



INSPECTOR GENERAL

U.S. Department of Defense

NOVEMBER 22, 2013



Missile Defense Agency and Defense Microelectronics Activity Use of Cost-Reimbursement Contracts



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Results in Brief

Missile Defense Agency and Defense Microelectronics Activity Use of Cost-Reimbursement Contracts

November 22, 2013

Objective

We are required to perform this audit in accordance with the FY 2009 National Defense Authorization Act, section 864, "Regulations on the Use of Cost Reimbursement Contracts." Our objective was to determine whether the Missile Defense Agency (MDA) and the Defense Microelectronics Activity (DMEA) complied with interim Federal Acquisition Regulation revisions on the use of cost-reimbursement contracts by documenting:

- that approval for the cost-reimbursement contract was at least one level above the contracting officer;
- that cost-reimbursement contracts were justified;
- how the requirements under the contract could transition to firm-fixed-price in the future;
- that Government resources were available to monitor the cost-reimbursement contract; and
- that contractors had an adequate accounting system in place at contract award.

This is the third in a planned series of audit reports on DoD compliance with the interim rule for the use of cost-reimbursement contracts.

Finding

Of the 88 contracts reviewed, valued at about \$1.66 billion, MDA and DMEA contracting personnel did not consistently implement the interim rule for 72 contracts, valued at about \$528 million. Contracting personnel issued contracts that did not follow the interim rule because of different interpretations of the interim rule requirements. As a result, MDA and DMEA contracting personnel continue to issue cost-reimbursement contracts that may inappropriately increase DoD's contracting risks because cost reimbursement contracts provide less incentive for contractors to control costs.

Recommendations

We recommend that the Director of Contracting, MDA:

- Emphasize the importance of the Federal Acquisition Regulation revisions to contracting personnel for the use of cost-reimbursement contracts.

We recommend that the Chief, Contracting Division, DMEA:

- Develop procedures that ensure a senior official approves all cost-reimbursement contracts one level above the contracting officer.
- Emphasize the importance of the Federal Acquisition Regulation revisions through guidance to contracting personnel for the use of cost-reimbursement contracts.
- Provide guidance to contracting personnel that the nature of DMEA's contracts and the inability to transition to a firm-fixed-price contract needs to be documented in the contract file of cost-reimbursement contracts.



Results in Brief (cont'd)

Missile Defense Agency and Defense Microelectronics Activity Use of Cost-Reimbursement Contracts

Management Comments

The Director, Missile Defense Agency, agreed with our recommendation and will emphasize the importance of the revisions to contracting personnel. MDA contracting personnel have updated their checklists to reflect the revisions. The Chief, Contracting Division, Defense Microelectronics Activity, agreed and immediately established procedures to ensure that a senior official

is always available to approve all cost-reimbursement contracts one level above the contracting officer. According to the Chief's comments, DMEA has provided additional training to contracting personnel regarding the requirements of the interim rule. We consider these comments responsive. Please see the recommendations table on the next page.

Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
Director of Contracting, Missile Defense Agency		1
Chief, Contracting Division, Defense Microelectronics Activity		2.a., 2.b., and 2.c.



**INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
4800 MARK CENTER DRIVE
ALEXANDRIA, VIRGINIA 22350-1500**

November 22, 2013

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION, TECHNOLOGY,
AND LOGISTICS

DIRECTOR, MISSILE DEFENSE AGENCY
DIRECTOR, DEFENSE MICROELECTRONICS ACTIVITY

SUBJECT: Missile Defense Agency and Defense Microelectronics Activity Use of
Cost-Reimbursement Contracts (Report No. DODIG-2014-011)

We are providing this report for information and use. Of the 88 contracts reviewed, valued at about \$1.66 billion, contracting personnel did not consistently implement the Federal Acquisition Regulation revisions for the use of cost-reimbursement contracts for 72 contracts, valued at about \$528 million. We are required to perform this audit in accordance with the FY 2009 National Defense Authorization Act, section 864, "Regulation on the Use of Cost Reimbursement Contracts." This is the third in a series of audit reports on DoD compliance with the interim rule for the use of cost reimbursement contracts.

We considered management comments on a draft of this report when preparing the final report. Comments from the Director, Missile Defense Agency, and the Chief, Contracting Division, Defense Microelectronics Activity, conformed to the requirements of DoD Directive 7650.3; therefore, additional comments are not required.

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 604-9077 (DSN 664-9077).

Jacqueline L. Wicecarver
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Assistant Inspector General
Acquisition, Parts, and Inventory

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Acronyms and Abbreviations

Introduction

Objective

Our objective was to determine whether Missile Defense Agency (MDA) and Defense Microelectronics Activity (DMEA) contracting personnel complied with interim Federal Acquisition Regulation (FAR) revisions regarding the use of cost-reimbursement¹ contracts. Specifically, we determined whether MDA and DMEA contracting personnel implemented the interim rule by documenting:

- that approval for the cost-reimbursement contract was at least one level above the contracting officer,
- that the use of cost-reimbursement contracts was justified,
- how the requirements under the contract could transition to firm-fixed-price in the future,
- that Government resources were available to monitor the cost-reimbursement contract, and
- that contractors had an adequate accounting system in place at contract award.

We also determined whether MDA and DMEA personnel intentionally misclassified contracts as firm-fixed-price to avoid the increased cost-reimbursement contract documentation requirements.

In addition to this report, we are issuing separate reports for each of the Services, as well as a summary report. This is the third report in the planned series of reports and includes contracts issued by MDA and DMEA. The first report of the series, “Air Force Needs Better Processes to Appropriately Justify and Manage Cost-Reimbursable Contracts” (Report No. DODIG-2013-059), was issued on March 21, 2013. The second report of the series, “Army Compliance with FAR Revisions Regarding the use of Cost-Reimbursement Contracts” (Report No. DODIG-2013-120), was issued on August 23, 2013. See Appendix A for the scope and methodology and prior coverage related to the objective.

¹ We use “cost reimbursement” to describe any type of contract other than firm-fixed-price contracts throughout the report, such as labor hour and time and materials contracts.

Background

Section 864 of the FY 2009 National Defense Authorization Act requires FAR revisions regarding the documentation of decisions and approvals necessary before issuance of other than firm-fixed-price contracts and the DoD Inspector General to audit DoD's compliance with the changes within 1 year of policy issuance. Federal Acquisition Circular (FAC) 2005-50, issued March 16, 2011, implemented the required revisions on an interim basis. This interim rule was effective immediately and was not subject to public comment before issuance. FAC 2005-50 amended FAR Part 7, "Acquisition Planning," FAR Part 16, "Types of Contracts," and FAR Part 42, "Contract Administration and Audit Services." The final rule was published in the Federal Register on March 2, 2012, without significant changes that would affect our audit objective. To promote savings in Federal contracting, the final rule stated that contracting personnel should choose the appropriate contract type. See Appendix B for a copy of the interim rule, FAC 2005-50, issued March 16, 2011.

Interim Rule Requirements and Our Interpretation

We divided our objective into five areas based on the interim rule. We interpreted parts of the interim rule for each of these areas to determine what we would accept as adequate documentation in the contract file. Contracting personnel were required by the interim rule to include the approval, justification, and transition areas in the acquisition planning documentation. For each of these areas, we accepted documentation anywhere in the contract file because some of the Acquisition Plans were completed before the interim rule. Contracting personnel were not required by the interim rule to document that adequate resources and an adequate accounting system were available specifically within the acquisition planning documentation.

Approval

Contracting personnel were required by the interim rule to obtain approval of a cost-reimbursement contract at least one level above the contracting officer. FAC 2005-50 states, "[t]he contracting officer shall document the rationale for selecting the contract type in the written Acquisition Plan and ensure that the plan is approved and signed at least one level above the contracting officer." Contracting personnel were required by the interim rule to document this approval in the Acquisition Plan. We accepted any documentation in the contracting files

that stated the contract type was cost reimbursement and was reviewed and signed by a senior official above the contracting officer as evidence of having met the interim rule requirement.

Justification

Contracting personnel were required by the interim rule to justify the use of a cost-reimbursement contract. FAC 2005-50 states:

[a]cquisition personnel shall document the acquisition plan with findings that detail the particular facts and circumstances, (e.g., complexity of the requirements, uncertain duration of the work, contractor's technical capability and financial responsibility, or adequacy of the contractor's accounting system), and associated reasoning essential to support the contract type selection. . . .

Contracting personnel were required by the interim rule to document the justification in the Acquisition Plan. We determined that contracting personnel followed the interim rule by completing a Determination and Finding memorandum on contract type for inclusion in the contract file or included a discussion of research and development efforts with results that cannot be precisely described in advance.

Transition

Contracting personnel were required by the interim rule to document the potential of cost-reimbursement contracts to transition to firm-fixed-price contracts. FAC 2005-50 states:

For each contract (and order) contemplated, discuss the strategy to transition to firm-fixed-price contracts to the maximum extent practicable. During the requirements development stage, consider structuring the contract requirements, e.g., contract line items (CLINS), in a manner that will permit some, if not all, of the requirements to be awarded on a firm-fixed-price basis, either in the current contract, future option years, or follow-on contracts.

We interpreted this section of the interim rule to require an explanation of the potential to transition to a firm-fixed-price contract or a justification as to why the particular effort will never be able to transition to a firm-fixed-price contract. Contracting personnel were required by the interim rule to document this strategy in the Acquisition Plan. In addition to areas where contracting personnel documented that future work will transition to firm-fixed-price, we determined that contracting personnel were following the interim rule if they issued contracts

that had both firm-fixed-price and cost-reimbursement contract line item numbers along with a statement in the contract file that allowed the firm-fixed-price contract line item numbers to be used when the requirements became appropriate for a firm-fixed-price contract. We also determined that contracts noting that the award will not be able to transition to a firm-fixed-price contract for various reasons met the intent of the interim rule.

Adequate Resources

Contracting personnel were required by the interim rule to document that adequate resources are available to manage a cost-reimbursement contract. FAC 2005-50 states:

A cost-reimbursement contract may be used only when—Adequate Government resources are available to award and manage a contract other than firm-fixed-priced (see 7.104(e)) including— (i) Designation of at least one contracting officer’s representative (COR) qualified in accordance with 1.602-2 has been made prior to award of the contract or order.

We interpreted this section of the interim rule to require, at a minimum, evidence of the assignment of an appropriate contracting officer’s representative (COR) or similarly qualified individual to the contract. We obtained the COR nomination letter, signed acceptance by the COR, and COR training documents. Contracting personnel were not required by the interim rule to document this evidence in any specific location of the contract file. We recognized that assigning a COR to the contract does not always indicate that adequate Government resources are available to monitor the contract as required by the interim rule. For purposes of our objective, however, we identified the assignment of a COR on the contracts and did not test the adequacy of the CORs assigned.

Adequate Accounting System

Contracting personnel were required by the interim rule to determine the adequacy of the contractor’s accounting system during the entire period of performance for cost-reimbursement contracts. FAC 2005-50 states, “Determine the adequacy of the contractor’s accounting system. The contractor’s accounting system should be adequate during the entire period of contract performance.” We interpreted this section of the interim rule to require documentation that the contracting officer concluded the accounting system was adequate. At a minimum, we required a statement in the file that the accounting system was adequate based on information from the Defense Contract Audit Agency, the Defense Contract Management Agency, or similar entities responsible for monitoring the contractor. We also accepted the contracting

officer's documented conclusion and e-mails from the Defense Contract Audit Agency and the Defense Contract Management Agency personnel as adequate documentation. We focused our audit on identifying whether the contracting officer determined that the accounting system was adequate at contract award, rather than during the entire period of performance, as required by the interim rule.

Contracts Reviewed

Our Federal Procurement Data System–Next Generation queries identified 971 cost-reimbursement, labor-hour, or time-and-materials contract actions issued by Defense agencies and activities from March 17, 2011 through February 29, 2012, valued at about \$13.9 billion; this includes the value of all potential options and any firm-fixed-price portions of the contracts. To meet DoD Inspector General's audit requirement in Section 864 of the FY 2009 National Defense Authorization Act, we determined that we would review one Defense agency and one Defense activity. We selected MDA and DMEA based on a combination of cost-reimbursement award amounts and number of cost-reimbursement contracts issued. MDA and DMEA were responsible for 291 of the 971 contracts issued by DoD agencies and activities during this time period. We reviewed 88 contracts, with cost-reimbursement portions, valued at about \$1.66 billion; 2 of the 88 contracts accounted for about \$932 million of this amount. Table 1 shows the number of basic contracts, the task or delivery orders reviewed, and the contract value at each site.

Table 1. Contracts Reviewed

Site	Basic Contracts	Task/Delivery Order	Total	Contract Value
MDA	25	14	39	\$1,256,385,631
DMEA	2	47	49	407,901,590
Total	27	61	88	\$1,664,287,221

The Small Business Innovation Research Program

The Small Business Innovation Research (SBIR) program is a three-phase program that encourages domestic small businesses to engage in Federal research and development with the potential for commercialization. The SBIR program was established under the Small Business Innovation Development Act of 1982 to increase small business opportunity in federally funded research and development, stimulate high-tech innovation, and increase private-sector commercialization. The U.S. Small Business Administration serves as the coordinating agency. Phase I of the program is designed for exploration of the technical merit or feasibility of

an idea or technology. A firm-fixed-price contract is almost always used for this phase. Phase II, typically a cost-plus-fixed-fee contract, consists of the research and development work, in which the developer also evaluates commercialization potential. During Phase III, the developer moves toward commercialization of the innovation. SBIR program funds cannot be used for Phase III. We did not target or avoid SBIR contracts as part of our nonstatistical sample because the interim rule does not include an exception for SBIR contracts.

The SBIR Desk Reference for Contracting and Payment states that, according to FAR Subpart 16.3, “Cost-Reimbursement Contracts,” a cost-reimbursement contract may be used only when the contractor’s accounting system is adequate for determining costs applicable to the contract and requires Government surveillance during the performance of the contract.

Review of Internal Controls

DoD Instruction 5010.40, “Managers’ Internal Control Program Procedures,” May 30, 2013, requires DoD organizations to implement a comprehensive system of internal controls that provides reasonable assurance that programs are operating as intended and to evaluate the effectiveness of the controls. We identified internal control weaknesses for implementing the changes required by the interim rule regarding the use of cost-reimbursement contracts. MDA and DMEA did not update local procedures or other guidance for issuing and administering cost-reimbursement contracts. Specifically, DMEA did not have procedures in place to justify the use of cost-reimbursement contracts. MDA and DMEA did not have procedures to approve the use of cost-reimbursement contracts and did not always document the potential of cost-reimbursement contracts to transition to firm-fixed-price contracts. Additionally, MDA and DMEA contracting personnel did not always verify the adequacy of the contractor’s accounting system as required by the interim rule. We will provide a copy of the report to the senior official in charge of internal controls in the Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics and in MDA and DMEA.

Finding

MDA and DMEA Inconsistently Implemented the Interim Rule

Of the 88 contracts reviewed, valued at about \$1.66 billion, MDA and DMEA contracting personnel did not consistently implement the interim rule for 72 contracts, valued at about \$528 million. MDA and DMEA contracting personnel fully met the interim rule on 16 contracts,² valued at about \$1.14 billion, of the 88 contracts.

Specifically, contracting personnel did not:

- obtain approval for the use of a cost-reimbursement contract for 19 contracts, valued at about \$74.9 million, at MDA, and 31 contracts, valued at about \$192.3 million, at DMEA;
- justify the use of a cost-reimbursement contract for 10 contracts, valued at about \$3.6 million, at DMEA;
- document the possibility of a transition to a firm-fixed-price contract for 2 contracts, valued at about \$43.6 million, at MDA, and 48 contracts, valued at about \$403 million, at DMEA;
- ensure adequate Government resources were available for 1 contract, valued at about \$.5 million, at DMEA; and
- verify the adequacy of the contractor's accounting system for 7 contracts, valued at about \$18.4 million, at MDA, and 20 contracts, valued at about \$115 million, at DMEA.

MDA and DMEA contracting personnel generally stated they issued contracts that did not meet the interim rule because of different interpretations of the interim rule's requirements.

As a result, MDA and DMEA contracting personnel continue to issue cost-reimbursement contracts that may inappropriately increase DoD's contracting risks because cost-reimbursement contracts provide less incentive for contractors to control costs.

² Contracting personnel at MDA issued 15 of the 16 fully compliant contracts.

More Consistent Documentation Procedures Needed to Fully Implement Federal Acquisition Regulation Revisions

MDA and DMEA contracting officers fully implemented FAR revisions on 16 of the 88 contracts valued at about \$1.14 billion. MDA contracting officials issued 15 of

the 16 fully compliant contracts. Contracting officials

implemented portions of the interim rule for the

other 72 contracts valued at about \$528 million,

but they did not consistently include

documentation in the contract files to meet the

interim rule. Contracting officials described

their contracting procedures and explained their

interpretation of the interim rule at each site

visited. When contracting officers documented

the elements of the interim rule, the elements

were in the signed Acquisition Plan, Price Negotiation

Memorandum, Business Clearance Memorandum, or in

the Determination and Finding of Contract Type. We interpreted the interim rule to

apply to task or delivery orders issued after the effective date of the interim rule

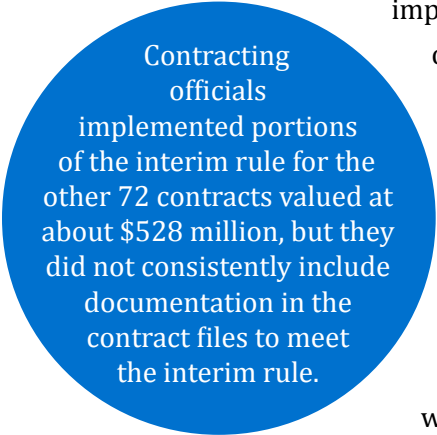
(March 16, 2011), regardless of the timing of the basic contract award. See

Appendix C for tables showing interim rule compliance by contract. MDA and

DMEA contracting officials should emphasize the importance of the Federal

Acquisition Regulation revisions to contracting personnel for the use of cost-

reimbursement contracts in guidance and training courses.



Contracting officials implemented portions of the interim rule for the other 72 contracts valued at about \$528 million, but they did not consistently include documentation in the contract files to meet the interim rule.

Cost-Reimbursement Contracts Approved Inconsistently

Contracting personnel at MDA and DMEA did not always meet the interim rule requiring approval one level above the contracting officer for the use of a cost-

reimbursement contract. Contracting personnel at MDA obtained proper approval

for the use of cost-reimbursement contracts on 20 of 39 contracts, valued at about

\$1.18 billion. MDA contracting personnel did not obtain proper approval for the use

of cost-reimbursement contracts on 19 of 39 contracts, valued at about \$74.9 million.

DMEA contracting personnel did not obtain proper approval for the use of cost-

reimbursement contracts on 31 of 49 contracts, valued at about \$192.3 million.

Contracting personnel at MDA were under the impression that, because acquisition

plans were not required for SBIR contracts, they were exempt from the interim

rule's requirement for approval one level above the contracting officer. Additionally, some contracting personnel at both sites cited different interpretations of the interim rule as the reason for their omission of the approval one level above the contracting officer. The Chief, Contracting Division, at DMEA should develop procedures that ensure a senior official approves all cost-reimbursement contracts one level above contracting officer.

No recommendation is directed to MDA because MDA took corrective actions as discussed on page 12 of this report. Additionally, we plan to discuss this area of the interim rule in our summary report. Table 2 shows the total contracts reviewed at each site and the number of those contracts that did not meet this section of the interim rule.

Table 2. Results of Level of Approval One Level Above the Contracting Officer

Site	Total Contracts	Did Not Meet Interim Rule
MDA	39	19
DMEA	49	31
Total	88	50

Generally Included Documentation to Justify the Use of a Cost-Reimbursement Contract Type

Contracting personnel at MDA fully satisfied the interim rule requirement to justify a cost-reimbursement type contract, justifying usage on all 39 contracts, valued at about \$1.26 billion. DMEA generally satisfied the requirement to justify a cost-reimbursement contract, including proper documentation in 39 of the 49 contracts reviewed, valued at about \$404.3 million. However, DMEA contracting personnel did not satisfy the interim rule's requirement to justify a cost-reimbursement type contract for 10 contracts, valued at about \$3.6 million because DMEA contracting personnel generally did not include supplemental documentation including justification of contract type for most contracts under \$1 million. DMEA contracting personnel should emphasize the importance of the Federal Acquisition Regulation revisions to contracting personnel for the use of cost-reimbursement contracts in guidance and training courses.

Table 3 shows the total contracts reviewed at each site and the number of those contracts that did not meet this section of the interim rule.

Table 3. *Justified the Use of a Cost-Reimbursement Contract Type*

Site	Total Contracts	Did Not Meet Interim Rule
MDA	39	0
DMEA	49	10
Total	88	10

MDA Generally Documented Transition Requirements to Firm-Fixed-Price Contracts, but DMEA Did Not Document Efforts for Most Contracts

Contracting personnel at MDA generally documented the possibility of transitioning from a cost-reimbursement type contract to a firm-fixed-price contract, providing the proper documentation on 37 of the 39 contracts reviewed, valued at about \$1.2 billion. The two contracts for which MDA did not provide adequate documentation were valued at about \$43.5 million.

DMEA contracting personnel did not provide adequate documentation on 48 of 49 contracts, valued at about \$403 million. The one contract for which DMEA did provide adequate documentation to support the transition from a cost-reimbursement type to firm-fixed-price contract was valued at about \$5 million. DMEA cited unique, one-time requirements on the majority of its contracts, which will never be renewed, as the reasoning for omitting documentation for the transition of cost-reimbursement type contracts to firm-fixed-price. The Chief, Contracting Division, at DMEA should provide guidance to contracting personnel that the nature of DMEA's contracts and the inability to transition to a firm-fixed-price contract needs to be documented in the contract file of cost-reimbursement contracts.

DMEA contracting personnel did not provide adequate documentation on 48 of 49 contracts, valued at about \$403 million.

Table 4 shows the total contracts reviewed at each site and the number of those contracts that did not meet this section of the interim rule.

Table 4. *Results of Efforts to Transition Subsequent Contracts to Firm-Fixed-Price*

Site	Total Contracts	Did Not Meet Interim Rule
MDA	39	2
DMEA	49	48
Total	88	50

Ensured Government Resources Were Available to Monitor Award

MDA and DMEA contracting personnel satisfied the interim rule requirement to make adequate Government resources available to monitor a cost-reimbursement contract by assigning a COR to 87 of 88 contracts, valued at about \$1.66 billion. The one contract for which DMEA did not provide adequate documentation was valued at about \$.5 million. We will not be making a recommendation based on the small number of non-compliant actions.

Table 5 shows the total contracts reviewed at each site and the number of those contracts that did not meet this section of the interim rule.

Table 5. Results of Government Resources Available to Monitor Contract

Site	Total Contracts	Did Not Meet Interim Rule
MDA	39	0
DMEA	49	1
Total	88	1

Inconsistent Verification That an Adequate Accounting System Was in Place at Award

Contracting personnel at MDA generally verified that an adequate accounting system was in place by providing proper documentation on 32 of 39 contracts reviewed, valued at about \$1.2 billion. MDA contracting personnel did not provide documentation of an adequate accounting system in place on 7 contracts, valued at about \$18.4 million.

DMEA contracting personnel inconsistently verified that an adequate accounting system was in place, providing proper documentation on 29 of 49 contracts reviewed, valued at about \$293 million. DMEA contracting personnel did not provide documentation to determine that an adequate accounting system was in place on 20 contracts, valued at about \$115 million.

Table 6 shows the total contracts reviewed at each site and the number of those contracts that did not meet this section of the interim rule.

Table 6. Results of Adequate Accounting System in Place

Site	Total Contracts	Did Not Meet Interim Rule
MDA	39	7
DMEA	49	20
Total	88	27

Of the 27 cases of noncompliance, valued at about \$133 million, MDA and DMEA contracting personnel stated they were unfamiliar with the interim rule requirements or stated that in some cases audit documentation was not available in the task order files, but was completed for the original contract. MDA and DMEA contracting officials should emphasize the importance of the Federal Acquisition Regulation revisions to contracting personnel for the use of cost-reimbursement contracts in guidance and training courses.

Contracting Personnel Properly Classified Firm-Fixed-Price Contracts

MDA and DMEA contracting personnel classified firm-fixed-price contracts correctly and did not miscode contracts in the Federal Procurement Database System-Next Generation. We reviewed 37 firm-fixed-price contracts issued by MDA and DMEA contracting personnel and determined that no contracts were classified incorrectly.

MDA Has Taken Additional Steps to Increase Compliance

After our initial site visit to MDA in June 2012, the MDA contracting office revised multiple checklists used in the contract writing process. MDA personnel provided four updated checklists for pre-solicitations, competitive awards, non-competitive awards, and issuance of task and delivery orders. Each checklist had a portion added to address specific areas of the interim rule. MDA proactively took steps to increase compliance on future cost-reimbursement contracts. Additionally, MDA personnel provided a list of actions taken on the specific contracts we reviewed to increase their compliance; however, we did not independently verify those actions.

DMEA Implemented New Procedures to Increase Compliance

Immediately after our site visit to DMEA in June 2012, the DMEA contracting office instituted new procedures, guidance, and training to ensure compliance with the

interim rule's requirements. DMEA officials introduced a new procedure that assures that all contracts have one senior official available to approve cost-reimbursement contracts one level above the contracting officer. DMEA contracting personnel were also provided training to highlight the importance of the FAR revisions with regard to the use of cost reimbursement contracts. Additionally, DMEA officials provided follow up guidance to contracting personnel that the nature of the DMEA's contracts and the inability to transition to firm-fixed-price needs to be documented in the contract file of cost-reimbursement contracts. We did not independently verify the adequacy of these new procedures.

Conclusion

Contracting personnel did not consistently implement the interim rule for 72 contracts, valued at about \$528 million, of the 88 contracts we reviewed, valued at about \$1.66 billion. MDA contracting personnel fully met the interim rule on 15 contracts, valued at about \$1.1 billion, of the 39 contracts reviewed. DMEA contracting personnel fully met the interim rule on only one contract valued at about \$5 million, of the 49 contracts reviewed. Contracting personnel continue to issue cost-reimbursement contracts that may inappropriately increase the contracting risks because cost-reimbursement contracts provide less incentive for contractors to control costs. Contracting personnel can better plan, issue, and oversee cost-reimbursement contracts by fully implementing the FAR revisions.

Management Comments on the Finding and Our Response

Defense Microelectronics Activity Comments

The Chief, Contracting Division, Defense Microelectronics Activity, agreed that the level of documentation required by the interim rule was lacking in some files. The Chief, Contracting Division, Defense Microelectronics Activity stated that immediate action was taken to improve internal controls and comply with the interim rule through additional training and new documentation policies.

Our Response

We agree that the implementation of the recommendations as agreed to by the Chief, Contracting Division, Defense Microelectronics Activity, should strengthen internal controls.

Recommendations, Management Comments, and Our Response

Recommendation 1

We recommend that the Director of Contracting, Missile Defense Agency, emphasize the importance of the Federal Acquisition Regulation revisions to contracting personnel for the use of cost-reimbursement contracts in guidance and training courses.

Missile Defense Agency Comments

The Director, Missile Defense Agency (MDA), agreed, stating that MDA officials will emphasize the importance of the Federal Acquisition Regulation revisions for the use of cost-reimbursement contracts to contracting personnel. MDA has already taken proactive action to increase compliance by updating contract checklists to ensure specific revisions are addressed. The director stated that additional guidance and training courses will be implemented. The director stated that the changes outlined should be completed in the second quarter of FY 2014.

Our Response

Comments from the Director, Missile Defense Agency, are responsive, and no further comments are required.

Recommendation 2

We recommend that the Chief, Contracting Division, Defense Microelectronics Activity:

- a. Develop procedures that ensure a senior official approves all cost-reimbursement contracts one level above the contracting officer.**

Defense Microelectronics Activity Comments

The Chief, Contracting Division, Defense Microelectronics Activity, agreed, and immediately established procedures that ensure a senior official is always available to approve all contracts one level above the contracting officer. According to the chief, all applicable contract actions include this level of approval and are documented in the contract file.

Our Response

Comments from the Chief, Contracting Division, Defense Microelectronics Activity, are responsive, and no further comments are required.

- b. Emphasize the importance of the Federal Acquisition Regulation revisions in guidance and training courses to contracting personnel for the use of cost-reimbursement contracts.**

Defense Microelectronics Activity Comments

The Chief, Contracting Division, Defense Microelectronics Activity, agreed, and immediately provided initial training as well as follow up guidance and refresher training to contracting personnel emphasizing the importance of the Federal Acquisition Regulation revisions regarding the use of cost-reimbursement contracts. The chief stated that the use of cost-reimbursement contracts including the risks they pose the Government continue to be a central and integral part of training.

Our Response

Comments from the Chief, Contracting Division, Defense Microelectronics Activity, are responsive, and no further comments are required.

- c. Provide guidance to contracting personnel that the nature of the Defense Microelectronics Activity's contracts and the inability to transition to a firm-fixed-price contract needs to be documented in the contract file of cost-reimbursement contracts.**

Defense Microelectronics Activity Comments

The Chief, Contracting Division, Defense Microelectronics Activity, agreed, and immediately informed contracting personnel that the nature of the Activity's contracts and the inability to transition to firm-fixed-price needs to be documented in the contract file of cost-reimbursement contracts. The chief stated that all applicable contract actions will include this documentation. Contracting personnel also were provided additional guidance and follow-up training on the need to specifically document the inability to transition to firm-fixed-price contracts given the nature of the contracts.

Our Response

Comments from the Chief, Contracting Division, Defense Microelectronics Activity, are responsive, and no further comments are required.

Appendix A

Scope and Methodology

We conducted work used as a basis for this report from February 2012 through August 2012 under DoD IG Project No. D2012-D000CG-0121.000. In August 2012, we decided to issue multiple reports as a result of those efforts. From August 2012 through May 2013, we primarily performed work on other reports in this series. In May 2013, we announced project DoD IG Project No. D2013-D000CG-0170.000 specifically for the Missile Defense Agency (MDA) and the Defense Microelectronics Activity (DMEA) contracts and conducted this performance audit through September 2013. We completed both projects 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

The criteria we applied to this audit included Federal Acquisition Regulation (FAR) revisions required by section 864 of the Duncan Hunter National Defense Authorization Act for Fiscal Year 2009 and implemented by the FAR interim rule, FAC 2005-50, 76 Federal Register 14542, "Proper Use and Management of Cost Reimbursement Contracts" (March 16, 2011). We also reviewed Defense Federal Acquisition Regulation Supplement 242.7502, "Policy" and the Defense Federal Acquisition Regulation Supplement Clause 252.242-7005, "Contractor Business Systems," as well as the Small Business Innovation Research (SBIR) policy directive. The FAR sections updated by the interim rule include FAR 1.602-2, "Responsibilities;" FAR 1.604, "Contracting Officers Representative;" FAR 2.101, "Definitions;" FAR 7.103, "Agency-Head Responsibilities;" FAR 7.104, "General Procedures;" FAR 7.105, "Contents of Written Acquisition Plans;" FAR 16.103, "Negotiating Contract Types;" FAR 16.104, "Factors in Selecting Contract Types;" FAR 16.301-2, "Application;" FAR 16.301-3, "Limitations;" FAR 42.302, "Contract Administration Functions;" and FAR subpart 50.1, "Extraordinary Contractual Actions."

In addition to this report, we plan to issue separate reports for each Service and a summary report. This is the third report in the planned series of reports. This audit was required by the FY 2009 National Defense Authorization Act, section 864, "Regulation on the Use of Cost Reimbursement Contracts." Our objective was to determine whether DoD has complied with interim Federal Acquisition Regulation revisions on the use of cost-reimbursement contracts.

To determine compliance with the interim rule, our methodology included reviewing basic contract and task and delivery order files that varied slightly from the specific interim rule requirements. In cases where the interim rule required areas to be documented in the Acquisition Plan, we expanded our review to the entire contract file because, in many cases, the Acquisition Plan was written and approved before the interim rule was issued. Additionally, we focused our audit to assess how contracting personnel determined that adequate resources were available to monitor the award by determining whether a contracting officer's representative (COR) or similar person was assigned to the contract at issuance. We did not determine whether the person assigned had an appropriate workload or was properly geographically located to monitor the award. We identified the assignment of a COR on the contracts rather than testing the adequacy of the COR assigned to the contract reviewed. Additionally, we determined whether the contracting officer documented that the contractor's accounting system was adequate at contract award and not during the entire period of contract performance as required by the interim rule.

Universe and Sample Information

We used Federal Procurement Data System-Next Generation data to identify a universe of cost-reimbursement, labor hour, and time and materials contracts issued by Defense agencies and activities from March 17, 2011, through February 29, 2012. We included task and delivery orders issued after March 17, 2011, in our universe even if the basic contract was issued before the interim ruling. We limited the review to contracts valued at \$150,000 or above. We removed contract modifications from our universe because they are not new contract awards. We eliminated contracts that were issued on General Service Administration contracts. We queried all cost-reimbursement contracts from March 17, 2011 through February 29, 2012. Our universe consisted of 971 contract actions, on 489 contracts, valued at about \$13.9 billion; this includes the value of all potential options and any firm-fixed-price portions of the contracts. To meet DoD Inspector General's audit requirement in Section 864 of the FY 2009 National Defense Authorization Act, we determined that we would review one Defense agency and one Defense activity. We chose MDA and DMEA based on a combination of cost-reimbursement award amounts and number of cost-reimbursement contracts and task or delivery orders issued.

MDA had 161 contract actions, on 106 unique contracts, valued at about \$7.5 billion. We visited MDA (Huntsville, Alabama) and reviewed 39 contracts with cost-reimbursement portions valued at about \$1.26 billion.

DMEA had 130 contract actions, on 12 unique contracts, valued at about \$674 million. We selected contract actions to review based on date issued, dollar amount, and other factors. We visited DMEA (McClellan, California) and reviewed 49 of the selected contracts with cost-reimbursement portions valued at about \$408 million.

Review of Documentation and Interviews

We reviewed documentation maintained by the MDA and DMEA contracting offices. The documents reviewed included Acquisition Plans, Pre/Post Price Negotiation Memorandums, Determination and Finding for Contract Type, COR designation letters, COR training certificates, Defense Contract Audit Agency audit reports, and other documentation included in the contract file to comply with the interim rule. We reviewed contract award documentation including basic contract files from FY 2007 through FY 2012. We interviewed personnel responsible for awarding contracts, as well as quality assurance personnel, such as CORs, who were responsible for monitoring the contracts.

At each site visited, we determined whether contracting personnel implemented the interim rule by documenting:

- that the approval for the cost-reimbursement contract was at least one level above the contracting officer;
- that the justification for the use of cost-reimbursement, time and materials, or labor hour contracts;
- how the requirements under the contract could transition to firm-fixed-price in the future;
- that Government resources were available to monitor the cost-reimbursement contract; and
- whether the contractor had an adequate accounting system in place at contract award.

We tested MDA and DMEA contracts to determine whether contracting personnel were misclassifying cost-reimbursement contracts as firm-fixed-price contracts.

We used Federal Procurement Data System-Next Generation and Electronic Document Access to review the firm-fixed-price contracts. We reviewed between 40 and 50 firm-fixed-price contracts at each site to determine whether contracts contained cost-reimbursement line items. Although we used these systems during our audit, we did not use them as a material basis for our findings, recommendations, or conclusions.

Use of Computer-Processed Data

We did not rely on computer-processed data for this audit.

Use of Technical Assistance

We worked with members of the DoD Office of Inspector General Quantitative Methods Division during our planning phase to determine the number of sites to visit and the number of contracts that should be reviewed at each site. They suggested that we review a nonstatistical sample of at least 30 contracts per site.

Prior Coverage

During the last 5 years, the Government Accountability Office, the Department of Defense Inspector General, the Department of Transportation Inspector General, the Department of Homeland Security Inspector General, the General Services Administration Inspector General, and the National Aeronautics and Space Administration Inspector General have issued seven reports discussing oversight of the use of cost-reimbursement contracts. Government Accountability Office reports can be accessed at www.gao.gov. Department of Defense Inspector General reports can be accessed at www.dodig.mil. Department of Transportation Inspector General Reports can be accessed at www.oig.dot.gov. Department of Homeland Defense Inspector General reports can be accessed at www.oig.dhs.gov. General Services Administration Inspector General reports can be accessed at www.gsaig.gov. National Aeronautics and Space Administration Inspector General reports can be accessed at www.oig.nasa.gov.

Government Accountability Office

Report No. GAO-09-921, "Contract Management: Extent of Federal Spending Under Cost-Reimbursement Contracts Unclear and Key Controls Not Always Used," September 30, 2009

Department of Defense Inspector General

Report No. DODIG-2013-120, "Army Needs Better Processes to Appropriately Justify and Manage Cost-Reimbursement Contracts," August 23, 2013

Report No. DODIG-2013-059, "Air Force Needs Better Processes to Appropriately Justify and Manage Cost-Reimbursable Contracts," March 21, 2013

Department of Transportation Inspector General

Report No. ZA-2013-118, "DOT Does Not Fully Comply With Revised Federal Acquisition Regulations on the Use and Management of Cost-Reimbursement Awards," August 5, 2013

Department of Homeland Security Inspector General

Report No. OIG-12-133, "Department of Homeland Security Compliance with the Federal Acquisition Regulation Revisions on Proper Use and Management of Cost-Reimbursement Contracts," September 28, 2012

General Services Administration Inspector General

Report No. A120052/Q/A/P12004, "Audit of GSA's Cost-Reimbursement Contracts," March 30, 2012

National Aeronautics and Space Administration Inspector General

Report No. IG-12-014, "Final Memorandum on NASA's Compliance with Provisions of the Duncan Hunter National Defense Authorization Act 2009–Management of Cost-Reimbursement Contracts," March 14, 2012

Appendix B

Federal Acquisition Circular 2005-50, Issued March 16, 2011

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DEPARTMENT OF DEFENSE

**GENERAL SERVICES
ADMINISTRATION**

**NATIONAL AERONAUTICS AND
SPACE ADMINISTRATION**

48 CFR Parts 1, 2, 7, 16, 32, 42, and 50

[FAC 2005-50; FAR Case 2008-030; Item
I; Docket 2011-0082, Sequence 1]

RIN 9000-AL78

**Federal Acquisition Regulation; Proper
Use and Management of Cost-
Reimbursement Contracts**

AGENCIES: Department of Defense (DoD),
General Services Administration (GSA),
and National Aeronautics and Space
Administration (NASA).

ACTION: Interim rule with request for
comments.

SUMMARY: DoD, GSA, and NASA are
issuing an interim rule amending the
Federal Acquisition Regulation (FAR) to
implement section 864 of the Duncan
Hunter National Defense Authorization
Act for Fiscal Year 2009. This law aligns

Federal Acquisition Circular 2005-50, Issued March 16, 2011 (cont'd)

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with the Presidential Memorandum on Government Contracting, issued on March 4, 2009, which directed agencies to save \$40 billion in contracting annually by Fiscal Year (FY) 2011 and to reduce the use of high-risk contracts. This rule provides regulatory guidance on the proper use and management of other than firm-fixed-price contracts (e.g., cost-reimbursement, time-and-material, and labor-hour).

DATES: *Effective Date:* March 16, 2011.

Comment Date: Interested parties should submit written comments to the Regulatory Secretariat on or before May 16, 2011 to be considered in the formulation of a final rule.

ADDRESSES: Submit comments identified by FAC 2005-50, FAR Case 2008-030, by any of the following methods:

- *Regulations.gov:* <http://www.regulations.gov>. Submit comments via the Federal eRulemaking portal by inputting "FAR Case 2008-030" under the heading "Enter Keyword or ID" and selecting "Search." Select the link "Submit a Comment" that corresponds with "FAR Case 2008-030." Follow the instructions provided at the "Submit a Comment" screen. Please include your name, company name (if any), and "FAR Case 2008-030" on your attached document.

- *Fax:* (202) 501-4067.
- *Mail:* General Services Administration, Regulatory Secretariat (MVCB), ATTN: Hada Flowers, 1275 First Street, NE., 7th Floor, Washington, DC 20417.

Instructions: Please submit comments only and cite FAC 2005-50, FAR Case 2008-030, in all correspondence related to this case. All comments received will be posted without change to <http://www.regulations.gov>, including any personal and/or business confidential information provided.

FOR FURTHER INFORMATION CONTACT: For clarification of content, contact Lori Sakalos, Procurement Analyst, at (202) 208-0498. For information pertaining to status or publication schedules, contact the Regulatory Secretariat at (202) 501-4755. Please cite FAC 2005-50, FAR Case 2008-030.

SUPPLEMENTARY INFORMATION:

I. Background

This case implements section 864 of the Duncan Hunter National Defense Authorization Act for Fiscal Year 2009 (Pub. L. 110-417), enacted October 14, 2008. This law aligns with the President's goal of reducing high-risk contracting as denoted in the March 4, 2009, Presidential Memorandum on Government Contracting.

Section 864 requires the FAR to be revised to address the use and management of cost-reimbursement contracts and identifies the following three areas that the Defense Acquisition Regulation Council and the Civilian Agency Acquisition Council (Councils) should consider in amending the FAR—

(a) Circumstances when cost-reimbursement contracts are appropriate;

(b) Acquisition plan findings to support the selection of a cost-reimbursement contract; and

(c) Acquisition resources necessary to award and manage a cost-reimbursement contract.

1. *Guidance on Cost-reimbursement contracts.* As required, the Councils included additional coverage at FAR subpart 16.1, Selecting Contract Types, and at subpart 16.3, Cost-Reimbursement Contracts, to provide further guidance as to when, and under what circumstances, cost-reimbursement contracts are appropriate. Therefore, this rule makes the following changes:

- FAR 16.103, Negotiating contract type, is amended to revise paragraph (d) to reflect additional documentation when other than a firm-fixed-price contract type is selected.

- FAR 16.104, Factors in selecting contract types, is amended to add a new paragraph (e) to provide guidance to the contracting officer to consider combining contract types if the entire contract cannot be firm fixed-price.

- FAR 16.301-2, Application, is amended to provide guidance to the contracting officer as to the circumstances in which to use cost-reimbursement contracts as well as outlining the rationale for documentation for selecting this contract type.

- FAR 16.301-3, Limitations, is amended to (1) provide additional guidance to the contracting officer as to when a cost-reimbursement contract may be used, (2) ensure that all factors have been considered per FAR 16.104, and (3) ensure that adequate Government resources are available to award and manage this type of contract.

- FAR 7.104(e) also requires the designation of a properly trained contracting officer's representative (COR) (or contracting officer's technical representative (COTR)) prior to award of the contract or order.

2. *Identification of acquisition plan findings.* FAR 7.103, Agency-head responsibilities, is amended and renumbered to add new paragraphs 7.103(d), 7.103(f), and 7.103(j) to ensure that acquisition planners document the file to support the selection of the

contract type in accordance with FAR subpart 16.1; ensure that the statement of work is closely aligned with the performance outcomes and cost estimates; and obtain an approval and signature from the appropriate acquisition official at least one level above the contracting officer. FAR 7.105(b)(5)(iv) was added to discuss the strategy to transition from cost-reimbursement contracts to firm-fixed-price contracts. Although FAR 7.105(b)(5), Acquisition considerations, requires the acquisition plans to include a discussion of contract type selection and rationale, the Councils believe that a greater emphasis on the use of cost-reimbursement contracts should be added and included a new paragraph at FAR 7.105(b)(3), Contract type selection. Additionally, FAR 16.301-3(a) has been amended and renumbered.

3. *Acquisition workforce resources.* The Councils recognize that assigning adequate and proper resources to support the solicitation, award, and administration of other than firm-fixed-price contracts (cost-reimbursement, time-and-material, and labor-hour) contract is challenging. There is also great concern that a lack of involvement in contract oversight by program offices is primarily present in other than firm-fixed-price contracts. Therefore, from the outset, contracting officers should be assured, to the greatest extent practicable, that the right resources in number, kind, and availability be assigned to support other than firm-fixed-price contracts. The Councils consider that greater accountability for the management and oversight of all contracts, especially other than firm-fixed-price contracts, can be gained and improved by requiring that properly trained CORs or COTRs (see FAR 2.101(b)(2), Definitions) be appointed before award. Therefore, FAR 7.104, General Procedures, and FAR 16.301-3(a)(4)(i) are amended to reflect that prior to award of a contract, especially on other than firm-fixed price contracts, at least one COR or COTR qualified in accordance with FAR 1.602-2 is designated. FAR 1.602-2, Responsibilities, is amended to add a new paragraph (d) outlining the requirement for the contracting officer to designate and authorize, in writing, a COR on contracts and orders, as appropriate. Additionally, a new section was added at FAR 1.604, Contracting officer's representative, outlining the COR's duties.

4. *Contract administration functions.* A new paragraph was added at FAR 42.302(a)(12) to require that the contracting officer determine the continuing adequacy of the contractor's

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accounting system during the entire period of contract performance. Also, paragraph (a)(12) was added to the list of functions at FAR 42.302(a) that cannot be retained and that must be delegated by the contracting officer when delegating contract administration functions to a contract administration office in accordance with FAR 42.202(a).

II. Executive Order 12866

This is a significant regulatory action and, therefore, was subject to review under Section 6(b) of Executive Order 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

III. Regulatory Flexibility Act

DoD, GSA, and NASA do not expect this interim rule to have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.*, because section 864 affects only internal Government operations and requires the Government to establish internal guidance on the proper use and management of all contracts especially other than firm-fixed-price contracts (e.g., cost-reimbursement, time-and-material, and labor-hour) and does not impose any additional requirements on small businesses.

Therefore, an Initial Regulatory Flexibility Analysis has not been performed. DoD, GSA, and NASA invite comments from small business entities and other interested parties on the expected impact of this rule on small entities.

DoD, GSA, and NASA will also consider comments from small entities concerning the existing regulations in subparts affected by the rule in accordance with 5 U.S.C. 610. Interested parties must submit such comments separately and should cite 5 U.S.C. 610 (FAC 2005-50, FAR Case 2008-030) in correspondence.

IV. Paperwork Reduction Act

The changes to the FAR do not impose information collection requirements that require the approval of the Office of Management and Budget under the Paperwork Reduction Act (44 U.S.C. chapter 35).

V. Determination To Issue an Interim Rule

A determination has been made under the authority of the Secretary of Defense (DoD), the Administrator of General Services (GSA), and the Administrator of the National Aeronautics and Space Administration (NASA) that urgent and

compelling reasons exist to promulgate this interim rule without prior opportunity for public comment. This action is necessary because section 864 of the Duncan Hunter National Defense Authorization Act for Fiscal Year 2009, enacted October 14, 2008, directs that it must be implemented within 270 days from enactment. This rule is also urgent because this law requires the Inspector General to conduct a compliance review for each executive agency, one year after the regulations have been promulgated, on the use of cost-reimbursement contracts and include the results of their findings in the IG's next semiannual report. However, pursuant to 41 U.S.C. 1707 and FAR 1.501-3(b), DoD, GSA, and NASA will consider public comments received in response to this interim rule in the formation of the final rule.

List of Subjects in 48 CFR Parts 1, 2, 7, 16, 32, 42, and 50

Government procurement.

Dated: March 4, 2011.

Millisa Gary,

Acting Director, Office of Governmentwide Acquisition Policy Division.

Therefore, DoD, GSA, and NASA amend 48 CFR parts 1, 2, 7, 16, 32, 42, and 50 as set forth below:

- 1. The authority citation for 48 CFR parts 1, 2, 7, 16, 32, 42, and 50 continues to read as follows:

Authority: 40 U.S.C. 121(c); 10 U.S.C. chapter 137; and 42 U.S.C. 2473(c).

PART 1—FEDERAL ACQUISITION REGULATIONS SYSTEM

- 2. Amend section 1.602-2 by adding paragraph (d) to read as follows:

1.602-2 Responsibilities.

* * * * *

(d) Designate and authorize, in writing, a contracting officer's representative (COR) on all contracts and orders other than those that are firm-fixed price, and for firm-fixed-price contracts and orders as appropriate. However, the contracting officer is not precluded from retaining and executing the COR duties as appropriate. *See* 7.104(e). A COR—

(1) Must be a Government employee, unless otherwise authorized in agency regulations;

(2) Shall be certified and maintain certification in accordance with the Office of Management and Budget memorandum entitled "The Federal Acquisition Certification for Contracting Officer Technical Representatives" dated November 26, 2007, or for DoD, DoD Regulations, as applicable;

(3) Must be qualified by training and experience commensurate with the responsibilities to be delegated in accordance with department/agency guidelines;

(4) May not be delegated responsibility to perform functions that have been delegated under 42.202 to a contract administration office, but may be assigned some duties at 42.302 by the contracting officer;

(5) Has no authority to make any commitments or changes that affect price, quality, quantity, delivery, or other terms and conditions of the contract; and

(6) Must be designated in writing, with copies furnished to the contractor and the contract administration office—

(i) Specifying the extent of the COR's authority to act on behalf of the contracting officer;

(ii) Identifying the limitations on the COR's authority;

(iii) Specifying the period covered by the designation;

(iv) Stating the authority is not redelegable; and

(v) Stating that the COR may be personally liable for unauthorized acts.

- 3. Amend section 1.603 by revising the section heading to read as follows:

1.603 Selection, appointment, and termination of appointment for contracting officers.

* * * * *

- 4. Add section 1.604 to read as follows:

1.604 Contracting Officer's Representative (COR).

A contracting officer's representative (COR) assists in the technical monitoring or administration of a contract (*see* 1.602-2(d)). The COR shall maintain a file for each assigned contract. The file must include, at a minimum—

(a) A copy of the contracting officer's letter of designation and other documents describing the COR's duties and responsibilities;

(b) A copy of the contract administration functions delegated to a contract administration office which may not be delegated to the COR (*see* 1.602-2(d)(4)); and

(c) Documentation of COR actions taken in accordance with the delegation of authority.

PART 2—DEFINITIONS OF WORDS AND TERMS

- 5. Amend section 2.101 in paragraph (b)(2) by adding, in alphabetical order, the definition "Contracting officer's representative (COR)" to read as follows:

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2.101 Definitions.

* * * * *

(b) * * *

(2) * * *

Contracting officer's representative (COR) means an individual, including a contracting officer's technical representative (COTR), designated and authorized in writing by the contracting officer to perform specific technical or administrative functions.

* * * * *

PART 7—ACQUISITION PLANNING

■ 6. Amend section 7.102 by adding paragraph (a)(3) to read as follows:

7.102 Policy.

(a) * * *

(3) Selection of appropriate contract type in accordance with part 16.

* * * * *

■ 7. Amend section 7.103 by—

■ a. Redesignating paragraphs (e) through (w) as paragraphs (g) through (y);

■ b. Redesignating paragraph (d) as paragraph (e);

■ c. Adding a new paragraph (d);

■ d. Revising newly redesignated paragraph (e);

■ e. Adding a new paragraph (f); and

■ f. Revising newly redesignated paragraph (j).

The added and revised text reads as follows:

7.103 Agency-head responsibilities.

* * * * *

(d) Ensuring that acquisition planners document the file to support the selection of the contract type in accordance with subpart 16.1.

(e) Establishing criteria and thresholds at which increasingly greater detail and formality in the planning process is required as the acquisition becomes more complex and costly, including for cost-reimbursement and other high-risk contracts (*e.g.*, other than firm-fixed-price contracts) requiring a written acquisition plan. A written plan shall be prepared for cost reimbursement and other high-risk contracts other than firm-fixed-price contracts, although written plans may be required for firm-fixed-price contracts as appropriate.

(f) Ensuring that the statement of work is closely aligned with performance outcomes and cost estimates.

* * * * *

(j) Reviewing and approving acquisition plans and revisions to these plans to ensure compliance with FAR requirements including 7.104 and part 16. For other than firm-fixed-price contracts, ensuring that the plan is

approved and signed at least one level above the contracting officer.

* * * * *

■ 8. Amend section 7.104 by adding paragraph (e) to read as follows:

7.104 General procedures.

* * * * *

(e) The planner shall ensure that a COR is nominated by the requirements official, and designated and authorized by the contracting officer, as early as practicable in the acquisition process. The contracting officer shall designate and authorize a COR as early as practicable after the nomination. *See* 1.602–2(d).

■ 9. Amend section 7.105 by—

■ a. Removing from the first sentence of the introductory text the words “*see* paragraph (b)(19)” and adding the words “*see* paragraph (b)(21)” in their place;

■ b. Redesignating paragraphs (b)(3) through (b)(21) as paragraphs (b)(4) through (b)(22), respectively;

■ c. Adding a new paragraph (b)(3);

■ d. Removing from newly redesignated paragraph (b)(5)(i) the words “contract type selection (*see* part 16);”;

■ e. Removing from newly redesignated paragraph (b)(5)(ii)(A) the words “*see* 7.103(t)” and adding the words “*see* 7.103(v)” in its place; and

■ f. Adding paragraph (b)(5)(iv).

The added text reads as follows:

7.105 Contents of written acquisition plans.

* * * * *

(b) * * *

(3) *Contract type selection.* Discuss the rationale for the selection of contract type. For other than firm-fixed-price contracts, *see* 16.103(d) for additional documentation guidance. Acquisition personnel shall document the acquisition plan with findings that detail the particular facts and circumstances, (*e.g.*, complexity of the requirements, uncertain duration of the work, contractor's technical capability and financial responsibility, or adequacy of the contractor's accounting system), and associated reasoning essential to support the contract type selection. The contracting officer shall ensure that requirements and technical personnel provide the necessary documentation to support the contract type selection.

* * * * *

(5) * * *

(iv) For each contract (and order) contemplated, discuss the strategy to transition to firm-fixed-price contracts to the maximum extent practicable. During the requirements development stage, consider structuring the contract

requirements, *e.g.*, contract line items (CLINS), in a manner that will permit some, if not all, of the requirements to be awarded on a firm-fixed-price basis, either in the current contract, future option years, or follow-on contracts. This will facilitate an easier transition to a firm-fixed-price contract because a cost history will be developed for a recurring definitive requirement.

* * * * *

PART 16—TYPES OF CONTRACTS

■ 10. Amend section 16.103 by revising paragraphs (d)(1) and (2) to read as follows:

16.103 Negotiating contract type.

* * * * *

(d) * * *

(1) Each contract file shall include documentation to show why the particular contract type was selected. This shall be documented in the acquisition plan, or if a written acquisition plan is not required, in the contract file.

(i) Explain why the contract type selected must be used to meet the agency need.

(ii) Discuss the Government's additional risks and the burden to manage the contract type selected (*e.g.*, when a cost-reimbursement contract is selected, the Government incurs additional cost risks, and the Government has the additional burden of managing the contractor's costs). For such instances, acquisition personnel shall discuss—

(A) How the Government identified the additional risks (*e.g.*, pre-award survey, or past performance information);

(B) The nature of the additional risks (*e.g.*, inadequate contractor's accounting system, weaknesses in contractor's internal control, non-compliance with Cost Accounting Standards, or lack of or inadequate earned value management system); and

(C) How the Government will manage and mitigate the risks.

(iii) Discuss the Government resources necessary to properly plan for, award, and administer the contract type selected (*e.g.*, resources needed and the additional risks to the Government if adequate resources are not provided).

(iv) For other than a firm-fixed price contract, at a minimum the documentation should include—

(A) An analysis of why the use of other than a firm-fixed-price contract (*e.g.*, cost reimbursement, time and materials, labor hour) is appropriate;

(B) Rationale that detail the particular facts and circumstances (*e.g.*,

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complexity of the requirements, uncertain duration of the work, contractor's technical capability and financial responsibility, or adequacy of the contractor's accounting system), and associated reasoning essential to support the contract type selection;

(C) An assessment regarding the adequacy of Government resources that are necessary to properly plan for, award, and administer other than firm-fixed-price contracts; and

(D) A discussion of the actions planned to minimize the use of other than firm-fixed-price contracts on future acquisitions for the same requirement and to transition to firm-fixed-price contracts to the maximum extent practicable.

(v) A discussion of why a level-of-effort, price redetermination, or fee provision was included.

(2) Exceptions to the requirements at (d)(1) of this section are—

(i) Fixed-price acquisitions made under simplified acquisition procedures;

(ii) Contracts on a firm-fixed-price basis other than those for major systems or research and development; and

(iii) Awards on the set-aside portion of sealed bid partial set-asides for small business.

* * * * *

■ 11. Amend section 16.104 by—

■ a. Redesignating paragraphs (e) through (k) as paragraphs (f) through (l), respectively;

■ b. Adding a new paragraph (e);

■ c. Removing from newly redesignated paragraph (f) the words “incentives to ensure” and adding the words “incentives tailored to performance outcomes to ensure” in their place;

■ d. Removing from newly redesignated paragraph (g) the words “price adjustment terms” and adding the words “price adjustment or price redetermination clauses” in their place; and

■ e. Revising newly redesignated paragraph (i).

The added and revised text reads as follows:

16.104 Factors in selecting contract types.

* * * * *

(e) *Combining contract types.* If the entire contract cannot be firm-fixed-price, the contracting officer shall consider whether or not a portion of the contract can be established on a firm-fixed-price basis.

* * * * *

(i) *Adequacy of the contractor's accounting system.* Before agreeing on a contract type other than firm-fixed-price, the contracting officer shall

ensure that the contractor's accounting system will permit timely development of all necessary cost data in the form required by the proposed contract type. This factor may be critical—

(1) When the contract type requires price revision while performance is in progress; or

(2) When a cost-reimbursement contract is being considered and all current or past experience with the contractor has been on a fixed-price basis. *See* 42.302(a)(12).

* * * * *

■ 12. Revise section 16.301–2 to read as follows:

16.301–2 Application.

(a) The contracting officer shall use cost-reimbursement contracts only when—

(1) Circumstances do not allow the agency to define its requirements sufficiently to allow for a fixed-price type contract (*see* 7.105); or

(2) Uncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy to use any type of fixed-price contract.

(b) The contracting officer shall document the rationale for selecting the contract type in the written acquisition plan and ensure that the plan is approved and signed at least one level above the contracting officer (*see* 7.103(j) and 7.105). If a written acquisition plan is not required, the contracting officer shall document the rationale in the contract file. *See also* 16.103(d).

■ 13. Amend section 16.301–3 by revising paragraph (a) to read as follows:

16.301–3 Limitations.

(a) A cost-reimbursement contract may be used only when—

(1) The factors in 16.104 have been considered;

(2) A written acquisition plan has been approved and signed at least one level above the contracting officer;

(3) The contractor's accounting system is adequate for determining costs applicable to the contract; and

(4) Adequate Government resources are available to award and manage a contract other than firm-fixed-priced (*see* 7.104(e)) including—

(i) Designation of at least one contracting officer's representative (COR) qualified in accordance with 1.602–2 has been made prior to award of the contract or order; and

(ii) Appropriate Government surveillance during performance to provide reasonable assurance that efficient methods and effective cost controls are used.

* * * * *

PART 32—CONTRACT FINANCING

32.1007 [Amended]

■ 14. Amend section 32.1007 by removing from paragraph (a) “(*see* 42.302(a)(12))” and adding “(*see* 42.302(a)(13))” in its place.

PART 42—CONTRACT ADMINISTRATION AND AUDIT SERVICES

■ 15. Amend section 42.302 by—

■ a. Removing from the introductory text of paragraph (a) the words “paragraphs (a)(5), (a)(9), and (a)(11)” and adding the words “paragraphs (a)(5), (a)(9), (a)(11), and (a)(12)” in their place;

■ b. Redesignating paragraphs (a)(12) through (a)(26) as paragraphs (a)(13) through (a)(27); and

■ c. Adding a new paragraph (a)(12) to read as follows:

42.302 Contract administration functions.

(a) * * *

(12) Determine the adequacy of the contractor's accounting system. The contractor's accounting system should be adequate during the entire period of contract performance. The adequacy of the contractor's accounting system and its associated internal control system, as well as contractor compliance with the Cost Accounting Standards (CAS), affect the quality and validity of the contractor data upon which the Government must rely for its management oversight of the contractor and contract performance.

* * * * *

PART 50—EXTRAORDINARY CONTRACTUAL ACTIONS AND THE SAFETY ACT

50.205–1 [Amended]

■ 16. Amend section 50.205–1 by removing from the first sentence in paragraph (b) the words “(*see* FAR 7.105(b)(19)(v))” and adding the words “(*see* 7.105(b)(20)(v))” in their place.

[FR Doc. 2011–5552 Filed 3–15–11; 8:45 am]

BILLING CODE 6820–EP–P

Appendix C

Contract Compliance with Interim Rule Requirements (Base Documentation Applies to Orders)

	Contract Number	Order Number (if applicable)	Site Location	Approval	Justification	Transition	Monitoring	Accounting System	Not-To-Exceed CR Value
1	HQ0147-11-C-7718		MDA	No	Yes	Yes	Yes	Yes	\$ 1,000,000
2	HQ0147-11-C-0013		MDA	Yes	Yes	Yes	Yes	Yes	4,251,761
3	HQ0147-12-C-7743		MDA	No	Yes	Yes	Yes	Yes	999,983
4	HQ0147-12-C-7716		MDA	No	Yes	Yes	Yes	Yes	1,000,000
5	HQ0147-11-C-7738		MDA	No	Yes	Yes	Yes	Yes	999,989
6	HQ0147-11-C-7744		MDA	No	Yes	Yes	Yes	Yes	999,993
7	HQ0147-11-C-7694		MDA	No	Yes	Yes	Yes	No	249,631
8	HQ0147-11-C-0016		MDA	Yes	Yes	Yes	Yes	Yes	13,573,003
9	HQ0147-11-D-0015		MDA	Yes	Yes	Yes	Yes	Yes	595,000,000
10	HQ0147-10-D-0022	0005	MDA	Yes	Yes	Yes	Yes	Yes	2,235,466
11	HQ0147-10-D-0024	0003	MDA	Yes	Yes	Yes	Yes	Yes	5,829,579
12	HQ0147-10-D-0010	0005	MDA	Yes	Yes	Yes	Yes	Yes	9,412,630
13	HQ0006-07-D-0002	0005	MDA	Yes	Yes	Yes	Yes	No	2,593,789
14	HQ0147-11-D-0014	0002	MDA	Yes	Yes	Yes	Yes	Yes	18,516,580
15	HQ0147-11-C-7731		MDA	No	Yes	Yes	Yes	Yes	999,407
16	HQ0147-11-C-7715		MDA	No	Yes	Yes	Yes	Yes	999,998
17	HQ0147-11-C-7737		MDA	No	Yes	Yes	Yes	Yes	1,000,000
18	HQ0147-11-C-0003		MDA	No	Yes	Yes	Yes	Yes	2,554,891
19	HQ0006-04-D-0006	0030	MDA	Yes	Yes	Yes	Yes	Yes	3,150,000
20	HQ0147-11-C-0100		MDA	Yes	Yes	Yes	Yes	Yes	43,295,215

Acronyms used throughout Appendix C are defined on the final page of Appendix C.

Contract Compliance with Interim Rule Requirements (cont'd)

	Contract Number	Order Number (if applicable)	Site Location	Approval	Justification	Transition	Monitoring	Accounting System	Not-To-Exceed CR Value
21	HQ0147-11-D-0052	0006	MDA	Yes	Yes	Yes	Yes	Yes	2,652,485
22	HQ0147-11-D-0008	0003	MDA	Yes	Yes	Yes	Yes	No	1,888,377
23	HQ0147-10-D-0008	0003	MDA	Yes	Yes	Yes	Yes	Yes	81,259,594
24	HQ0147-12-C-6013		MDA	No	Yes	No	Yes	No	837,503
25	HQ0147-10-D-0050	0008	MDA	Yes	Yes	Yes	Yes	Yes	7,618,221
26	HQ0147-11-C-7687		MDA	No	Yes	Yes	Yes	Yes	350,000
27	HQ0147-12-C-7727		MDA	No	Yes	Yes	Yes	Yes	999,631
28	HQ0147-12-C-7724		MDA	No	Yes	Yes	Yes	Yes	999,998
29	HQ0006-08-D-0003	0014	MDA	Yes	Yes	Yes	Yes	Yes	1,670,346
30	HQ0147-11-C-6011		MDA	No	Yes	Yes	Yes	Yes	800,000
31	HQ0147-11-C-7752		MDA	No	Yes	Yes	Yes	Yes	999,940
32	HQ0147-11-C-7699		MDA	No	Yes	Yes	Yes	Yes	1,245,963
33	HQ0147-11-C-0014		MDA	No	Yes	Yes	Yes	No	9,558,740
34	HQ0147-12-D-0003	0001	MDA	Yes	Yes	Yes	Yes	Yes	337,069,176
35	HQ0147-10-D0001	0007	MDA	Yes	Yes	Yes	Yes	Yes	5,387,767
36	HQ0147-12-C-0001		MDA	Yes	Yes	Yes	Yes	No	899,983
37	HQ0147-10-D-0011	0003	MDA	Yes	Yes	Yes	Yes	No	2,417,733
38	HQ0147-11-C-0009		MDA	Yes	Yes	No	Yes	Yes	42,716,764
39	HQ0147-11-D-0013		MDA	No	Yes	Yes	Yes	Yes	48,351,494
	MDA Subtotal:			20	39	37	39	32	\$ 1,256,385,631

Contract Compliance with Interim Rule Requirements (cont'd)

	Contract Number	Order Number (if applicable)	Site Location	Approval	Justification	Transition	Monitoring	Accounting System	Not-To-Exceed CR Value
40	H94003-04-D-0004	0188	DMEA	No	No	No	Yes	No	152,012
41	H94003-04-D-0006	0211	DMEA	No	Yes	No	Yes	Yes	154,800
42	H94003-04-D-0006	0202	DMEA	No	Yes	No	Yes	Yes	197,784
43	H94003-04-D-0007	0023	DMEA	No	No	No	Yes	No	199,579
44	H94003-04-D-0004	0190	DMEA	No	No	No	Yes	No	227,496
45	H94003-04-D-0001	0051	DMEA	No	No	No	Yes	No	234,441
46	H94003-04-D-0002	0081	DMEA	No	No	No	Yes	Yes	249,890
47	H94003-04-D-0004	0207	DMEA	No	No	No	Yes	No	299,742
48	H94003-04-D-0008	0005	DMEA	No	No	No	Yes	Yes	669,778
49	H94003-04-D-0006	0199	DMEA	No	No	No	Yes	Yes	349,717
50	H94003-04-D-0006	0186	DMEA	No	Yes	No	Yes	Yes	410,979
51	H94003-07-D-7001	0003	DMEA	No	No	No	No	No	520,394
52	H94003-04-D-0006	0224	DMEA	No	Yes	No	Yes	Yes	571,915
53	H94003-04-D-0004	0174	DMEA	No	No	No	Yes	No	679,915
54	H94003-04-D-0004	0187	DMEA	No	Yes	No	Yes	No	925,334
55	H94003-04-D-0004	0198	DMEA	No	Yes	No	Yes	No	1,056,839
56	H94003-04-D-0004	0181	DMEA	No	Yes	No	Yes	No	1,131,648
57	H94003-04-D-0005	0039	DMEA	No	Yes	No	Yes	Yes	1,537,071
58	H94003-04-D-0007	0025	DMEA	No	Yes	No	Yes	No	1,898,592
59	H94003-04-D-0002	0084	DMEA	No	Yes	No	Yes	Yes	2,235,449
60	H94003-04-D-0001	0053	DMEA	Yes	Yes	No	Yes	No	19,209,762
61	H94003-11-C-1107		DMEA	No	Yes	No	Yes	No	7,580,409
62	H94003-04-D-0001	0050	DMEA	No	Yes	No	Yes	No	25,701,837

Contract Compliance with Interim Rule Requirements (cont'd)

	Contract Number	Order Number (if applicable)	Site Location	Approval	Justification	Transition	Monitoring	Accounting System	Not-To-Exceed CR Value
63	H94003-04-D-0004	0208	DMEA	No	Yes	No	Yes	No	20,049,007
64	H94003-04-D-0005	0040	DMEA	Yes	Yes	No	Yes	Yes	37,918,034
65	H94003-04-D-0005	0042	DMEA	Yes	Yes	No	Yes	Yes	18,827,639
66	H94003-04-D-0006	0185	DMEA	Yes	Yes	No	Yes	Yes	23,208,889
67	H94003-04-D-0006	0187	DMEA	Yes	Yes	No	Yes	Yes	26,483,654
68	H94003-04-D-0006	0207	DMEA	No	Yes	No	Yes	Yes	44,426,524
69	H94003-04-D-0006	0222	DMEA	No	Yes	No	Yes	Yes	45,535,713
70	H94003-04-D-0007	0019	DMEA	Yes	Yes	No	Yes	No	19,949,457
71	H94003-04-D-0002	0072	DMEA	Yes	Yes	Yes	Yes	Yes	5,081,429
72	H94003-04-D-0002	0075	DMEA	Yes	Yes	No	Yes	Yes	15,852,197
73	H94003-04-D-0002	0077	DMEA	Yes	Yes	No	Yes	Yes	3,729,218
74	H94003-04-D-0002	0078	DMEA	Yes	Yes	No	Yes	Yes	11,351,487
75	H94003-04-D-0002	0082	DMEA	No	Yes	No	Yes	Yes	2,900,000
76	H94003-04-D-0002	0083	DMEA	No	Yes	No	Yes	Yes	3,996,717
77	H94003-04-D-0003	0048	DMEA	Yes	Yes	No	Yes	Yes	4,322,669
78	H94003-04-D-0003	0054	DMEA	Yes	Yes	No	Yes	Yes	5,842,270
79	H94003-04-D-0004	0182	DMEA	Yes	Yes	No	Yes	No	3,708,090
80	H94003-04-D-0004	0183	DMEA	No	Yes	No	Yes	No	3,944,679
81	H94003-04-D-0005	0036	DMEA	Yes	Yes	No	Yes	Yes	2,898,380
82	H94003-04-D-0005	0037	DMEA	No	Yes	No	Yes	Yes	4,666,750
83	H94003-04-D-0006	0191	DMEA	Yes	Yes	No	Yes	Yes	7,633,126
84	H94003-04-D-0006	0192	DMEA	Yes	Yes	No	Yes	Yes	2,465,030
85	H94003-04-D-0006	0197	DMEA	Yes	Yes	No	Yes	Yes	3,864,901

Contract Compliance with Interim Rule Requirements (cont'd)

	Contract Number	Order Number (if applicable)	Site Location	Approval	Justification	Transition	Monitoring	Accounting System	Not-To-Exceed CR Value
86	H94003-04-D-0006	0216	DMEA	No	Yes	No	Yes	Yes	15,568,715
87	H94003-04-D-0007	0015	DMEA	No	Yes	No	Yes	No	4,258,768
88	H94003-11-C-1108		DMEA	Yes	Yes	No	Yes	No	3,222,864
	DMEA Subtotal:			18	39	1	48	29	\$ 407,901,590
	Total of All Compliant Contracts:			38	78	38	87	61	
	Total of All Non-Compliant Contracts			50	10	50	1	27	
	Total CR Value of All Contracts Reviewed								\$ 1,664,287,221

CR Cost Reimbursement
MDA Missile Defense Agency
DMEA Defense Microelectronics Activity

Management Comments

Missile Defense Agency Comments



DEPARTMENT OF DEFENSE
MISSILE DEFENSE AGENCY
5700 18TH STREET
FORT BELVOIR, VIRGINIA 22060-5573

OCT 15 2013

Ms. Jacqueline L. Wiccarver
Department of Defense Inspector General
Assistant Inspector General
Acquisition and Contract Management
4800 Mark Center Drive
Alexandria, Virginia 22350-1500

Dear Ms. Wiccarver:

This is the Missile Defense Agency (MDA) response to the DoD IG Draft Report, "Missile Defense Agency and Defense Microelectronics Activity Use of Cost-Reimbursement Contracts," dated September 13, 2013 (Project No. D2013-D000CG-0170.000).

The MDA concurs with Recommendation 1 in the Draft Report. The rationale for our position is included in the enclosure. The response to Recommendation 2 will be provided by the Director, Defense Microelectronics Activity. Additionally, the technical comments of the Report's content are enclosed for your consideration. MDA's comments on the Discussion Draft are also applicable to the Draft Report.

We appreciate the opportunity to comment on the Draft Report. My point of contact for this effort is [REDACTED]

Sincerely,

A handwritten signature in black ink, appearing to read "J. D. Syring", is positioned above the printed name.

J. D. SYRING
Vice Admiral, USN
Director

Enclosures:
As stated

Missile Defense Agency Comments (cont'd)

**DoD IG D2013-D000CG-0170.000-DoD Compliance with FAR Revisions for
Use of Cost-Reimbursement Contracts
DRAFT REPORT
13 September 2013**

Missile Defense Agency Response to DoD IG Recommendation

RECOMMENDATIONS

Recommendation 1:

Director of Contracting, Missile Defense Agency, emphasize the importance of the Federal Acquisition Regulation revisions to contracting personnel for the use of cost-reimbursement contracts in guidance and training courses.

MDA Response to Recommendation 1: Concur

The Director of Contracting, Missile Defense Agency (MDA), will emphasize the importance of the Federal Acquisition Regulation revisions for the use of cost-reimbursement contracts to contracting personnel. MDA has already taken proactive action to increase compliance by updating contract checklists to ensure specific revisions are addressed. Additional guidance and training courses will be implemented.

Estimated Completion Date: 2QFY14

Recommendation 2:

Director of Contracting, Defense Microelectronics Activity:

- a. Develop procedures that ensure a senior official approves all cost-reimbursement contracts one level above the contracting officer.
- b. Emphasize the importance of the Federal Acquisition Regulation revisions in guidance and training courses to contracting personnel for the use of cost reimbursement contracts.
- c. Provide guidance to contracting personnel that the nature of the Defense Microelectronics Activity's contracts and the inability to transition to firm-fixed-price needs to be documented in the contract file of cost-reimbursement contracts.

Response to the Recommendation to be provided by the Director of Contracting, Defense Microelectronics Activity.

Defense Microelectronics Activity Comments



DEFENSE MICROELECTRONICS ACTIVITY

4234 54th Street
McClellan, CA 95652-2100

30 SEP 2013

MEMORANDUM FOR INSPECTOR GENERAL PROGRAM DIRECTOR, ACQUISITION, PARTS, AND INVENTORY

SUBJECT: Defense Microelectronics Activity Use of Cost-Reimbursement Contracts
(Project No. D2013-D000CG-0170.000), Your Ltr, 13 Sep 2013

Thank you for the opportunity to provide comments in response to subject, official draft report. We will respond to recommendations 2.a, 2.b, and 2.c. As recommended, we will also provide comments on the Review of Internal Controls.

Recommendation 2.a: The Director of Contracting develop procedures that ensure a senior official is available to approve all contracts one level above contracting officer.

Response: Agree with finding. Action taken: The Director of Contracting immediately established procedures that ensure a senior official is always available to approve all contracts one level above the contracting officer. (Additional personnel were assigned to insure these specific duties were performed.) All applicable contract actions include this level of approval and are documented in the contract file.

Recommendation 2.b: The Director of Contracting emphasize the importance of the Federal Acquisition Regulation revisions through guidance to contracting personnel for the use of cost-reimbursement contracts.

Response: Agree with finding. Action taken: The Director of Contracting immediately provided initial training as well as follow up guidance and refresher training to contracting personnel emphasizing the importance of the Federal Acquisition Regulation revisions with regard to the use of cost-reimbursement contracts. The use of cost-reimbursement contracts including the risks they pose the Government have in the past and continue to be a central and integral part of DMEA's on-going training and emphasis to contracting personnel.

Recommendation 2.c: The Director of Contracting provide guidance to contracting personnel that the nature of the Activities' contracts and the inability to transition to firm-fixed-price needs to be documented in the contract file of cost-reimbursement contracts.

Response: Agree with finding. Action taken: The Director of Contracting immediately informed and provided training and follow up guidance to contracting personnel that the nature of the Activity's contracts and the inability to transition to firm-fixed-price needs to be documented in the contract file of cost-reimbursement contracts. All applicable contract actions include this documentation.

Review of Internal Controls.

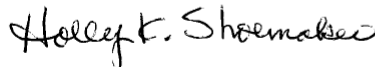
Response: DMEA has always had procedures in place for the review and evaluation of cost-reimbursement contracts. While we agree that the level of documentation required by the interim rule was lacking in some files, contract actions requiring the use of cost-reimbursement

Defense Microelectronics Activity Comments (cont'd)

contracts are reviewed by several disciplines within our process—program management, engineering, finance, legal, and contracting. Action review can include upper-level management in each of these disciplines including the Deputy Director of DMEA. Review and evaluation of cost-reimbursement contracts are documented in our Acquisition Strategy meeting minutes as well as the Price Negotiation Memorandum (PNM). We take the use of cost-reimbursement contracts and the risks associated with them very seriously. DMEA processes for the use, evaluation, and monitoring of cost-reimbursement contracts are followed by the full acquisition team. As stated above, immediate action was taken to comply with the interim rule. Before the IG visit was concluded on 8 Jun 2012, DMEA became compliant with the additional documentation required. By early July, contracting personnel were trained and our new documentation policy deployed.

Regarding verification of the adequacy of the contractor's accounting system. The adequacy of the contractor's accounting system is verified by the Defense Contract Management Agency (DCMA). The (8) major contracts that were audited are with the following contractors-- Raytheon, NGES, NGAS, BAE, Boeing, General Dynamics, and Honeywell. All have adequate accounting systems and this was documented in the basic contract file. DCMA keeps contracting personnel updated on this status. Before the IG visit DMEA contracting personnel documented adequacy in the contract file for contracts (delivery orders) over the TINA threshold in the PNM. After the IG visit the process was expanded to all cost reimbursement actions.

Thank you again, for the opportunity to respond to the draft report. We appreciate being able to have our comments noted in the final report. If you have any questions regarding our response, please contact me at [REDACTED].



HOLLY K. SHOEMAKER
Chief, Contracting Division
Defense Microelectronics Activity

Acronyms and Abbreviations

COR	Contracting Officer's Representative
DMEA	Defense Microelectronics Activity
FAC	Federal Acquisition Circular
FAR	Federal Acquisition Regulation
MDA	Missile Defense Agency
SBIR	Small Business Innovation Research



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U.S. DEPARTMENT OF DEFENSE

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