



U.S. ENVIRONMENTAL PROTECTION AGENCY

OFFICE OF INSPECTOR GENERAL

# Policies Needed for Proper Use and Management of Cost-Reimbursement Contracts Based on Duncan Hunter Act

Report No. 12-P-0320

March 6, 2012



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## Abbreviations

CMM	Contracts Management Manual
CO	Contracting Officer
COR	Contracting Officer's Representative
CPFF	Cost-Plus-Fixed-Fee
EPA	U.S. Environmental Protection Agency
FAR	Federal Acquisition Regulation
FPDS-NG	Federal Procurement Data System-Next Generation
ID/IQ	Indefinite-Delivery/Indefinite-Quantity
OIG	Office of Inspector General

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# At a Glance

## Why We Did This Review

We conducted this audit to determine whether the U.S. Environmental Protection Agency (EPA) complied with revisions made to the Federal Acquisition Regulation (FAR) for use of cost-reimbursement contracts.

## Background

The Duncan Hunter National Defense Authorization Act for fiscal year 2009 required the FAR to be revised to address the use of cost-reimbursement contracts. The FAR was revised on March 16, 2011. The revisions provide additional guidance on when cost-reimbursement contracts are appropriate, require agencies to develop acquisition plans to support the contract type selection, and require agencies to discuss the acquisition resources necessary to award and manage cost-reimbursement contracts. A cost-reimbursement contract is one in which a contractor is paid based on the occurrence of allowable costs.

For further information, contact our Office of Congressional and Public Affairs at (202) 566-2391.

The full report is at:  
[www.epa.gov/oig/reports/2012/20120306-12-P-0320.pdf](http://www.epa.gov/oig/reports/2012/20120306-12-P-0320.pdf)

## ***Policies Needed for Proper Use and Management of Cost-Reimbursement Contracts Based on Duncan Hunter Act***

### What We Found

EPA did not comply with several key revisions to the FAR as amended by the interim rule, *Proper Use and Management of Cost Reimbursement Contracts* (FAR Case 2008-030). Although EPA complied with several revisions, those tended to be areas where the new rules expanded on requirements already in existence. For example, we found that the contract files reviewed generally did not have documentation of:

- Discussions concerning minimizing the use of other than firm-fixed-price contracts on future acquisitions for the same requirement;
- Consideration as to whether portions of the contract could be established on a firm-fixed-price basis; and
- A written acquisition plan.

EPA did not always nominate or appoint contracting officer's representatives (CORs) in writing. EPA program staff did not nominate the current COR for two of the seven contracts in our sample, and contracting officers did not appoint the current COR in writing for four of the seven contracts reviewed.

EPA improperly coded four indefinite-delivery/indefinite-quantity (ID/IQ) Task Order contracts as cost-plus-fixed-fee contracts in EPA's contract writing system and in the Federal Procurement Data System-Next Generation.

### What We Recommend

We recommend that EPA develop a policy that provides a standardized approach for preparing written acquisition plans to ensure compliance with the new FAR revisions. We also recommend that EPA update the procurement initiation notice to include a copy of the COR appointment memorandum and direct contracting officers to verify that nomination forms and appointment memorandums are included in all contract files. Further, we recommend that EPA develop and distribute instructions on coding of ID/IQ contracts. EPA, in its response to the draft report and at the exit conference, concurred with our recommendations and provided milestone dates.



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY  
WASHINGTON, D.C. 20460

THE INSPECTOR GENERAL

March 6, 2012

**MEMORANDUM**

**SUBJECT:** Policies Needed for Proper Use and Management of Cost-Reimbursement  
Contracts Based on Duncan Hunter Act  
Report No. 12-P-0320

**FROM:** Arthur A. Elkins, Jr.  
Inspector General

A handwritten signature in black ink, appearing to read "Arthur A. Elkins, Jr.", is written over the printed name.

**TO:** Craig E. Hooks  
Assistant Administrator for Administration and Resources Management

This is our report on the subject audit conducted by the Office of Inspector General (OIG) of the U.S. Environmental Protection Agency. This report contains findings that describe the problems the OIG has identified and corrective actions the OIG recommends.

**Action Required**

In responding to the draft report, the Agency provided a corrective action plan for addressing the recommendations with milestone dates. Therefore, a response to the final report is not required. The Agency should track corrective actions not implemented in the Management Audit Tracking System. We have no objections to the further release of this report to the public. This report will be available at <http://www.epa.gov/oig>.

If you or your staff have any questions regarding this report, please contact Melissa Heist, Assistant Inspector General for Audit, at (202) 566-0899 or [heist.melissa@epa.gov](mailto:heist.melissa@epa.gov); or Janet Kasper at (312) 866-3059 or [kasper.janet@epa.gov](mailto:kasper.janet@epa.gov).

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# Chapter 1

## Introduction

### Purpose

The U.S. Environmental Protection Agency (EPA) Office of Inspector General (OIG) conducted this audit to determine whether EPA complied with the revisions to the Federal Acquisition Regulation (FAR). The Duncan Hunter National Defense Authorization Act for Fiscal Year 2009 (Act), or Public Law 110-417, Section 864(a), *Regulations on the Use of Cost-Reimbursement Contracts*, required the FAR to be revised to address use of cost-reimbursement contracts. The Act required the OIG to complete a review of the use of cost-reimbursement contracts for compliance with the FAR revisions.

### Background

As the federal government faces pressure to reduce spending, efforts to reform government contracting have increased. Congress has passed legislation, the President has issued a memorandum, and the Office of Management and Budget has issued guidance to federal agencies to improve the effectiveness and efficiency of the federal acquisition system. The federal government obligates hundreds of billions of dollars in contracts for goods and services each year—about \$537 billion in fiscal year 2010. Thus, the potential for savings through improved contracting practices has been a key area of focus, especially on the use of high risk contracts such as cost-reimbursement contracts.

#### ***National Defense Authorization Act and FAR Revisions***

Congress passed the Duncan Hunter National Defense Authorization Act for Fiscal Year 2009 on October 14, 2008, to address the use of high risk contracts awarded throughout the federal government. Section 864 of the Act required that the FAR be revised to address the use of cost-reimbursement contracts. It also required that the Inspector General for each executive agency review the use of cost-reimbursement contracts for compliance with the new FAR revisions and include the results of the review in its next semiannual report, beginning no later than 1 year after the FAR's promulgation.

As mandated by Section 864 of the Act, an interim rule, FAR Case 2008-030, was published on March 16, 2011, through Federal Acquisition Circular 2005-50. FAR Case 2008-030, *Proper Use and Management of Cost-Reimbursement Contracts*, amends the FAR to implement Section 864 of the Act. The interim rule became effective on March 16, 2011. The revisions to the FAR provide additional guidance on when cost-reimbursement contracts are appropriate, require agencies to develop acquisition plans to support the type of contract selected, and require

agencies to discuss the acquisition resources necessary to award and manage a cost-reimbursement contract.

### ***Contract Types and Associated Risks***

The FAR identifies several different contract types: fixed-price, cost-reimbursement, incentive, indefinite-delivery/indefinite-quantity, and time-and-materials. Selecting a contract type is generally a matter for negotiation and requires the exercise of sound judgment. The objective is to negotiate a contract type and price (or estimated cost and fee) that will result in reasonable contractor risk and provide the contractor with the greatest incentive for efficient and economical performance.

Under a cost-reimbursement contract, contractors are paid based on the incurrence of allowable costs, as opposed to the delivery of a completed product or service. This contract type is used in circumstances where an agency is not able to define its requirements sufficiently enough to allow for a fixed-price contract. Complex projects, where the costs of performance cannot be reasonably estimated with a high degree of accuracy, are suitable for this type of contract.

Firm-fixed-price contracts provide a price that is not subject to adjustment and are used when the government's requirements can be well defined. This type of contract places upon the contractor full responsibility for the costs associated with performance and the resulting profit (or loss). They impose a minimum administrative burden on the issuing agency and expose the government to the least risk. For these reasons, firm-fixed-priced contracts are the preferred contract type.

## **Noteworthy Achievements**

EPA's Office of Acquisition Management developed a Balanced Scorecard Performance Measurement and Performance Management Program (Balanced Scorecard) to provide a methodology for assessing performance of EPA's procurement offices. A component of the Balanced Scorecard is a compliance review that focuses on EPA's ability to comply with laws, regulations, etc. To assist in the compliance portion of the self-assessment process, the Office of Acquisition Management developed a checklist to facilitate the review. That checklist contains numerous items, including a step to ensure that all necessary support and documentation are included in the contract file when EPA anticipates a cost-type contract.

## **Scope and Methodology**

We conducted this audit from October 2011 to January 2012 in accordance with generally accepted government auditing standards, issued by the Comptroller General of the United States. 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.

To determine whether EPA complied with FAR revisions relating to FAR Case 2008-030, *Proper Use and Management of Cost-Reimbursement Contracts*, EPA provided a universe of cost-reimbursement contracts the Agency awarded between March 17, 2011, and September 30, 2011. To verify the accuracy of EPA information provided, we conducted independent searches of government contract information systems. We reviewed contract language to verify that the contracts were cost-reimbursement contracts. We did not conduct additional testing of contracts not coded as cost-reimbursable, as this was not part of our scope.

EPA awarded nine<sup>1</sup> cost-reimbursement contracts from four EPA contracting offices during this period. We judgmentally selected a sample of seven contracts representing contracts from each of the four offices. These seven contracts represent 78 percent of the contracts awarded, and 59 percent of the value of the contracts.

**Table 1: Universe of cost-reimbursement contracts**

Contract number	Contractor	Award date	Contract value
EPC11046	Eastern Research Group, Inc.	9/19/2011	\$22,530,518
EPD11006	Eastern Research Group, Inc.	4/29/2011	11,638,236
EPD11060	Oneida Total Integrated Enterprises, LLC	3/24/2011	5,530,737
EPD11073	Dynamac Corporation	6/15/2011	816,467
EPW11029	Research Triangle Institute	3/29/2011	10,299,235
EPW11043	Engineering & Environmental Solutions JV	5/26/2011	18,144,322
EPW11044	Eastern Research Group, Inc.	5/24/2011	6,291,470
<b>Not reviewed</b>			
EPD11092	Trinity Engineering Associates	9/28/2011	6,296,150
EPD11084	RTI International	9/29/2011	45,436,484

Source: OIG analysis

Our work encompassed reviewing contracts in the following EPA contracting offices: Headquarters Procurement Operations Division, Cincinnati Procurement Operations Division, Research Triangle Park Procurement Operations Division, and the Superfund/RCRA Regional Procurement Operations Division. We determined whether the FAR changes (Appendix A) were covered in the sampled contracts through review of the pre-award files and interview of contracting officers (COs).

<sup>1</sup> One of the contracts—EPD11084—was not originally identified by EPA, but was identified by the OIG later through audit steps to determine the validity of the universe provided by EPA.

### ***Internal Control Structure***

In planning and performing our audit, we reviewed management controls related to our objective. Specifically, we examined EPA's Contracts Management Manual and determined whether EPA issued guidance pursuant to the FAR revisions. We reviewed the Office of Administration and Resources Management's fiscal year 2011 Federal Managers' Financial Integrity Act Assurance Letter. EPA did not identify internal control weaknesses related to the audit's objectives. There were no previous audits regarding compliance with the FAR revisions.

## Chapter 2

### EPA Has Not Fully Complied With New FAR Regulations

EPA did not comply with several key revisions to the FAR as amended by the interim rule, *Proper Use and Management of Cost Reimbursement Contracts* (FAR Case 2008-030). Although EPA complied with several revisions, those tended to be areas where the new rules expanded on requirements already in existence. For example, we found that the contract files reviewed generally did not have documentation of:

- Discussions concerning minimizing the use of other than firm-fixed-price contracts on future acquisitions for the same requirement;
- Consideration as to whether portions of the contract could be established on a firm-fixed-price basis; and
- A written acquisition plan.

EPA stated it did not issue guidance pertaining to the FAR revisions because the revisions were promulgated by an interim rule that may be changed. Also, EPA contracting officers did not believe the revisions were applicable because the acquisition process for all of the contracts sampled began prior to the date the FAR revisions were published. Excessive reliance on cost-reimbursement contracts creates a risk that taxpayer funds will be spent on contracts that are wasteful, inefficient, subject to misuse, or otherwise not well designed to serve the needs of the federal government or the interests of the American taxpayer.

#### **FAR Revisions Required by the Duncan Hunter Act**

The FAR was amended through the interim rule *Proper Use and Management of Cost-Reimbursement Contracts* (FAR Case 2008-030). The rule became effective on March 16, 2011, and implements Section 864 of the Act. The revisions to the FAR provide additional guidance regarding:

- 1) Circumstances when cost-reimbursement contracts are appropriate;
- 2) Acquisition plan findings to support the selection of a cost-reimbursement contract; and
- 3) Acquisition resources necessary to award and manage a cost-reimbursement contract.

FAR Subpart 16.103(c) instructs COs to avoid the protracted use of cost-reimbursement contracts after experience provides a basis for firmer pricing. This aligns with a March 4, 2009, Presidential memorandum on government contracting, which contends that the reliance on cost-reimbursement contracts

creates a risk that taxpayer funds are spent on contracts that are wasteful, inefficient, subject to misuse, or otherwise not well designed to serve the needs of the federal government or the interests of the American taxpayer.

## **EPA Has Not Fully Complied With New FAR Regulations**

EPA complied with some, but not all, of the new FAR regulations revised by the interim rule. During reviews of pre-award files we found evidence of:

- Discussions of why circumstances do not allow the Agency to define its requirements sufficiently to allow for a fixed-price type contract;
- Discussions of why a cost-reimbursement contract was selected to meet the Agency's need;
- Evidence of price competition, price analysis, and cost analysis;
- Evaluations of the contractor's technical capability and financial responsibility; and
- Determinations as to the adequacy of the contractor's accounting system

Generally, the requirements complied with were already in existence but reinforced by the new regulations. For example, prior to March 16, 2011, the FAR required documentation showing why a particular contract type was selected. EPA accomplished this through the use of a Determination and Findings document. We identified a Determination and Findings document discussing the contract type selected and why the use of a contract type other than a firm-fixed-price contract was appropriate in all seven of the pre-award files reviewed. However, these documents generally had limited detail, and often included boilerplate language taken from the FAR. The new regulations include additional requirements regarding justifying the use of cost-reimbursable contracts.

In contrast, EPA did not address in the pre-award files a number of key revisions. Most notably, we found no evidence of discussions concerning minimizing the use of other than firm-fixed-price contracts on future acquisitions for the same requirement or establishing portions of the contract on a firm-fixed-price basis. We determined that EPA did not create a written acquisition plan for six of the seven contracts because EPA did not require an acquisition plan for contracts under \$25 million. However, under the new FAR requirements, a written acquisition plan must be approved and signed at least one level above the CO for all cost-reimbursable contracts. In addition, we found the following:

- Six of seven pre-award files did not contain a discussion of the government's additional risks and burden to manage a cost-reimbursement contract.
- None of the seven pre-award files contained a discussion on the adequacy of government resources needed to plan, award, and administer the contract.

- None of the seven pre-award files contained a discussion on the urgency of the Agency's need.
- Six of seven pre-award files did not contain a consideration of the impact of concurrent operations in other contracts.

Details on EPA's compliance with the revised FAR are in appendix A.

In addition, each of the contracts reviewed were follow-on contracts. Because of the nature of the preceding contracts, EPA may have had the opportunity to establish firmer pricing on the current contracts, as EPA was obtaining similar services.

## **EPA Policy Has Not Been Updated**

EPA did not issue internal policy to implement the FAR revisions promulgated by the interim rule. EPA staff said that no policy was issued because the FAR revisions were in an interim rule and changes to the rule may arise from the public comment period before the final rule is established.

The COs for each contract in our sample stated that the regulations did not impact the award of their contracts because the documentation justifying the contract type was completed prior to the effective date of the new regulations, March 16, 2011. We confirmed that the acquisition process for each of the seven contracts began prior to the effective date of the new regulations. However, all the contracts were awarded after this date.

Although the revisions to the FAR were an interim rule, the effective date of those revisions was March 16, 2011. Based on the language in the Act and the FAR, the key was when the contract was awarded, not when the supporting documentation was generated. With this conclusion, all contracts awarded after March 16, 2011, would be subject to the new requirements, even if the justification for the contract type was completed prior to that date.

## **Recommendation**

We recommend that the Assistant Administrator for Administration and Resources Management:

1. Develop a policy for COs that provides guidance on preparing written acquisition plans that comply with the FAR revisions resulting from the interim rule (FAR Case 2008-030).

## Agency Response and OIG Evaluation

While EPA concurred with our recommendation to develop a policy to ensure compliance with the new FAR revisions, the Agency's response did not identify any new actions it would take. EPA stated that it published information and implementation guidance on the FAR revisions on March 17, 2011.

At the exit conference on February 23, 2012, the Director, Office of Acquisition Management, provided some additional explanation regarding the Agency's response. Specifically, the Office of Acquisition Management agreed to complete the following by March 31, 2012:

- Issue an Interim Policy Notice updating the references to the Contracts Management Manual for acquisition planning.
- Update the Peer Review Checklist to reflect changes made to the FAR.

The Agency's response and comments at the exit conference meet the intent of the recommendation.

# Chapter 3

## EPA Staff Are Not Always Nominating or Appointing Contracting Officer's Representatives

EPA did not always nominate or appoint the current contracting officer's representatives (CORs) to serve in that capacity. Both the FAR and EPA's Contracts Management Manual (CMM) require that program staff nominate the COR and require that the CO appoint the COR in writing. EPA staff was aware of the requirements to nominate and appoint CORs but did not officially do so due to an oversight. CORs have vital roles in ensuring, managing, and measuring contract performance in addition to providing technical direction. To accomplish the duties of a COR and act on behalf of the government, proper documentation must be in place to authorize the COR to perform those duties in the prescribed manner.

### Regulations and Internal Guidance Require CORs to Be Nominated and Appointed

FAR Subpart 7.104 states that the requirements official is to nominate a COR as early as practicable in the acquisition process. FAR Subpart 16.301 states that the CO shall designate a COR prior to contract award. EPA's CMM requires that the potential COR's immediate supervisor nominate a COR, and that program offices initiate contact with EPA contracting offices through the use of a procurement initiation notice for new procurements. The CO is to respond to the nomination in writing by either appointing the nominee as a COR or stating why the nominee was not appointed.

### CORs Acting on Behalf of the Government Without Being Formally Nominated or Appointed

Supervisors did not nominate the current COR for EPA contracts EPW11044 and EPD11073. The CO did not appoint the current COR for contracts EPD11006, EPW11044, EPD11073, and EPW11029. During the audit, EPA staff took action to complete all of the missing nomination forms and appointment memorandums. EPA program staff was aware of the requirement to nominate CORs but did not do so due to an oversight. COs did not appoint CORs for two of the four contracts because program staff did not nominate the COR. For the other two contracts, the COs did not appoint the COR due to an oversight. The CMM refers to a form 1900-65, Nomination of the Contracting Officer Representative, and that the form is to be attached to the procurement initiation notice. However, while the procurement initiation notice was included in all files we reviewed, the EPA form 1900-65 for the current COR was not included as an attachment in two cases.

## **Recommendations**

We recommend that the Assistant Administrator for Administration and Resources Management:

2. Update the procurement initiation notice as contained in the CMM to include, as an attachment, a copy of the COR appointment memorandum.
3. Direct COs to verify that nomination forms and appointment memorandums are included in contracting files for all current contracts.

## **Agency Response and OIG Evaluation**

EPA concurred with both recommendations. Based on its response to the draft report and exit conference, EPA agreed to issue an Interim Policy Notice that will require that the contract files include COR appointment memorandums and require COs to verify that both COR nomination forms and appointment memorandums are included in all current contracts. EPA indicated the Interim Policy Notice will be issued by September 30, 2012.

The Agency's response and comments at the exit conference meet the intent of the recommendations.

## Chapter 4

### EPA Miscoded Contracts

EPA contracting staff improperly coded four indefinite-delivery/indefinite-quantity (ID/IQ) task order contracts as cost-plus-fixed-fee (CPFF) contracts in EPA's contract writing system,<sup>2</sup> which updates the Federal Procurement Data System-Next Generation (FPDS-NG). The FAR requires that ID/IQ contracts be coded as "IDV" for reporting purposes in FPDS-NG. COs coded the ID/IQ contracts as CPFF contracts because the majority of the task orders were anticipated to be CPFF task orders. When contract types are miscoded, EPA does not have accurate data on the type of contracts it awards. Complete, accurate, and timely federal procurement data is essential for ensuring that the government has the right information when planning and awarding contracts and that the public has reliable data to track how tax dollars are spent.

#### **Regulations and Memorandums Require Data Integrity for Reporting Requirements on Federal Spending**

FAR Subpart 4.606 states that Indefinite Delivery Vehicles, such as the four task and delivery order contracts discussed above, should be coded as "IDV" in the FPDS-NG. In addition, the FPDS-NG User's Manual states that the contract type for Indefinite Delivery Vehicles, such as the contracts in question, should be coded as follows: "Order Dependent (IDV allows pricing arrangement to be determined separately for each order)."

The Office of Management and Budget's memorandum on Open Government states that challenges exist with the quality of federal spending information and cites inaccurate or untimely data as a challenge. The memorandum suggested that agencies take steps to ensure that data disseminated comply with applicable standards on information quality and that adequate internal controls are in place to ensure the integrity of the data released to the public.

EPA contracting offices' Quality Assessment Plans place the responsibility for data quality and integrity on the contract specialists and COs. EPA's Acquisition Handbook, Section 4.2.4.2, states that all Quality Assessment Plans must contain some mandatory activities, including contracting office verification and validation that the information in official contract files is consistent with the data in EPA's procurement systems and FPDS-NG.

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<sup>2</sup> According to the CO, the contracts were initiated in EPA's previous contracting writing system—the Integrated Contracts Management System.

## **EPA Contracting Staff Improperly Coded Contracts**

EPA provided a universe of cost-reimbursement contracts awarded between March 17, 2011, and September 30, 2011, to the OIG for analysis on whether the Agency complied with the new FAR revisions. The EPA CO improperly coded four ID/IQ contracts as CPFF contracts because the majority of the task orders to be issued were anticipated to be CPFF task orders. In reviewing the contract language for EPA contracts EPC11036, EPC11037, EPC11038, and EPC11039, we found language identifying them as ID/IQ contracts.

In discussing our results with EPA staff, they pointed out that the FPDS-NG User's Manual contains conflicting guidance regarding coding of contracts. For example, paragraph 4.8.1 of the manual states that if a contract has more than one contract type, agencies should identify the type with the greater contract value. The manual also states that agencies should follow their own instructions if they report multiple actions. However, the same section in the manual identifies a contract type value of "Order Dependent (IDV allows pricing arrangement to be determined separately for each order)." This allows an agency to identify the pricing data (e.g., cost-reimbursement, fixed-price) for each order it places under a contract.

## **Recommendation**

We recommend that the Assistant Administrator for Administration and Resources Management:

4. Develop and distribute instructions on coding of ID/IQ contracts. EPA should ensure that the four contracts identified in this finding are coded consistent with the instructions.

## **Agency Response and OIG Evaluation**

EPA concurred with our recommendation. EPA indicated it will publish a flash policy notice advising staff that ID/IQ contracts should be coded in the FPDS in accordance with the FPDS Government User's Manual dated April 2011. EPA said it will issue the flash policy notice by March 31, 2012.

The Agency's response and comments at the exit conference meet the intent of the recommendation.

## **Status of Recommendations and Potential Monetary Benefits**

RECOMMENDATIONS						POTENTIAL MONETARY BENEFITS (in \$000s)	
Rec. No.	Page No.	Subject	Status <sup>1</sup>	Action Official	Planned Completion Date	Claimed Amount	Agreed-To Amount
1	7	Develop a policy for COs that provides guidance on preparing written acquisition plans that comply with the FAR revisions resulting from the interim rule (FAR Case 2008-030).	O	Assistant Administrator for Administration and Resources Management	03/31/12		
2	10	Update the procurement initiation notice as contained in the CMM to include, as an attachment, a copy of the COR appointment memorandum.	O	Assistant Administrator for Administration and Resources Management	09/30/12		
3	10	Direct COs to verify that nomination forms and appointment memorandums are included in contracting files for all current contracts.	O	Assistant Administrator for Administration and Resources Management	09/30/12		
4	12	Develop and distribute instructions on coding of ID/IQ contracts. EPA should ensure that the four contracts identified in this finding are coded consistent with the instructions.	O	Assistant Administrator for Administration and Resources Management	03/31/12		

<sup>1</sup> O = recommendation is open with agreed-to corrective actions pending  
 C = recommendation is closed with all agreed-to actions completed  
 U = recommendation is unresolved with resolution efforts in progress

## ***Agency Response***

February 9, 2012

### **MEMORANDUM**

**SUBJECT:** Response to Draft Audit Report: Policies Needed for Proper Use and Management of Cost-Reimbursement Contracts Based on Duncan Hunter Act, Project N. OA-FY-11-0563

**FROM:** Craig E. Hooks, Assistant Administrator  
Office of Administration and Resources Management

**TO:** Melissa M. Heist, Assistant Inspector General for Audit  
Office of the Inspector General

Thank you for the opportunity to comment on the draft report entitled “Policies Needed for Proper Use and Management of Cost-Reimbursement Contracts Based on Duncan Hunter Act” dated January XX, 2012. Our comments on the report and recommendations are below:

### **Recommendations and Responses:**

**Recommendation 1: Develop a policy to ensure compliance with the new Federal Acquisition Regulations (FAR) revisions resulting from the interim rule (FAR Case 2008-030).**

**Response:** OAM concurs with this recommendation. On March 17, 2011, the Policy, Training, and Oversight Division (PTOD) of the Office of Acquisition Management (OAM) published information and implementation guidance on FAR Case 2008-030. In order for OAM to hold agency contracting and management staff accountable for understanding and implementing such regulatory changes, OAM has included review and evaluation of the proper use and management of cost-reimbursement contracts in the self-assessment and peer review checklists under OAM’s Balanced Scorecard Performance Measurement and Management Plan (PMMP). Under the PMMP, OAM Divisions and Regional Acquisition Offices will perform reviews using the self-assessment checklist to ensure compliance. The OAM Contract Management Assessment Team will perform reviews of these organizations to verify and validate internal review and compliance results.

**Recommendation 2: Update the procurement initiation notice checklist as contained in the Contracts Management Manual (CMM) to include, as an attachment, a copy of the Contracting Officer Representative (COR) appointment memorandum.**

**Response:** OAM concurs with this recommendation. EPA's Acquisition System (EAS) allows COR nominations to be accomplished electronically in the requisition document. OAM will publish an Interim Policy Notice (IPN) requiring program and technical staff to nominate prospective COR's in EAS requisition documents.

**Recommendation 3: Direct COs to verify that nomination forms and appointment memorandums are included in contracting files for all current contracts.**

**Response:** OAM concurs with this recommendation, and the above-described IPN will require the "Nomination of the Contracting Officer's Representative (COR)" form be included in the official contract file in accordance with FAR 4.803(a)(33).

**Recommendation 4: Develop and distribute instructions on coding of ID/IQ contracts. EPA should ensure that the four contracts identified in this finding are coded consistent with the instructions.**

**Response:** OAM concurs with this recommendation. OAM will publish a flash policy notice advising staff that ID/IQ contracts should be coded in the Federal Procurement Data System (FPDS) in accordance with the FPDS Government User's Manual dated April 2011. Accordingly, if cost-type orders are anticipated to be the greater contract value, the contract file shall contain either an acquisition plan or analysis explaining why cost-type pricing is appropriate to support the requirement, as well as include a discussion on future plans to minimize the use of cost-type orders in accordance with FAR Part 16. OAM will also ensure the files for the contracts identified in the report contain either the required plan or analysis.

Please contact John Bashista, Director of OAM, if you have any questions regarding the above responses.

## ***FAR Revisions and Results of File Reviews***

FAR	Revised language	Yes	No
16.103(d) (1)(i)	Explain why the contract type selected must be used to meet the agency need.	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.103(d) (1)(ii)	Discuss the Government's additional risks and the burden to manage the contract type selected ( <i>e.g.</i> , 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-	EPW11029	EPC11046 EPD11006 EPD11060 EPD11073 EPW11043 EPW11044
16.103(d) (1)(ii)(A)	How the Government identified the additional risks ( <i>e.g.</i> , pre-award survey, or past performance information);	EPW11029	EPC11046 EPD11006 EPD11060 EPD11073 EPW11043 EPW11044
16.103(d) (1)(ii)(B)	The nature of the additional risks ( <i>e.g.</i> , 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	EPW11029	EPC11046 EPD11006 EPD11060 EPD11073 EPW11043 EPW11044
16.103(d) (1)(ii)(C)	How the Government will manage and mitigate the risks.	EPC11046 EPW11029	EPD11006 EPD11060 EPD11073 EPW11043 EPW11044
16.103(d) (1)(iii) <sup>1</sup>	Discuss the Government resources necessary to properly plan for, award, and administer the contract type selected ( <i>e.g.</i> , resources needed and the additional risks to the Government if adequate resources are not provided).		EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044

<sup>1</sup> Similar language revisions regarding adequacy of resources were included in FAR 16.103(d)(1)(iv)(C) and 16.301-3(a)(4).

FAR	Revised language	Yes	No
16.103(d)(1)(iv) <sup>2</sup>	For other than a firm-fixed price contract, at a minimum the documentation should include-	EPC11046 EPD11006 EPD11060	
16.103(d)(1)(iv)(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;	EPD11073 EPW11029 EPW11043 EPW11044	
16.103(d)(1)(iv)(B)	Rationale 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;	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.103(d)(1)(iv)(D) <sup>3</sup>	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.		EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044
16.103(d)(1)(v)	A discussion of why a level-of-effort, price redetermination, or fee provision was included.	EPC11046 EPD11006 EPD11060 EPD11073 EPW11043 EPW11044	EPW11029
16.301-2(a)(1)	The contracting officer shall use cost-reimbursement contracts only when—  Circumstances do not allow the agency to define its requirements sufficiently to allow for a fixed-price type contract (see 7.105); or	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.301-2(a)(2)	Uncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy to use any type of fixed-price contract.	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.301-3(a)(1)	A cost-reimbursement contract may be used only when-  The factors in 16.104 have been considered;	Addressed below for FAR 16.104	

<sup>2</sup> Similar language revisions regarding documenting why a particular contract type was selected were included in FAR 7.103(d), 7.105(b)(3), and 16.301-2(b).

<sup>3</sup> Similar language revisions regarding transitioning to firm-fixed-price contracts to the maximum extent practicable were included in FAR 7.105(b)(5)(iv).

FAR	Revised language	Yes	No
16.301-3(a)(2) <sup>4</sup>	A written acquisition plan has been approved and signed at least one level above the contracting officer;	EPW11043	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11044
16.104(a)	There are many factors that the contracting officer should consider in selecting and negotiating the contract type. They include the following:  Price Competition	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.104(b)	Price Analysis	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.104(c) <sup>5</sup>	Cost Analysis	EPC11046 EPD11006 EPD11060 EPW11029 EPW11043 EPW11044	
16.104(d)	Type and complexity of the requirement	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.104(e)	Combining contract types		EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044
16.104(f)	Urgency of the requirement		EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044

<sup>4</sup> Similar language revisions requiring a written acquisition plan approved one level above the CO were included in FAR 16.301-2(b), 7.103(e), and 7.103(j).

<sup>5</sup> We determined that a cost analysis for contract EPD11073 was not required as this was a competitive proposal process.

<b>FAR</b>	<b>Revised language</b>	<b>Yes</b>	<b>No</b>
16.104(g)	Period of performance or length of production run	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.104(h)	Contractor's technical capability and financial responsibility	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.104(i) <sup>6</sup>	Adequacy of the contractor's accounting system	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.104(j)	Concurrent contracts	EPW11043	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11044
16.104(k)	Extent and nature of proposed subcontracting	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
16.104(l)	Acquisition history	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
7.103(f)	Ensuring that the statement of work is closely aligned with performance outcomes and cost estimates.	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	

<sup>6</sup> Similar language revisions regarding the adequacy of the contractor's accounting system were included in FAR 16.301-3(a)(3) and 42.302(a)(12).

FAR	Revised language	Yes	No
1.602-2(d)  1.602-2(d)(6) <sup>7</sup>	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 must be designated in writing, with copies furnished to the contractor and the contract administration office-	EPC11046 EPW11029	EPW11043 EPD11073 EPW11044 EPD11006 EPD11060
1.602-2(d)(6)(i)	Specifying the extent of the COR's authority to act on behalf of the contracting officer;	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
1.602-2(d)(6)(ii)	Identifying the limitations on the COR's authority;	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
1.602-2(d)(6)(iii)	Specifying the period covered by the designation;	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
1.602-2(d)(6)(iv)	Stating the authority is not redelegable; and	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
1.602-2(d)(6)(v)	Stating that the COR may be personally liable for unauthorized acts.	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	
1.604	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-	EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	

<sup>7</sup> Similar language revisions regarding nominating a COR were included in FAR 7.104(e) and 16.301-3(a)(4)(i).

FAR	Revised language	Yes	No
1.604(a)	A copy of the contracting officer's letter of designation and other documents describing the COR's duties and responsibilities;	EPC11046 EPW11043 EPD11060	EPD11006 EPW11029 EPW11044 EPD11073
1.604(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		EPC11046 EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044
1.604(c) <sup>8</sup>	Documentation of COR actions taken in accordance with the delegation of authority.	EPD11006 EPD11060 EPD11073 EPW11029 EPW11043 EPW11044	

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<sup>8</sup> No actions on contract EPC11046 had been taken at the time of our review.

## ***Distribution***

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