

**Proposals.** DTRA issued RFP HDTRA1-04-R-0013 on January 6, 2005, with provisions that competitive proposals be delivered to DTRA by February 22, 2005. The RFP stated that "The Government anticipates awarding one contract under full and open competition." DTRA had previously conducted an industry day session for all prospective offerors and interested parties on February 23, 2004, a year earlier. According to the DTRA acquisition plan, 76 representatives

from 53 companies attended. Twenty companies expressed interest and provided feedback on the requirement after the industry day session.

The RFP provided for the award of a single IDIQ contract with a ceiling of $375 million and an overall period of performance of 60 months. The RFP requested contractors to provide technical and cost proposals in four areas expected to result in the award of four task orders concurrent with or subsequent to the award of the basic contract. These four task orders included the following:

- Technology Development/Director's Support Group,
- Combat Support,
- Chemical and Biological Defense Non-Medical, and
- Chemical and Biological Medical.

DTRA received only one proposal, submitted by the incumbent A&AS contractor. The DTRA contracting officer stated no formal follow-up occurred with the other 52 companies to determine why they did not submit proposals; however, through conversations, companies indicated that proposals were not submitted because there was an entrenched incumbent. As one contractor stated in its comments concerning the February 23, 2004, industry day, "The incumbent on this effort has been the primary supplier of these services to DTRA and its predecessors for more than 30 years. As demonstrated during the last competition, it is very difficult to defeat a long standing incumbent for essentially follow-on work." Also, the industry day included several subcontractors. The contracting officer stated that he had expected more proposals in the response to the RFP.

**Notice of Source Selection.** DTRA selected the sole offeror as documented in a Source Selection Decision memorandum dated May 18, 2005. At that time, DTRA dissolved the formal source selection process and directed that the contractor propose an organizational conflict of interest plan, and technical and cost proposals for the Technology Development task order and Combat Support task order. These task orders must realistically and reasonably reflect updated requirements. The technical and cost proposals for the Chemical and Biological (CB) Defense directorate's medical and non-medical tasks must reflect a total understanding of the DTRA program and issues should be resolved using an Integrated Product Team.

On May 20, 2005, the DTRA contracting officer informed NGIT that "DTRA will enter into negotiations only with NGIT, via an Integrated Product Team." The letter also states:

- "Receipt of the letter "opens negotiations" between the Defense Threat Reduction Agency and Northrop Grumman Information Technology (NGIT) regarding solicitation HDTRA1-04-R-0013."
- "NGIT's proposal does not represent the best value to DTRA, however . . . the proposal is correctable."

- " . . . NGIT is hereby notified that the Agency A&AS source selection has been dissolved."

- "The goal is to resolve all deficiencies prior to NGIT submitting its final proposal."

Once DTRA entered direct negotiations with NGIT, months prior to the award of the contract, this procurement was no longer competitive.

**Technical Evaluations.** DTRA teams prepared technical evaluations of the offeror's technical approach for each of the four proposed task orders. The proposals were to be evaluated on overall technical support and management, past performance, organizational conflict of interest plan, specific work to be performed (first four task orders), and cost. The technical evaluations for the Technology Development and the Combat Support task orders are dated March 15, 2005, and contain the same wording although the evaluations are signed by different team leaders. The evaluations were brief and stated that they were based on historical information from the current A&AS contract and from an estimate of future A&AS requirements. The evaluations conclude that "a more detailed analysis by the Government could have been made if the offeror proposed to its Work Breakdown Structure and presented prime and subcontractor costs separately."

The evaluations for CB Defense Non-Medical and Medical task orders also contained almost the same wording although the evaluations were signed by different team leaders. The evaluations were dated March 15, 2005, and concluded, "the offeror failed to understand the complexities and scope of the technical aspects of the CB Non-Medical program [and the CB Medical program]. Therefore, the task order team cannot perform a meaningful cost realism analysis on the offeror's proposed estimated labor and other direct cost elements."

**Integrated Product Team Process.** The Integrated Product Team process was initiated in May 2005 and concluded in October 2005. Through the Integrated Product Team process, the contractor, with full knowledge that it was the only company negotiating the contract and with the assistance of DTRA, made significant revisions to its proposal.

The cost reviews of each of the first four task orders laid out the changes between the initial task order proposals and the revised final proposals developed by the Integrated Product Team. The cost reviews regarded the initial proposals as a baseline even though the technical analyses of those proposals stated that a complete review could not be conducted on two tasks and that the contractor did not understand the scope or complexities of the other two tasks. In addition, on the revised proposals, the non-medical and medical CB tasks were combined and a new task for Combating Weapons of Mass Destruction (WMD) was added. The contract time period is 60 months but the task orders have a base year and 3 option years (48 months), although the $375 million ceiling remained. Despite shortening the period of performance of the contract, the number of proposed labor hours on the revised final proposals increased significantly. See the table for proposed hours.

| Proposed Hours on Contract HDTRA1-05-D-0003 | | | |
|---|---|---|---|
| **Task** | **Initial** | **Revised** | **Percent Increase** |
| Technology Development | 1,009,887 | 1,349,722 | 34 |
| Combat Support | 144,862 | 433,946 | 199 |
| Chemical Biological | 244,474 | 478,272 | 96 |
| Combating WMD | 0 | 125,624 | N/A |
| **Total** | **1,399,223** | **2,387,564** | **71** |

The labor rate in the initial proposal differs drastically from the rate in the revised proposal. For instance, the average Combat Support task labor rate in the initial proposal is $358.94 per hour; in the revised final proposal, it is $91.83 per hour. The total labor hours for the contract increased 988,207 hours from the initial proposal. The revised final proposal contains no explanation for the difference other than a note that a suspected error in the initial proposal failed to account for all hours proposed.

The October 27, 2005, award of the basic contract and the subsequent award of the first four task orders were based on the final revised proposal that was substantially different than the contractor's initial proposal. DTRA inappropriately worked with the contractor to correct proposal deficiencies and materially altered both the technical and cost elements of the contractor's initial proposal. Under these circumstances, the FAR requires the contracting officer to cancel the original solicitation and issue a new one, regardless of the stage of the acquisition. In addition, because the contractor knew that it was the only company being considered, the contracting officer cannot claim that there was a reasonable expectation of competition on the revised final proposal.

**Acceptance of Other Direct Costs.** The revised final proposal contained contract "other direct costs" (ODC) adding direct costs that would have changed the competitive environment had those items been listed on the initial RFP. Foremost among those items is the $10.2 million cost of procuring a dedicated facility that the contractor leased for the DTRA A&AS support personnel. Also included were the costs of furnishing that facility with IT equipment, office furniture, and break room furnishings including dishwashers, microwaves, and refrigerators. The initial RFP did state that the contractor should demonstrate the ability to provide support to DTRA within 30 minutes after request during business hours.

ODCs are defined in the FAR as incidental services for which there is not a labor category specified in the contract such as travel or computer usage charges. The costs of facilities and equipment are normally considered an indirect cost. The Government pays contractors for those types of costs through the payment of overhead costs. In this case, the facility and equipment costs are considered direct costs because, as a contracting officer representative states:

> I find that it is reasonable for the government to reimburse the contractor for these ancillary items as they are required to support such things as snacks to visitors as well as employees, conferences, meetings, etc., conducted in support of the government.

DTRA did not comply with regulations to determine whether the costs proposed for ODCs were fair and reasonable. The contracting officer's cost review memorandums that certified fair and reasonable costs on the first four task orders stated that the Defense Contract Audit Agency (DCAA) "took no exception to the elements which comprised the ODC cost." However, DCAA did not take any exceptions as they were not tasked to evaluate the items for allowability or to offer an audit opinion. DCAA stated in its report that "The reported findings do not include an audit opinion."

On March 22, 2005, a DTRA contracting specialist requested that DCAA verify other direct costs to supporting documentation. However, DCAA could not verify approximately 50 percent of the proposed ODCs due to the lack of supporting documentation. DCAA Report No. 6161-2005B28000705, "Application of Agreed-Upon Procedures for Defense Enterprise Solutions (DES) Advisory and Assistance Services (A&AS) Proposal," May 5, 2005, stated that regarding other direct costs, "We verified the proposed other direct costs to the vendor quotes, actual accounting records. Due to some of the proposed other direct costs were not based on adequate supporting documentation, we were unable to verify the proposed costs and have noted differences in this report."

We also note that the ODCs include replacement of personal computers on a 3-year cycle at a proposed cost of $792,000. We do not consider it good management to use Government funds to replace the contractor's computers in the third year of a 4-year contract.

Had all 20 companies that expressed an interest in this contract been aware that they would have been directly reimbursed for all business start-up costs, a different competitive environment would have existed than the environment that resulted in one bid from the incumbent contractor. Considering that the incumbent contractor is a large, well-established major defense contractor, we consider it unconscionable that the contracting officer would include these ODCs in this contract.

**Acceptance of Profit Rates.** Profit or fee is the amount paid over and above allowable costs to a contractor for contract performance. Contracting officers usually use a structured approach such as the weighted guidelines method for developing a fee objective on any negotiated contract action. The weighted guidelines method focuses profit analysis on four factors: performance risk, contract type risk, facilities capital employed, and cost efficiency. However, a

structured method is not required for cost-plus-award-fee contract actions. In addition, competitive contracts do not require the contracting office to perform a profit analysis when the price is based on adequate competition.

The Combat Support and Technology Development task orders are cost-plus-award-fee contract actions and as such do not require a structured fee development. The negotiated award fee on both tasks is 11 percent with no base fee. The contracting officer does not justify the 11 percent fee other than stating that the Integrated Product Team process negotiated the fee down from the originally proposed amount of 12 percent. Considering that the performance risk of an A&AS contract is low, the contract type risk of a cost-plus contract is very low, and that the contractor is being directly reimbursed for all facility costs on this contract, we consider an 11 percent award fee abnormally high.

The CB and Combating WMD task orders are both cost-plus-fixed-fee contract actions and do require structured fee development. The negotiated fixed fee on both of these tasks is 8.5 percent of estimated labor costs. Using weighted guidelines, DTRA developed a fee objective of 8.0 percent. The fee objective was based on a 7.0 percent value for the performance risk profit factor that is considered a high value. That value was based on the contractor's good record of past performance as well as the high degree of integration and coordination required for the efforts. The final negotiated percentage for both task orders was agreed upon at 8.5 percent. To provide a higher performance risk value because of past performance is a correct use of weighted guidelines; however, the value given should have been a middle value given the generally low performance risk of A&AS contracts. In addition, as stated earlier, the contract type risk is very low and the contractor is being directly reimbursed for all facility costs. A 10 percent fee is the maximum allowed by law on this type of contract. We consider an 8.5 percent fee abnormally high.

We recognize that it is in the Government's best interest to offer contractors opportunities for financial rewards sufficient to stimulate efficient contract performance and to attract business concerns to Government contracts. We also recognize contracting officers must have discretion to be able to negotiate fee amounts on contracts. But when contract prices are negotiated after informing a contractor that it is the sole negotiator, all prices are suspect. On this contract, the contracting officer does not sufficiently justify the high profit rates that were negotiated in a noncompetitive environment.

**Determination of Fair and Reasonable Prices.** The contracting officer did not have a basis for his determination of price reasonableness. FAR Part 15, "Contracting by Negotiation," requires contracting officers to certify that the prices on each contract are fair and reasonable. On each of the first four task orders of this contract the contracting officer used the same wording on his certification paragraph:

> Based upon the results of the competitive solicitation and proposal and the resulting agreements of the Integrated Process Team (IPT's) and the corresponding evaluations by Government personnel, the undersigned Contracting Officer has determined the estimated cost and fixed fee is fair and reasonable.

On this contract, although many companies expressed interest, only one proposal was received and it came from the incumbent contractor. Without informing other prospective companies, contract prices and technical approaches were negotiated after numerous deficiencies were discovered in the initial proposal. The Integrated Process Team[3] was composed of Government officials and representatives of the sole offeror. The agreements made occurred after notifying the team that the selection board had been dissolved and there was only one offeror. Because of the circumstances of the award, we do not believe that there was an expectation that multiple proposals would be received or that agreements were made with the Integrated Process Team in a competitive environment.

Regarding corresponding evaluation by Government personnel, the technical evaluations of the first four task orders stated that two task orders needed more information and that the offeror did not understand the complexities and scope of the other two task orders. The DCAA report on this contract did not offer an audit opinion; it only verified costs and was unable to verify many of those costs because of a lack of documentation.

## FAR A&AS Contract Guidance

Although DTRA initially used competitive procedures to solicit RFPs, prior to award of the A&AS contract, DTRA notified the contractor that DTRA was entering into direct negotiations only with NGIT and proceeded to develop a revised final proposal in partnership with NGIT. Therefore, DTRA did not use full and open competition procedures to award this contract and these actions cast doubts on the value the Government is receiving from this contract. The proposed contract effort increased significantly after the Government informed the contractor that it was the sole offeror. However, there was no documentation of technical reviews of the revised final proposed tasks. The negotiation methods used cast doubt as to whether those tasks were efficiently designed or cost effective. The tasks on this contract should be recompeted in a competitive atmosphere as soon as possible.

In addition, the contracting officer did not conform to the intent of FAR guidance concerning A&AS contracts when developing the contract. FAR 16.504(c)(2) states that the Government prefers multiple-award contracts for A&AS if the contract is an indefinite-quantity contract that exceeds 3 years and $11.5 million including all options. If a multiple-award contract is not used, the contracting officer or other official designated by the head of the contracting activity must include the reason why in its acquisition planning documentation. The DTRA Acquisition Plan for Advisory and Assistance Services, July 23, 2004, states:

> Despite FAR's preference for multiple awards for A&AS, IDIQ contracts that exceed 3 years and $10 million, a single award was chosen because "Agency Integration and Synergy" was named as one of the key program objectives by DTRA senior leaders during

[3]DTRA contract documentation uses "Integrated Product Team" and "Integrated Process Team" interchangeably.

> acquisition planning. Because of DTRA's special mission to reduce the threat of weapons of mass destruction, many of the programs managed by the Agency are unique, highly technical, and interrelated. For these reasons, it is more practicable to have one contractor assisting senior leadership to promote coordination, cooperation, and communication between the directorates, so that tasks are not duplicated, resources are appropriately allocated, and programs are properly executed.

The DTRA Acquisition Plan does not provide an explanation of how a multiple-award contract would negatively affect "agency integration and synergy." The plan also does not explain why a single contractor can better handle the unique, highly technical, and interrelated tasks associated with reducing the WMD. The initial four A&AS tasks cover program management, scientific, medical, and military functions. Although the tasks may be interrelated, logic dictates more expertise could be found among several commercial entities than in a single Defense contractor. The contracted tasks are for advice and assistance to Government officials assigned the responsibility of safeguarding America's interests from WMD. For one company to provide such a multitude of A&AS tasks on a Defense contract of this magnitude raises additional questions as to whether all advice and assistance being provided on these complex inherently Governmental tasks are in the best interest of the Government. Competition among several companies would preclude those doubts. This is exactly the type of A&AS contract the FAR addresses when it provides a strong preference for multiple-award contracts.

# Conclusion

Contrary to FAR guidance, DTRA awarded a large A&AS single-source, IDIQ contract to its incumbent contractor, a contractor that has been supplying the same type of services to DTRA and its predecessors for a very long time. DTRA informed the incumbent contractor that it was the sole company negotiating and then proceeded to negotiate the technical approach and cost of the contract in what essentially was a sole-source environment. DTRA is reimbursing contractor expenses on a cost-plus basis including $10.2 million to procure dedicated facilities and $792,372 to obtain initial IT equipment and replace the equipment within a 3-year period. Considering that there is an entrenched DTRA A&AS contractor, competition on any single-source, IDIQ contract for those services will be difficult to obtain. However, a multiple-award, IDIQ contract will ensure that the most efficient and effective commercial organizations have a chance to compete for project management, scientific, medical, and military advice, and assistance tasks; and the resultant competition will ensure that the Government receives fair and reasonable prices. We substantiated six of the allegations (see Appendix B).

## Management Comments on the Finding and Audit Response

**Management Comments.** The Director, DTRA nonconcurred with the recommendations and requested the report not be issued, as DTRA officials complied with the FAR. The Director stated that the report lacked factual evidence and did not support the conclusions that DTRA violated any regulations. Further, negotiations led to lower labor rates and profit percentages than originally proposed, and the contract was in the best interest of the Government. The Director questioned the methodology used by the audit team stating that the auditors did not conduct interviews with the acquisition team and relied on contract file documentation. DTRA officials provided factual corrections to a "Discussion Draft" of the report.

**Audit Response.** Rather than lower labor rates through negotiations, DTRA officials worked with the incumbent contractor to develop tasks with labor hours and labor rates that bore little resemblance to those proposed on the contractor's initial proposal. This is discussed in more detail below. The methodology used for this audit was not unusual for an audit of specific Hotline allegations. The allegations we received contained support information that referred to specific documents that were required to be in the contract file. For some of the allegations, we were simply verifying that the documents we were given to support the allegations were, in fact, copies of the official documents contained in the contract file. The person who made the allegations was familiar with the solicitation, negotiations, and final contract awarded for advisory and assistance services to support DTRA. As stated in the report, we believe that the evidence obtained provides a reasonable basis for our findings and conclusions. We conducted this audit in accordance with generally accepted government audit standards.

**Management Comments.** The Director, DTRA nonconcurred with the finding that the revised final proposal was substantially different from the solicitation. The Director stated that the statement of objectives, contract ordering period, and period of performance were consistent for the original RFP and awarded contract. The number of labor hours for the task orders increased. However, DTRA officials negotiated lower labor rates and profit percentage. The Director states that as a result, the total cost decreased by 13.88 percent. Therefore, officials found it appropriate to award the contract based on the negotiations.

**Audit Response.** On an IDIQ contract, there is a basic contract that contains task orders with specifications agreed to under the basic contract. Each task order awarded under the basic contract contains a statement of work for the specific effort to be performed in accordance with the specifications of the task order. As explained in our report, the request for proposal associated with this contract requested contractors to provide technical and cost proposals in four areas expected to result in the award of four task orders concurrently with the award of the basic contract. The Director's contention that because the contract ordering period and contract period of performance of the basic contract did not change, the contract proposal did not change substantially is without merit because each task order did change. Reviews of individual task orders showed substantial changes in both labor hours and labor costs. For instance, the initial proposal for

the Combat Support task order contained 144,862 labor hours, or approximately 71 man-years of effort, at an average cost of $358.94 per hour while the revised final proposal contained 433,946 labor hours, or approximately 213 man-years of effort, at an average cost of $91.83 per hour. The DTRA comments suggest that the initial proposal was submitted in a competitive environment and therefore needs no further analysis to determine that the number of labor hours and cost submitted are the best value for the Government. Also the comments state that no further analysis of labor hours and cost per hour should be conducted on the revised final proposal to determine whether a fair and reasonable price was obtained for this effort because the cost of that effort is less than in the initial proposal, and that the final revised proposal represents considerable savings to the Government obtained through negotiation. Our view is that a change from 71 man-years of effort to 213 man-years of effort is so significant from the originally proposed task order that other contractors should have been provided another chance to bid on this effort and that there is no way to determine whether the revised final proposal was fairly and reasonably priced. Claimed savings are suspect because negotiation alone cannot explain how labor hours and labor cost can change so drastically. Finally, if the proposal had been re-competed, other contractors may have bid on the effort when it became obvious that the incumbent contractor did not understand the scope of the assistance and advisory services that were required by DTRA.

**Management Comments.** The Director, DTRA nonconcurred with the finding that officials informed the contractor it was the only company in negotiations and stated that the acquisition was a competitive solicitation. The original RFP allowed for discussions with offerors determined to be in the competitive range, so the officials' decision to enter into negotiations was consistent with the RFP. Officials violated no regulations. Negotiations occurred with the intent of receiving a revised proposal, as allowed by the FAR. The requirement did not change, only the level of effort changed.

**Audit Response.** As stated in our report, on May 20, 2005, the DTRA contracting office informed NGIT that "DTRA will enter into negotiations only with NGIT, via an Integrated Product Team." After informing the contractor that it was the only company in negotiations, DTRA and NGIT proceeded to develop task orders that had little resemblance to the task orders contained in the initial proposal. This level of revision is not standard negotiations as referred to in the FAR. The revised final proposal cannot be regarded as a document produced or received in a competitive environment.

**Management Comments.** The Director, DTRA nonconcurred with the finding that the competitive environment changed with the acceptance of ODCs. DTRA officials complied with FAR to determine ODCs were fair and reasonable. The RFP informed offerors of the requirement to assist DTRA officials within 30 minutes after requested and the responsibility of providing office space. The FAR allows rental and equipment costs and those costs may be charged as direct costs. The Director states charging such items as direct cost is the generally preferred method. Also, ODCs charge no fee; however, if the costs were indirect expenses, fees could be charged. Charging facility costs as ODCs is an accepted business practice. The DCAA Contract Audit Manual Part 7-303, June 29, 2007,

prefers identifiable costs be charged to the contract. Further, the ODC facility cost decreased by $2.1 million. DCAA took no exceptions to the proposed costs.

**Audit Response.** The conditions of this contract allowed NGIT to lease and furnish new office space to support DTRA A&AS. At Government expense, NGIT furnished its office spaces far better than most Government office spaces as allowed costs included dishwashers, microwave ovens, refrigerators, and other break room furniture. Curiously, DTRA management has commented on this allegation by quoting DCAA Contract Audit Manual Part 7-300, a section that addresses the cost of special facilities such as wind tunnels and space chambers. We are discussing fully funding a major contractor to lease and furnish new office space. The requirement in the solicitation for offerors "to maintain the ability to provide support to DTRA within 30 minutes after requests" in no way obligates the Government to fully fund the cost of a new office building and furnishings. Also, provisions such as RFP Provision H11 that states offerors will be responsible for providing office space in the performance of the contract are usually interpreted as meaning the offeror will not be directly reimbursed for the cost of the office space. The DTRA comments also state that DCAA took no exception to the proposed costs and their direct application to the proposal; however, as stated in our report, DCAA was not tasked to evaluate "other direct costs" for allowability and was unable to verify the cost of approximately 50 percent of proposed other direct costs because of missing documentation. The point of the allegation is not that DTRA cannot reimburse a contractor for all startup and operating costs; but that if the solicitation was clearer on this point, a much more competitive environment would have existed.

**Management Comments.** The Director, DTRA nonconcurred with the finding that the contractor received high profit rates. He stated that the contracting officer properly justified the negotiated profit rates. The report subjectively determined the rates were high and did not state what is high versus normal. The Director does not consider the contract for support in protecting America from WMDs to be a low risk venture. Further evidence of importance is that key DTRA officials coordinated the contract. The acquisition plan identified a moderate technical and schedule risk.

The original proposal contained a fixed fee of 10 percent. Using weighted guidelines, DTRA officials used 8 percent, based on a value of 7 percent for the technical and management risk factors. Though 7 percent represents the higher end of the standard range, it was based on the contractor's past performance and effort needed. DTRA officials negotiated an 8.5 percent fee, which excluded ODCs. The fee is significantly lower then the maximum 10 percent of the contract's estimated cost allowed under the FAR. The award fee was also within guidelines. The DoD FAR Supplement establishes a 3 percent limit on the base fee, with no limit on the amount of award fee. The FAR states the award fee is based upon judgment. The fee was 9.84 percent of total estimated costs, with the 11 percent referred to in the report based only on labor costs. The contracting officer justified the fees in the memorandum for the record cost review of task order 2. The memorandum for the record states the fee was developed according to guidelines, the fee was negotiated, and the original fee was proposed in a competitive environment. Also the fee is 9.84 percent when ODCs are included.

Task order 1 includes a similar analysis. Therefore, the Director states it was the contracting officer's judgment that the fee was acceptable.

**Audit Response.** We agree with the Director, DTRA that whether profit rates are high or low is a subjective determination. However, for the reasons outlined in our report, we stand by our determination that the profit rates for this A&AS contract are abnormally high. We also agree that protecting Americans from WMDs is a high risk venture; however, the A&AS contractor is not taking a high risk.

**Management Comments.** The Director, DTRA nonconcurred with the finding that officials certified that contract prices were fair and reasonable based on competitive contract award although the contract was not competitively awarded. He stated that DTRA followed the FAR for competitive solicitation, with the contracting officer determining the costs and fees as fair and reasonable, based on competitive solicitation and the revised proposal. The March 2005 FAR, in effect at the time, states that price is based on adequate price competition if there was a reasonable expectation of competition, even if only one bid was received. The Director stated that DTRA officials expected competition. To encourage competition, DTRA officials offered organizational conflict of interest provisions, so that potential contractors could still maintain eligibility as DTRA performers; requested contractors to comment on contracting methods and structures; and used contractor feedback to obtain recommendations on making the acquisition competitive.

The Director, DTRA stated that the report leads toward the conclusion that costs were not fair and reasonable. Information within the contract files leads to a more comprehensive analysis. The report states that labor hours increased 71 percent from the original proposal to the negotiated proposal, which implies DTRA officials did not negotiate a fair and reasonable price. However, labor costs consist of labor hours and labor rates. DTRA officials negotiated an additional 988,341 hours and a 13.88 percent decrease in labor costs from the initial proposal. Discussing only labor hours without the decrease in labor rates gives the impression that DTRA officials negotiated significant labor costs. The Director states that DTRA officials negotiated fair and reasonable documented task order costs.

**Audit Response.** The Director, DTRA contends that although the only proposal received was from NGIT, an incumbent contractor, there was an expectation of competition and therefore, the proposal was received in a competitive environment and all prices in the proposal can be considered fair and reasonable based on a competitive contract award. We contend that for all the reasons listed above and in the report, the revised final proposal upon which the contract award was based was so different from the initial proposal that DTRA cannot claim the revised final proposal was received in a competitive environment. In addition, the quality of the initial proposal was so deficient as evidenced by two task order technical evaluations stating "the offeror [NGIT] failed to understand the complexities and scope of the technical aspects of the CB [Chemical Biological] Non-Medical Program [and the CB Medical Program]" and labor prices that were up to three times higher than what was finally agreed upon that the initial proposal should not have been considered in a competitive range whether other

proposals were received or not. As stated earlier, the revised final proposal cannot be regarded as a document produced or received in a competitive environment.

## Recommendations, Management Comments, and Audit Response

**We recommend that the Director of the Defense Threat Reduction Agency:**

**1. Terminate contract HDTRA1-5-D-0003 at the end of the current option period in October 2007.**

**Management Comments.** The Director, Defense Threat Reduction Agency nonconcurred with the recommendation and stated that the Defense Threat Reduction Agency complied with the Federal Acquisition Regulation, statutes, and regulations in the award of the contract. Knowledgeable senior level personnel made the acquisition decisions. The report failed to: recognize Government benefits the Defense Threat Reduction Agency obtained; appreciate the intolerable consequences on the mission; and recognize the impractical time frames to execute a new competition.

**Audit Response.** Our review validated Hotline allegations that Defense Threat Reduction Agency contract HDTRA1-05-D-0003 was awarded based on a final revised proposal that was significantly different from requirements contained in the contract solicitation; that contracting officials did not provide for full and open competition through the use of competitive procedures contained in the Federal Acquisition Regulation for source selection; that the contracting officer certified that contract prices were fair and reasonable based on a competitive contract award although the contract was not competitively awarded; that the contracting officer did not negotiate fair and reasonable prices; that the contracting officer did not adequately evaluate contract "other direct costs" resulting in significant unnecessary costs to the Government; and that officials did not determine reasonable profit rates and awarded the contract with abnormally high profit rates. The most cost advantageous step for the Government that can be taken at this time is to terminate the contract at the end of the current option period as recommended. We request the Director, Defense Threat Reduction Agency reconsider his response and provide a plan by October 26, 2007, to terminate this contract.

**2. Compete a multiple-award, indefinite-delivery, indefinite-quantity contract for Defense Threat Reduction Agency advisory and assistance services in accordance with FAR 16.504.**

**Management Comments.** The Director, Defense Threat Reduction Agency nonconcurred with the recommendation and stated the Defense Threat Reduction Agency complied with Federal Acquisition Regulation 16.504 in determining that a single award contract was in the

best interest of the Government. Senior leaders within the Defense Threat Reduction Agency thoroughly reviewed the use of single-award versus multiple-award contracts and determined single-award was the best approach, which the Federal Acquisition Regulation allows. Officials at the Defense Threat Reduction Agency approved the document to support the decision and compliance with the Federal Acquisition Regulation. The Director stated that the report does not identify any procedures not followed.

The Defense Threat Reduction Agency followed Federal Acquisition Regulation guidelines. The Defense Threat Reduction Agency uses the advisory and assistance services contract for highly technical expertise on a continuous basis to support staff with mission demands. The Director stated that it would be impractical, and also would hurt the mission, to compete each task between multiple-award contracts.

**Audit Response.** In its contract documentation, the Defense Threat Reduction Agency officials conceded that the Federal Acquisition Regulation has a preference for multiple awards for advisory and assistance contracts. However, Defense Threat Reduction Agency officials have yet to present a cogent argument that the Defense Threat Reduction Agency and the Government are better served by a single-award indefinite-delivery, indefinite-quantity contract than by a multiple-award indefinite-delivery, indefinite-quantity contract. Defense Threat Reduction Agency officials stated that they complied with Federal Acquisition Regulation provisions because a paragraph (that is quoted verbatim in our report, page 11) was included in the Acquisition Plan that was approved by senior officials. However, this paragraph does not explain why the Defense Threat Reduction Agency will be better served by a single contractor reimbursed for all advisory and assistance tasks on a cost-plus basis than they would be by competing tasks among several responsible contractors.

Regulatory contractual procedures exist to ensure the Government receives goods and services at fair and reasonable prices. For this contract, Defense Threat Reduction Agency officials did issue a solicitation in a competitive environment. However, the Defense Threat Reduction Agency did not receive a responsive proposal from any contractor and cannot claim its advisory and assistance contract was awarded on a competitive basis. Rather than work on a new solicitation after receiving no responsive bids, Defense Threat Reduction Agency officials worked with its incumbent contractor to develop a contract that did not resemble the original solicitation, that was not competed, that reimbursed the contractor for unnecessary costs, that had abnormally high profit rates, and that did not contain verifiable fair and reasonable prices.

The procedures by which the revised final proposal was developed are not in compliance with the Federal Acquisition Regulation. The resultant contract should be terminated and a new competitive contract should be awarded. There are many companies capable of providing advisory and assistance services required by the Defense Threat Reduction Agency,

especially if tasks are for single areas of expertise such as chemical-biological medical support. We are confident that a multiple-award contract will convey to Defense Threat Reduction Agency officials all the advantages of a competitive business environment, while a single-award contract with a long-time support contractor will continue to raise questions of efficiency and fairness of costs. We request the Director, Defense Threat Reduction Agency to reconsider his response and provide a plan by October 26, 2007, to award a multiple-award contract for advisory and assistance services.

# Appendix A. Scope and Methodology

We conducted this performance audit from October 2006 through June 2007 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

This audit was a review of Defense Threat Reduction Agency (DTRA) contracting methods. We performed the audit in response to allegations to the Defense Hotline. As a result, we reviewed contract HDTRA1-05-D-0003 and the contract procedures.

Our audit included six major areas of review. Our review concentrated on the solicitation, competition, price reasonableness, other direct costs, profit, and funding of contract HDTRA1-05-D-003. Initial audit work was performed at DTRA. We reviewed documentation maintained by the contracting officials to support contract HDTRA1-05-D-0003. The documents reviewed included the basic contract, eight task orders, initial proposal, revised proposal, Defense Contract Audit Agency (DCAA) reviews, DTRA acquisition plans, Integrated Product Team Summaries, price negotiation memorandums, statements of objectives, technical evaluations, and other miscellaneous correspondence. Much of the information was obtained from copies of the contracting file received from DTRA. Information was also received from the Defense Hotline allegations.

**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 (GAO) has identified several high-risk areas in DoD. This report provides coverage of the "DoD Contract Management" high-risk area.

## Prior Coverage

During the last 5 years, the DoD Inspector General (IG) and DCAA have issued two reports discussing the Defense Threat Reduction Agency. Unrestricted DoD IG reports can be accessed at http://www.dodig.mil/audit/reports.

## DoD IG

DoD IG Report No. D-2004-111, "Cooperative Threat Reduction Contracts Awarded by the Defense Threat Reduction Agency in Support of the Cooperative Threat Reduction Program," August 25, 2004

# DCAA

DCAA Report No. 6161-2005B28000705, "Application of Agreed-Upon Procedures for Defense Enterprise Solutions (DES) Advisory and Assistance Services (A&AS) Proposal," May 5, 2005

# Appendix B. Allegations

The following seven allegations were made to the Defense Hotline concerning contracting methods of DTRA. The allegations were in regard to contract HDTRA1-05-D-0003.

- The final NGIT proposal that resulted in the contract award was significantly different from the DTRA requirements contained in the contract solicitation. A contract RFP containing the contract specifications that were awarded would likely have resulted in a competitive environment for contract award.

- The DTRA contracting officials did not provide for full and open competition through the use of competitive procedures contained in the FAR for source selection.

- The contracting officer certified that contract prices were fair and reasonable based on a competitive contract award although the contract was not competitively awarded.

- Negotiations for contract direct costs, other direct costs, and labor rates occurred during meetings of the Contract Integrated Product Team (a combination of NGIT and Government employees) after NGIT was aware that it was the only contractor submitting a proposal and that NGIT would be awarded the contract. Therefore the DTRA contracting officer did not negotiate fair and reasonable prices with NGIT.

- The contracting officer did not adequately evaluate contract "other direct costs" resulting in significant unnecessary costs to the Government such as the costs of procuring a dedicated building for NGIT contractors working on the DTRA effort.

- DTRA officials did not determine reasonable profit rates and awarded the contract with abnormally high profit rates considering the type of contract used and the risks involved in the contract effort.

- DTRA officials improperly co-mingled Operations and Maintenance and Research, Development, Test, and Evaluation appropriated funds on contract tasks.

We substantiated the first six allegations. We did not substantiate the allegation on improperly co-mingling Operations and Maintenance and Research, Development, Test, and Evaluation appropriated funds on contract tasks.

# Appendix C. Report Distribution

## Office of the Secretary of Defense

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

## Department of the Army

Auditor General, Department of the Army

## Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy

## Department of the Air Force

Auditor General, Department of the Air Force

## Other Defense Organizations

Director, Defense Contract Audit Agency
Director, Defense Threat Reduction Agency

## 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 Oversight and Government Reform
House Subcommittee on Government Management, Organization, and Procurement, Committee on Oversight and Government Reform
House Subcommittee on National Security and Foreign Affairs, Committee on Oversight and Government Reform

# Defense Threat Reduction Agency Comments

**Defense Threat Reduction Agency**
8725 John J. Kingman Road, MSC 6201
Fort Belvoir, VA 22060-6201

AUG 2 7 2007

MEMORANDUM FOR PROGRAM DIRECTOR, ACQUISITION AND CONTRACT MANAGEMENT, OFFICE OF THE DEPARTMENT OF DEFENSE INSPECTOR GENERAL

SUBJECT: DoDIG Draft Report on Hotline Allegations Concerning the Defense Threat Reduction Agency Advisory and Assistance Service Contract (Project No. D2006-D000CF-0262.000, Draft Report - July 13, 2007)

This Memorandum is the Defense Threat Reduction Agency (DTRA) response to your July 13, 2007, draft audit report and request for review and comment to the report findings and recommendations.

The following feedback is provided to the report findings and recommendations:

**a. DoDIG Draft Report Recommendation 1.** "Terminate contract HDTRA-5-D-0003 (sic) at the end of the current option period in October 2007."

**DTRA Response: Nonconcur**. The DoDIG draft report does not support this recommendation. DTRA complied with the Federal Acquisition Regulation (FAR) in the solicitation, evaluation, and award of the contract for Agency-wide advisory and assistance services (A&AS). The report contains no factual findings that support the allegation that DTRA violated any statute or regulation in the award of the contract. The report does not mention relevant portions of the official contract file documentation and facts provided to the audit team that substantiate DTRA's position. Acquisition decisions were made at the most senior levels within the Agency and were based on sound business and acquisition principles, knowledge, and experience with the DTRA mission and the complexities of this requirement. The report fails to recognize the Governmental benefits of DTRA's approach which include a reduction in contractor fees and facility costs from what was originally proposed and the fact that the Government received 988,341 additional hours of support for 13.88 percent less cost than the original proposal which was submitted in a competitive environment. The report fails to appreciate the intolerable consequences on DTRA's mission or the practicality of executing the timeframe of this recommendation.

**b. DoDIG Draft Report Recommendation 2.** "Compete a multiple-award, indefinite-delivery, indefinite-quantity contract for Defense Threat Reduction Agency advisory and assistance services in accordance with FAR 16.504."

**DTRA Response: Nonconcur**. DTRA complied with all provisions of the FAR 16.504(c)(2)(i)(a) in determining that a single-award indefinite-delivery, indefinite-quantity (IDIQ) contract was in the best interest of the Government. The official contract file contains substantial evidence that the single-award versus multiple-award issue was analyzed at numerous acquisition strategy meetings, both internal to the Government and with prospective offerors. A single-award was agreed to be the best approach for DTRA by several senior leaders throughout the Agency. In addition, DTRA benchmarked with other DoD agencies with similar missions and requirements to learn from their experience. The FAR clearly allows for the discretion to issue a single-award IDIQ contract as it specifies the procedures to document the decision. The required documentation to support the determination was approved at the appropriate level within the Agency and is in full compliance with the requirements of the FAR. The DoDIG report does not identify any provision or regulatory procedure that was not followed by the contracting officer and/or the senior designated official in making this determination.

DTRA consistently followed the FAR guidelines in accomplishing this acquisition. FAR 16.504(c)(1)(ii)(A)(4) states that the contracting officer should consider the ability to maintain competition among the awardees throughout the contract period of performance when determining if multiple-awards are appropriate. A&AS support at DTRA predominately entails providing highly technical expertise to support four distinct Enterprises and various Staff Offices. Each Enterprise and Staff Office utilizes A&AS support on a continuous basis to assist with numerous mission demands. The ability and flexibility to integrate this support is vital. It is impractical and would be a degradation of the execution of these missions to compete each distinct tasking or project among multiple-award contract holders.

I respectfully request in light of the information provided, that the DoDIG dismiss all findings and recommendations. DTRA complied with all FAR provisions for making and documenting the decision that a single-award IDIQ contract was in the best interests of the Government, and we will do the same with follow on contracts to determine if circumstances warrant multiple-award contracts. Please refer to the attached detailed response to every finding and statement contained in the draft report. If you require further assistance, please contact Mr. Kenneth Harsha at (703) 767-7890 or Ms. Shari Durand at (703) 767-7900.

James A. Tegnelia
Director

Attachment:
As stated

2

**Defense Threat Reduction Agency (DTRA) Response to DoDIG Draft Report**
**Project No. D2006-D000CF-0262.000**

DTRA nonconcurs in the recommendations in Draft Report Project No. D2006-D000CF-0262.000. The draft report does not support the conclusion that DTRA violated any statutes or regulations in award of the Agency-wide Advisory and Assistance Services (A&AS) contract. The draft report lacks factual evidence to support the claim that DTRA used flawed techniques that were in conflict with the Federal Acquisition Regulation (FAR). On the contrary, as a result of our negotiations, the task orders included lower labor rates per hour and a lower profit percentage than those originally proposed in response to the competitive solicitation. The reality is that entering into negotiations was indeed in the best interest of the government.

DTRA questions the methodology employed by the audit team based on the large number of discrepancies and factual errors in the draft report. The DoDIG team did not conduct any interviews with key members of the acquisition team; instead, it relied solely on a review of contract file documentation which the DoDIG team copied and took with them after an initial visit to DTRA. The audit team submitted their "Discussion Draft of a Proposed Report" on June 12, 2007 requesting DTRA respond to factual omissions. Subsequent to receiving DTRA's response, "DTRA Factual Corrections Discussion Draft of Proposed Report Project No. D2006-D000CF-0262" in which key omissions were highlighted and forwarded to the DoDIG Project Manager on June 27, 2007, the DoDIG team requested specific contract file documentation. For example, on July 5, 2007, the DoDIG requested file verification that NGIT proposed facility costs in its original proposal. Copies of the proposal, which documented that facility costs were indeed in NGIT's original proposal, were transmitted to the DoDIG on July 5, 2007. The DoDIG findings related to ODC facility costs are nevertheless still included in this draft report. While it was evident that the DoDIG team did not originally review the complete contract file, it appears that they still have not considered all relevant contract file documentation in this draft report.

Additional information is provided below to substantiate DTRA's position. These comments stem from the findings that were summarized on page 3 of the DoDIG Draft Report.

**Finding**

- Based the contract award on a revised final proposal developed by the contractor with DTRA assistance that was substantially different than requirements contained in the contract solicitation.

**DTRA nonconcurs with the above finding.**

**DTRA Response**: DTRA issued a Request for Proposal (RFP) for A&AS with a 5 year ordering period and a ceiling amount of $375 million. The resultant contract award was executed for the aforementioned services with the identical Statement of Objectives (SOO) issued with the RFP. The contract ordering period and contract period of performance were consistent between the original RFP and the resultant contract. While

the level of effort to meet the task order SOOs and task order requirements were revised during Integrated Product Team (IPT) negotiations, the requirements of the contract did not change. DTRA negotiated a change to the level of effort required to meet the mission requirements, but the requirement itself did not change. As a result of the IPT negotiations, the awarded task orders included lower labor rates per hour and a lower profit percentage than that originally proposed in response to the competitive solicitation. Specifically, the Government was able to increase the labor hours for this effort and decrease the labor rate by 48.75 percent, thereby decreasing the labor costs by 12.49 percent. As a result, the total acquisition cost was decreased by 13.88 percent. Therefore, it is both appropriate and reasonable that DTRA would award a contract based upon a final proposal developed as a result of negotiations.

**Finding**

- Negotiated contract prices and terms using the final revised proposal after informing the contractor that it was the only company in negotiations with DTRA.

**DTRA nonconcurs with the above finding.**

**DTRA Response**: The A&AS acquisition was solicited as a competitive acquisition according to FAR 15.002(b). Although only one proposal was received, it was submitted in a competitive environment. DTRA conducted the evaluation, negotiation and award of the contract in a competitive environment. Section M2.9 of the original RFP instructed offerors to "submit its best proposal as the opportunity to submit a revised proposal is not anticipated." However, Section M2.9 also notified offerors that "if during the evaluation period it is determined to be in the best of the Government to hold discussions, these discussions will be held with only those offerors determined by the Contracting Officer to be in the competitive range." DTRA's decision to enter into negotiations with the only offeror (therefore the only offeror within the competitive range) was consistent with the intent of the RFP. Neither the FAR, nor the RFP, were violated by DTRA's decision to enter into negotiations with the only offeror in the competitive range and by the utilization of the IPT process.

Negotiations were undertaken with the intent of allowing the offeror to revise its proposal as is standard practice and supported by the FAR. Throughout these discussions, DTRA's requirement (Agency A&AS support for a period of 5 years) did not change. DTRA negotiated a change to the level of effort required to meet the mission requirements. As a result of the IPT negotiations, the awarded task orders included lower labor rates per hour and a lower profit percentage than that originally proposed in response to the competitive solicitation. Specifically, the Government was able to increase the labor hours for this effort and decrease the average labor rate by 48.75 percent, thereby, decreasing the labor costs by 12.49 percent. As a result, the total acquisition cost was decreased by 13.88 percent.

**Finding**

- Accepted "other direct costs" in the revised final proposal that would have changed the competitive environment if those requirements had been included in the initial RFP.

**DTRA nonconcurs with the above finding.**

**DTRA Response**: DTRA complied with the regulations by requesting and using field pricing support according to FAR 15.404-2 and conducting cost and price analysis according to FAR 15.404-1 to determine that the contract costs, and specifically the other direct costs (ODCs), were fair and reasonable.

Section L10.3.2 of the RFP instructed all offerors to include in their cost proposals "estimates of all non-labor costs that will be required." Section M2.7 of the RFP informed the offerors of the requirement to maintain the ability to provide support to DTRA within 30 minutes after requests during business hours. In addition, RFP provision H11, "Government-Provided Office Space," stated that the offerors would be responsible for providing office space in the performance of the contract, unless otherwise specified in individual task orders. Therefore, offerors were on notice that the cost of providing nearby office facilities to satisfy the contract requirements would be an allowable cost under the contract.

The costs associated with the accomplishment of the Government's requirement for A&AS support, such as facility rental costs and purchase of necessary equipment such as information technology (IT) equipment, according to FAR 31.205-36, are allowable costs and may be charged as a direct cost to the contract consistent with the contract requirements and contractor's accounting practices. It is entirely acceptable and in many cases preferable for such costs to be treated as direct cost to the contract. In fact, this method is generally preferred as it is more accurate and equitable than attempting to distribute the costs through various indirect expense categories. Additionally, these ODCs are not fee bearing. If the contractor proposed these costs as an indirect expense, as the IG report recommends, the contractor would have been entitled to add fees to the overhead costs. Although the DoDIG considers it is "unconscionable" for the contracting officer to reimburse a large, well established major defense contractor for facility costs as ODCs, it is an acceptable, even preferred, method of accounting for all businesses large or small. The DCAA Contract Audit Manual Part 7-303, June 29, 2007, describes the three basic methods for allocating facility costs. The three methods are full costing on usage basis; only directly identifiable costs allocated on usage basis, and general indirect cost allocation. Under the full costing on usage basis; all readily identifiable direct costs are charged to projects, contracts or other work involved. Per the Manual, generally this

method yields the most equitable results and should be used if cost and usage data for the facility can be economically accumulated with reasonable accuracy.

Further, DTRA did not accept any ODCs in the revised final proposal from the successful offeror that were not included in the offeror's original proposal. The ODCs as originally proposed included a total ODC facility cost of $12.3 million of which $7.4 million was rent. The final negotiated amounts included a total ODC facility cost of $10.2M of which $7.2M was rent. This constituted a reduction of $2.1M. In addition to the aforementioned facility costs, the other significant ODCs were related to telecommunications and travel costs. The program office considered these costs reasonable and realistic for the services to be performed. DCAA's review of the ODCs took no exception to the proposed costs and their direct application to the proposal.

**Finding**

- Accepted abnormally high profit rates on the revised cost proposal.

**DTRA nonconcurs with the above finding.**

**DTRA Response**: The Contracting Officer properly justified the profit ratios that were negotiated on the task orders. Exception is taken to the categorization of this profit ratio as high as it is a subjective determination lacking substantiation as to what constitutes high versus normal ratios. The contract provides A&AS support services for Government officials assigned the responsibility of safeguarding America's interest from weapons of mass destruction. Based on the magnitude of this mission and current threats, we do not consider this a low risk venture particularly considering the potential consequence of failure. The A&AS contractor supports critical Agency missions and is expected to provide top level capabilities and often upon short fuse notice. The importance of this program to the Agency is evidenced by the fact that it was coordinated with the Head of the Contracting Activity (HCA), the Component Acquisition Executive (CAE), and the Associate Directors of all the Agency's Enterprises and key Staff Offices. As a result, the Acquisition Plan for this requirement identified a moderate technical and schedule risk "attributable to the contractor's ability to recruit and retain appropriate expertise at a reasonable cost."

Regarding the profit ratios, DTRA did not accept abnormally high profit ratios. In the original proposal the contractor proposed a fixed fee of 10 percent for the task orders designated as Cost Plus Fixed Fee (CPFF) orders. Through the use of the weighted guidelines which were included in the contract file, the Agency developed a fee objective of 8.0 percent. This was based upon providing a value of 7 percent for the Technical and Management Risk Factors. This 7 percent represents the higher end of the standard value range and was justified based upon the contractor's record of past performance as well as the high degree of integration and coordination required for the effort. The final fee percentage was agreed upon at 8.5 percent. However, it should be noted that the fixed

fee amount is based upon the application of the 8.5 percent to labor costs only and excludes ODCs. Therefore, when ODCs are considered, the fee rate of return is 7.47 percent. This is significantly below the fee limitation prescribed in FAR 15.404(c)(4)(i)(C): "For other cost-plus-fixed fee contracts, the fee shall not exceed 10 percent of the contract's estimated cost." Even if the ODCs are not considered, the negotiated fee was still within the acceptable range established in the FAR.

The negotiated rate for the award fee task orders is also within regulatory guidelines. DFARS 216-405-2(c)(2)(B) establishes a 3 percent limit on the amount of base fee that may be negotiated but does not establish a limit on the amount of award fee. Instead, FAR 16.305 (b) highlights that the award fee amount is "based upon a judgmental evaluation by the Government, sufficient to provide motivation for excellence in contract performance…" The negotiated fee rate for the award fee task orders equates to 9.84 percent of total estimated costs. The 11 percent rate referred to in the DoDIG audit report is based upon the application of the rate to only the labor costs. The Contracting Officer provided justification for this rate and did not merely state that the IPT negotiated the fee down from 12 percent. The Contracting Officer, in his Memorandum for Record (MFR), Cost Review of Task Order 2 stated the following:

> "This fee was developed according to the provisions of FAR 16.405-2 and DFARS 215.404-74. Under the competitively awarded contract (DTRA01-00-C-0088) the fee structure allows for an award fee of 7 percent of estimated cost and a fixed fee based on 3 percent of the estimated cost for a total maximum fee rate of return of 10 percent. For the current task order Northrop Grumman Information Technology (NGIT) originally proposed an award fee based upon 12 percent of the estimated cost with no base fee. Through the IPT an award fee based upon 11 percent of estimated cost was agreed upon. While the 11 percent is greater than the 10 percent maximum available under the 2000 contract, it does take into account the greater risk assumed by NGIT in not receiving a base fee. It should further be noted that the initial 12 percent fee was proposed in a competitive environment. It should also be noted that the award fee amount is based upon the application of the 11 percent to labor costs only and excludes ODCs. Therefore, when ODCs are considered, the fee rate of return is 9.84 percent. Similar language was included in the MFR, Cost Review for Task Order 1. Thus, it is the Contracting Officer's judgment that the fee amount negotiated is consistent with the FAR 16.405-2(a)(2) requirement that the award fee amount be "sufficient to provide motivation for excellence in such areas as quality timeliness, technical ingenuity, and cost-effective management."

**Finding**

- Certified that contract prices were fair and reasonable based on a competitive contract award although the contract was not competitively awarded.

**DTRA nonconcurs with the above finding.**

**DTRA Response**: DTRA's requirement for A&AS services was solicited in a full and open fashion as required by FAR 6.1 and evaluated and awarded according to FAR Part 15. The only specific reference to a "conflict" with the FAR is that the Contracting Officer violated the "intent" of the FAR, not the actual FAR provision.

The Contracting Officer determined the estimated cost and fees for the subject task orders to be fair and reasonable based upon the proposal submitted in response to the competitive solicitation, the offeror's revised proposals resulting from the Integrated Process Team (IPT) negotiations, and the corresponding evaluations by Government personnel.

The March 2005 version of FAR 15.403-1(c)(1)(ii), which was in effect at the time of this procurement, states that a price is based on adequate price competition if:

> "(ii) There was a reasonable expectation, based on market research or other assessment, that two or more responsible offerors, competing independently, would submit priced offers in response to the solicitation's expressed requirement, *even though only one offer is received from a responsible offeror and if* –
>
> (A) Based on the offer received, the contracting officer can reasonably conclude that the offer was submitted with the expectation of competition, e.g., circumstances indicate that --
>
> (1) The offeror believed that at least one other offeror was capable of submitting a meaningful offer; and
>
> (2) The offeror had no reason to believe that other potential offerors did not intend to submit an offer; and
>
> (B) The determination that the proposed price is based on adequate price competition, is reasonable, and is approved at a level above the contracting officer;"

In this instance, DTRA's market research led to the expectation that two or more offerors would submit proposals. In addition, given the participation of 55 contractors at Industry Day, it was reasonable to conclude that the offeror submitted its proposal with the expectation of competition. The Component Acquisition Executive's Source Selection Decision Document indicates concurrence that the offer was submitted with the expectation of competition. As previously noted, even after the source selection was dissolved and negotiations were conducted, the Government benefited from reduced labor rates.

To encourage competition, DTRA took specific actions including:

(1) Providing maximum flexibility in the RFP's Organizational Conflict of Interest (OCI) provisions. OCI issues were raised as an area of concern from some of DTRA's "performers"; to encourage competition, DTRA invited the potential offerors to propose an OCI Mitigation Plan that we would then evaluate. This provided an opportunity for offerors who may previously have chosen not to compete for the DTRA A&AS contract to propose in response to the RFP and potentially be awarded the contract while still maintaining their eligibility as DTRA performers. This was done specifically to expand the potential field of competition.

(2) Specifically requested potential offerors to comment on preferred contracting methods and structures, i.e. multiple award, scope of contract (i.e., Agency-Wide, by Directorate, by Function), number of performers and type of contract.

(3) Utilized draft RFP and requested comments from industry to solicit recommendations to make this acquisition as competitive as possible..

The information provided in the report appears to be skewed toward the ultimate conclusion that the negotiated costs were not fair and reasonable. The review of additional information available in the official contract file provides a more comprehensive analysis. For example, the table on page 8 of the report highlights the percent increase (71 percent) of proposed hours from the initial proposal to the final revised proposal. The report implies that this contributed to the determination that DTRA did not negotiate a fair and reasonable price. However, labor costs are the result of the combination of labor hours and labor rate. Therefore, the total labor costs cannot be determined fair and reasonable without a corresponding discussion of the labor rates. The ultimate result of negotiations was that DTRA received an additional 988,341 hours from the initial proposal while it negotiated a 13.88 percent reduction in total labor cost from the initial proposal. In more simple terms, the Agency was able to acquire more resources at a reduced cost as a result of the negotiation process. Focusing on the increase in labor hours alone, without a corresponding discussion of the decrease in labor rates and costs, gives an erroneous impression that DTRA accepted a significant labor cost increase in the final revised proposal. In actuality, DTRA negotiated fair and reasonable task order costs as documented in the MFR, Cost Review for each of the task orders.

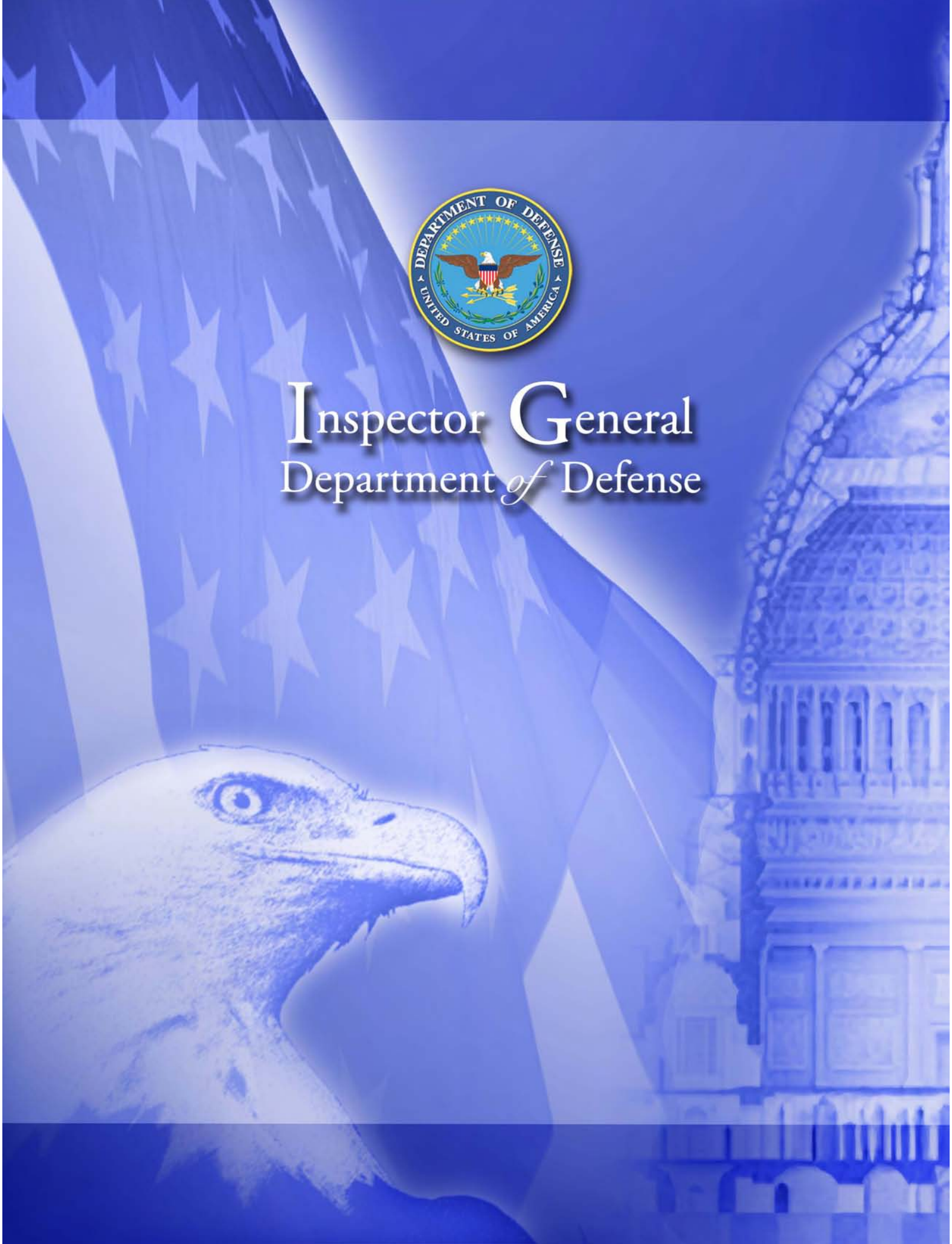
**Conclusion**

DTRA complied with the Federal Acquisition Regulation and the Department of Defense Federal Acquisition Supplement in the solicitation, evaluation and award of the contract for Agency-wide Advisory and Assistance Services (A&AS). The DoDIG draft report contains no factual findings to the contrary.

# Team Members

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

Richard B. Jolliffe
Terry L. McKinney
Timothy E. Moore
Christine M. McIsaac
Karen A. Ulatwoski
Bethany M. Thomas
Meredith H. Johnson




# Inspector General
## Department of Defense