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BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The Secretary Of Energy

DOE Should Strengthen Its Controls Over Award Fees To Contractors

The Department of Energy hires contractors to run its government-owned, energy- and defense-related research and production facilities. DOE furnishes the plants and equipment, pays employee salaries, and provides the contractors with working capital through letters of credit. Most contractors also receive a fee for their services. DOE favors using award-fee contracts, where the fee amount partially depends on the quality of the contractor's performance.

In 1982, six DOE field offices administered 25 award-fee contracts totaling almost \$2.8 billion and paid these contractors about \$58 million in fees.

GAO concludes that DOE needs to improve its guidance and practices for calculating allowable fees. DOE also needs to expand its periodic reviews of field offices' procurement operations to include evaluations of how field offices are determining fee amounts.



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RESOURCES, COMMUNITY,
AND ECONOMIC DEVELOPMENT
DIVISION

B-208076

The Honorable Donald Hodel
The Secretary of Energy

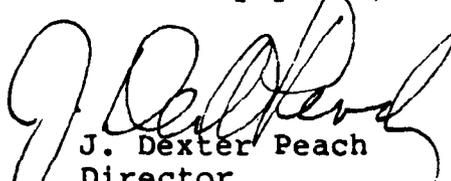
Dear Mr. Secretary:

This report presents the results of our evaluation of the Department of Energy's policies and procedures for determining available fees to contractors working for the Department under cost-plus-award-fee contracts.

This report contains recommendations to you on page 12. As you know, 31 U.S.C. §720 requires the head of a federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Chairmen, House and Senate Committees on Appropriations, House Committee on Government Operations, Senate Committee on Governmental Affairs, House Committee on Energy and Commerce, Senate Committee on Energy and Natural Resources, and the House and Senate Committees on Armed Services. We are also sending copies of the report to your Office of the Controller and the Director, Office of Management and Budget. We will make copies available to other interested parties upon request.

Sincerely yours,



J. Dexter Peach
Director

D I G E S T

The Department of Energy (DOE) hires contractors to operate and provide services to its government-owned, energy- and defense-related research and production facilities. DOE furnishes all plants and equipment, pays all employee salaries, and provides day-to-day working capital to the contractors through letters of credit. The contracts are managed by DOE's field offices, principally its operations offices, located throughout the country.

Some DOE contractors are reimbursed for their costs only and receive no fees or profit, but most contractors receive fees. DOE uses two basic types of fee contracts--cost-plus-fixed-fee, where the fee amount is agreed upon when the contract is awarded, and cost-plus-award-fee, where the fee partially depends on the quality of the contractor's performance. DOE favors using award-fee contracts because it believes such contracts provide the best incentive for good performance.

Six of DOE's eight operations offices use award-fee contracts. In fiscal year 1982, these offices administered 25 award-fee contracts totaling almost \$2.8 billion and paid these contractors about \$58 million in fees. On August 1, 1983, DOE revised the schedules and procedures it uses to calculate the maximum fees available to contractors. This was the first adjustment to its fee schedules in about 20 years. DOE estimated that if the revised fee schedules had been in effect in 1982 the fees available to contractors could have been about 48 percent higher. According to DOE, the fees available under the revised fee schedule are about equal to the value of fee dollars in 1972 after considering the effects of inflation.

GAO reviewed three operations offices' practices for computing the amounts of award fees on 6 of the 25 award-fee contracts. GAO concluded that DOE needs to improve both its guidance and its practices for calculating allowable fees for award-fee contracts. DOE

also needs to expand the scope of its periodic headquarters procurement reviews of operations office procurement activities to ensure that these offices properly calculate allowable fees.

DOE'S GUIDANCE AND PRACTICES
FOR COMPUTING ALLOWABLE AWARD
FEES NEED IMPROVEMENT

DOE's procurement regulations and procurement handbook provide guidance to operations offices to assist them in negotiating allowable fees on award-fee contracts. DOE headquarters procurement review teams provide additional guidance during periodic reviews of operations offices' procurement activities.

GAO found several instances where operations offices did not comply with procurement guidance. This occurred because the guidance was unclear and/or operations offices wanted to increase the fees contractors could be paid. For example

--DOE guidance permits paying fees to contractors for procuring special equipment in addition to the cost of the equipment. However, the guidance does not clearly define what special equipment is. As a result, the three operations offices included in GAO's review were inconsistent in calculating allowable fees for special equipment. (See p. 6.)

--DOE guidance requires a reduction in maximum allowable fees when 45 percent or more of the work under a contract is to be subcontracted. One operations office did not make the required reduction on two contracts GAO reviewed because it believed that DOE's fees did not provide fair and reasonable compensation to the contractors. (See p. 8.)

In an August 1982 study of its fee policies, which led it to revise its fee schedules, DOE also found that operations offices were using "innovative methods," contrary to existing procurement guidelines, to increase available fees. While the study does not comment on how widespread the use of these "innovative

methods" is, it appears that the examples GAO found may not be isolated occurrences.

Clear guidance, and adherence to that guidance, on appropriate procedures for computing maximum available fees and setting fee negotiating objectives is always important. It is especially important now that DOE has increased the ceilings on allowable fees.

DOE NEEDS TO EXPAND PROCUREMENT
REVIEWS TO ENSURE COMPLIANCE WITH
FEE POLICIES

Over a number of years, DOE headquarters procurement review teams are expected to assess all significant aspects of each operations office's procurement operation. Determining appropriate available fees is but one small part of the review. GAO found, however, that procurement reviews conducted in fiscal year 1982 at three operations offices were not conducted in sufficient depth to detect the instances of noncompliance and inconsistent interpretation of procurement guidance discussed above. (See p. 10.)

RECOMMENDATIONS TO THE
SECRETARY OF ENERGY

GAO recommends that, for award-fee contracts, the Secretary of Energy

--clarify guidance for calculating fee negotiation objectives to help eliminate inconsistent practices among operations offices and

--include evaluations of how operations offices compute fee bases and maximum available fees in headquarters reviews of operations offices' procurement activities.

COMMENTS OF RESPONSIBLE AGENCY
OFFICIALS

GAO obtained oral comments from DOE's Director, Procurement and Assistance Management, and members of his staff. These officials agreed with GAO's conclusions and recommendations and stated that they are taking steps to clarify procurement guidance, monitor operations offices' calculations of allowable fees, and include occasional in-depth reviews of

fee-setting practices in their periodic reviews of operations offices' procurement activities.

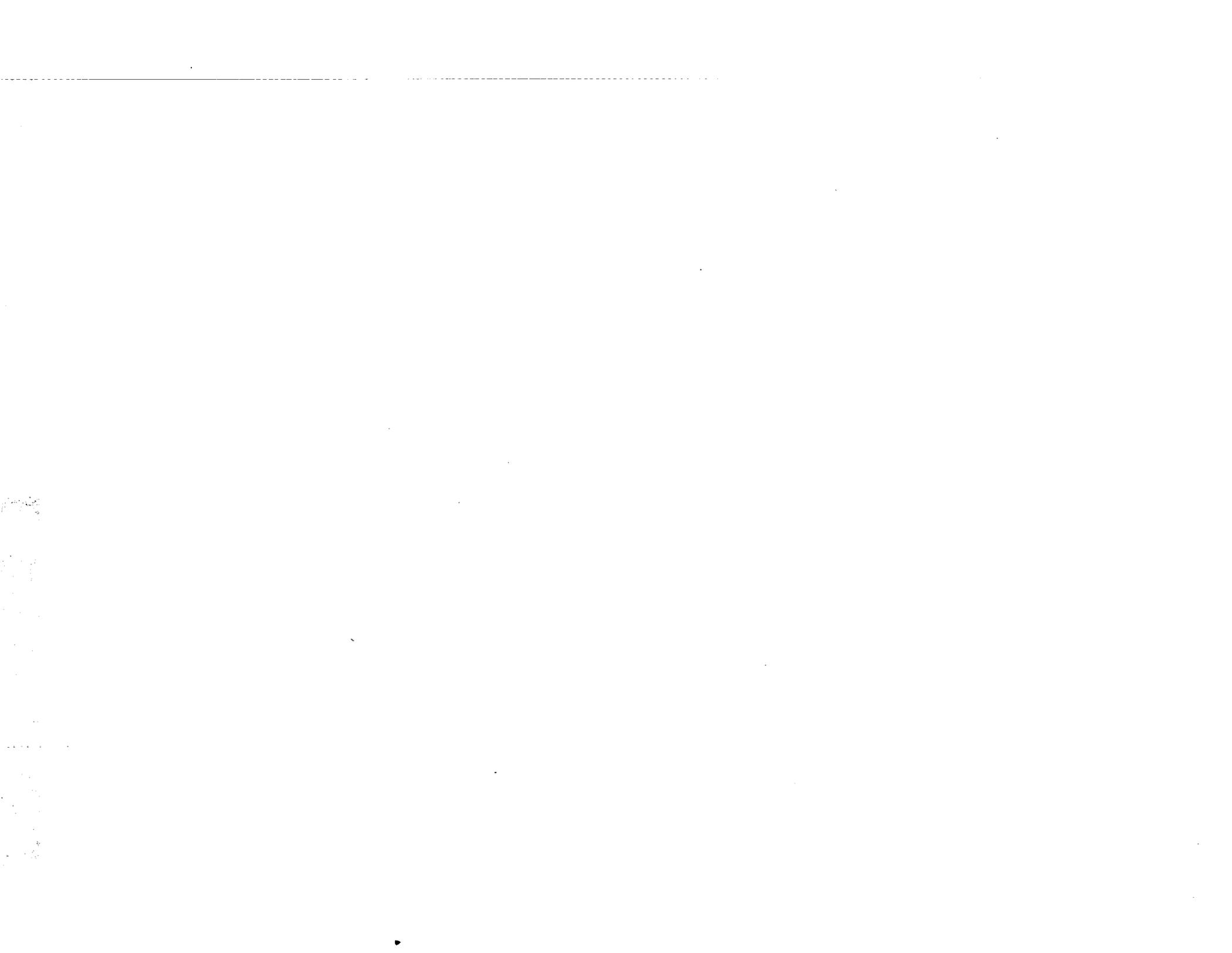
These officials also suggested that the report recognize (1) that the new fee schedules are the first changes in the fee schedules in about 20 years and (2) the broad nature of periodic DOE headquarters reviews of operations offices' procurement activities. GAO changed its report as it believed appropriate to reflect these suggestions.

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ABBREVIATIONS

DOE	Department of Energy
GAO	General Accounting Office



CHAPTER 1

INTRODUCTION

To carry out its many energy- and defense-related missions, the Department of Energy (DOE) has a large network of research and production facilities, including 12 multiprogram national laboratories, 31 specialized laboratories, and 13 nuclear material and weapons production facilities. The facilities are all government-owned; but, most are operated by corporations, universities, or nonprofit contractors. The facilities represent an investment of about \$15 billion and provide employment to over 100,000 people. Most of these contractors are directed and controlled by eight DOE operations offices. The operations offices are located in Oak Ridge, Tennessee; Savannah River, South Carolina; Chicago, Illinois; Albuquerque, New Mexico; San Francisco, California; Las Vegas, Nevada; Idaho Falls, Idaho; and Richland, Washington.

DOE headquarters allows each operations office to select the most appropriate contract type for the work to be performed. DOE operations offices used four basic types of cost-reimbursable contracts in fiscal year 1982 to secure 49 contractors to operate and provide services to its government-owned facilities. Twenty-five contracts were cost-plus-award-fee. Award-fee contracts contain special provisions that permit DOE to adjust the fees paid to the contractors--increasing them for high-quality performance and reducing them for low-quality performance. Eight contracts were cost-plus-fixed-fee, including one contract with E.I. DuPont DeNemours & Co. for operating the Savannah River Reservation at cost plus \$1. Fixed-fee contracts provide for payment of a fee that, once negotiated, is fixed and cannot be adjusted to reflect performance quality. Eleven contracts were cost-plus-no-fee contracts with universities, institutes, and a private corporation--Western Electric Company. The remaining five contracts were cost-plus-management-allowance contracts with universities. These contracts do not permit payment of fee but do provide for payment of a negotiated contract management-related allowance in addition to full reimbursement of contract costs.

DOE favors using award-fee contracts when it must pay fees because it believes such contracts provide the best incentives for motivating contractors. DOE has been converting existing fixed-fee contracts to award fee whenever possible. Currently, six of DOE's eight operations offices administer award-fee contracts. In fiscal year 1982, the 25 award-fee contractors had operating budgets of almost \$2.8 billion and were paid fees of about \$58 million, or about 2 percent of the contractors' operating budgets.

Award-fee contracts have two fee parts--a base fee and an award fee. The base fee is a fixed amount paid to the contractor. The award fee, however, varies depending upon the quality

of the contractor's performance. It may range from nothing, for poor performance, to the maximum available fee negotiated, for outstanding performance.

The amount of the award fee is determined by DOE operations office officials who evaluate the contractor's performance against criteria DOE established and furnished to the contractor. These evaluations are usually made, and a portion of the award fee paid, several times during the year. In fiscal year 1982, the award-fee contractors earned almost \$19.6 million in base fees and more than \$38.8 million in award fees. The \$38.8 million represented about 83 percent of the approximately \$47 million maximum award fees available to the contractors.

On August 1, 1983, DOE revised the estimated schedules and procedures it uses to calculate the maximum fee payable for a given cost of work. The Director, Procurement Assistance and Management, said that this was the first change to DOE's fee schedules in about 20 years. Had these new fee schedules been in effect in 1982, according to DOE's estimates, its contractors could have been paid as much as 48 percent more in fees. The Director pointed out, however, that after considering the effects of inflation over the last 20 years, this change equates to the value of fee dollars in about 1972.

OBJECTIVES, SCOPE, AND METHODOLOGY

Our objective was to determine whether DOE's operations offices were negotiating fair and reasonable fees for award-fee contracts. To accomplish this objective, we examined DOE's

- procurement guidance for award-fee contracts,
- operations offices' compliance with this guidance, and
- Procurement and Assistance Management Directorate's oversight of the fee-setting process.

We evaluated compliance with headquarters guidance at the Albuquerque, Idaho Falls, and Richland operations offices by reviewing the two largest award-fee contracts at each operations office. Our reviews consisted of comparing the contracts and records of contract negotiations with DOE's procurement regulations and supplementing guidance for implementing these regulations. In addition, we discussed the contracts, negotiation records, and apparent discrepancies with procurement officials.

The six contracts we reviewed involved about 48 percent of the almost \$2.8 billion total contract costs and about 43 percent of the \$58 million in fees paid for the 25 award-fee type contracts administered in fiscal year 1982.

DOE Award-Fee Contracts Selected for Review

<u>Operations office/ contractor</u>	<u>Total fee base (cost)</u>	<u>Maximum available fee</u>
	----- (millions) -----	
<u>Albuquerque</u>		
The Bendix Corporation	\$430.6	\$5.7
Rockwell International Corporation	251.5	6.3
<u>Idaho Falls</u>		
E G & G Idaho, Inc.	170.0	3.9
Exxon Nuclear Idaho Company	59.5	2.4
<u>Richland</u>		
Rockwell Hanford Operations	230.2	5.7
Westinghouse Hanford Company	195.0	4.4

We also interviewed DOE headquarters procurement officials to determine the procedures for and the scope of headquarters reviews of operations offices' compliance with DOE procurement policies. In addition, we reviewed the reports these officials prepared as a result of their compliance reviews to determine if the headquarters reviews included evaluations of how operations offices were computing award fees.

Our audit was performed in accordance with generally accepted government auditing standards.

CHAPTER 2

DOE'S GUIDANCE AND PRACTICES CONCERNING COST-PLUS-AWARD-FEE CONTRACTS NEED IMPROVEMENT

DOE headquarters provides its operations offices with procurement guidance to help them negotiate fees on award-fee contracts. The principal guidance is contained in the procurement regulations and DOE's procurement handbook Establishing and Negotiating Fee and Profit. DOE headquarters procurement teams provide further guidance during their periodic reviews of operations offices' procurement activities.

The guidance contained in the regulations and handbook is often unclear or incomplete. As a result, operations offices' procurement officials or their managers interpret the guidance on an office-by-office, or in some cases, on a contract-by-contract basis. Differing interpretations among operations offices have resulted in inconsistent fee negotiating objectives and possibly inequitable fees.

Moreover, in a number of instances, operations office officials interpreted procurement guidance in ways that would increase fees payable to contractors because they believed that fees should have been higher to provide fair and reasonable compensation. In this regard, according to DOE, the recent changes to its approximately 20-year old fee schedules will permit its operations offices to negotiate maximum allowable fees as much as 48 percent higher than the maximum allowable fees in 1982.

Periodic DOE headquarters procurement reviews generally have not been of sufficient depth to detect inconsistent fee negotiating objectives and noncompliance with procurement guidance.

PROCEDURES FOR CALCULATING ALLOWABLE FEES

Federal procurement regulations state that:

"It is the policy of the Government to procure property and services from responsible sources at fair and reasonable prices calculated to result in the lowest ultimate overall cost to the Government."

Part of this cost is the fees paid to contractors. DOE's procurement regulations state that the amounts payable as fees on contracts for operating government-owned facilities and providing onsite support and construction services will not exceed maximum amounts derived from appropriate fee schedules included in DOE's procurement handbook. The handbook contains instructions to assist procurement officials (1) calculate maximum fees and (2) negotiate fees that are consistent with DOE's procurement policies.

An essential step in preparing to negotiate a fair and reasonable price is to select a sound fee objective for each contract. The fee objective is the amount that, in the procurement official's judgment, is appropriate compensation for the tasks the contractor will perform. The fee objective guides DOE's initial negotiating position.

The fee objective is determined before negotiations begin with the contractor. Operations office officials can set the fee objective at any amount that does not exceed the maximum allowable fee set out in the fee schedules and instructions contained in DOE's procurement handbook. DOE has four fee schedules--one each for production-type operations, research and development, construction, and procurement of special equipment for construction projects.

To calculate the maximum allowable fee, the DOE handbook instructs procurement officials to first classify the total contract cost in one or more of the four fee-schedule categories. Then, for each category, they exclude the costs of those activities that require little or no management effort and thus do not warrant a fee payment. The net cost is the fee base to which rates from the appropriate fee schedules are applied to determine the maximum fees payable. The maximum fees then must be adjusted downward to reflect reduced work complexity or services expected to be subcontracted. Finally, after all net fees have been calculated, they are combined and, in the case of award-fee contracts, increased by 50 percent to calculate the maximum allowable fee. This is the maximum amount that can be paid to award-fee contractors without special approval from DOE's Director, Procurement and Assistance Management. However, operations office procurement officials do not have to offer contractors the maximum allowable fee.

OPERATIONS OFFICES FOLLOW DIVERSE
PROCUREMENT PRACTICES THAT ARE
OFTEN INCONSISTENT WITH GUIDANCE

DOE's handbook is vague with respect to adjustments that should be made to fee bases before calculating the maximum allowable fee. Vague procurement guidance has resulted in inconsistent determinations of maximum allowable fees among operations offices and occasionally within the same office. Even when guidance is clearly stated, however, operations offices sometimes interpret the guidance in ways that would increase allowable fees because they believe that contractors' fees are too low. For example, DOE cites, in the study of fee adequacy it performed and used as the basis for revising its fee schedules, instances where operation offices were using "innovative methods" to calculate fees at or near maximum authorized amounts.

We found specific examples of vague procurement guidance and misinterpretation of procurement guidance in the way that three

operations offices handled special equipment procurements, leasing costs, and adjustments to fees on construction contracts.

Operations offices were inconsistent
in treatment of special equipment

DOE's handbook states that fees may be paid to contractors procuring special equipment in conjunction with construction projects, architect-engineer services, or facility operating contracts. This fee is in addition to the cost of procuring the equipment. There is a separate fee schedule for determining allowable fees for procuring special equipment. Using this fee schedule to calculate allowable fees for procuring equipment increases the contractor's total allowable fee. The handbook does not, however, clearly define what is meant by special equipment except to say that it is equipment of a complex nature.

The Chief of the Contract Pricing Policy Branch in DOE's Procurement and Assistance Management Directorate agreed that special equipment is not defined anywhere in DOE guidance. He added that procurement officials should have a general understanding of what special equipment means. We found that this was not the case. For example, the Idaho Falls operations office did not allow special equipment fees on either of the two contracts we reviewed. According to the Chief of that office's Contract Operations Branch, purchased equipment was treated as either operating capital equipment or construction equipment but not special equipment. In contrast, the Albuquerque and Richland operations offices allowed special equipment fees not only for procurement of construction equipment but usually for capital equipment not related to construction.

Before October 1981, the Albuquerque operations office computed fees for equipment costs using the production fee schedules. Subsequently, the office changed its practice and used the fee schedule for procuring special equipment. This change increased the allowable fees under the contracts. That office's Chief, Administrative Branch, said the office made this change because office procurement officials believed the lesser amount of fee allowed by the production schedule was insufficient to provide the contractors with fair and reasonable fees. Richland's Director, Procurement Division, said that his staff used the special equipment fee schedule because they believed that the contractors procured complex equipment and were entitled to the fees provided by this schedule. These Richland and Albuquerque officials agreed the fee handbook is unclear with respect to how special equipment fee bases should be computed.

The Chief, Contract Pricing Policy Branch, in DOE's Procurement and Assistance Management Directorate told us that DOE plans to issue new guidance to operations office procurement staffs. This was recommended in the directorate's recent study of fee adequacy, which led DOE to revise its fee schedules. The study

recommended that the new guidance describe when it is appropriate to use special equipment purchase fee schedules and define the costs to be excluded from fee bases. The study also recommended that before revising the handbook, the proposed changes be evaluated and concurred with by the various DOE organizations involved in the fee process. If these recommendations are effectively carried out, much of the uncertainty that now exists should be resolved.

Operations offices treated
leasing costs differently

DOE policy is to exclude leasing costs from contract fee bases. Specifically, DOE's handbook states that the operating fee base is

". . .the estimated cost of the work, adjusted to reflect all allowable costs considered to be reasonable and necessary and, generally to exclude . . . estimated costs of land, buildings and facilities whether to be leased, purchased or constructed . . ."

However, the Albuquerque, Idaho Falls, and Richland operations offices treated leasing costs differently when estimating operating fee bases.

Richland's procurement division director said that their normal practice was to require that all leasing costs, whether DOE-negotiated or contractor-negotiated, be excluded from the fee base. Accordingly, they deducted about \$560,000 in annual leasing costs from the operating fee bases on the two contracts we reviewed.

In contrast, the Chief, Contract Finance Branch, at Idaho Falls and the Director, Contracts and Industrial Relations Division, at Albuquerque said that they included contractor-negotiated leasing costs, which totaled over \$600,000 for the two contracts reviewed at Idaho Falls and \$547,000 for the two contracts reviewed at Albuquerque, in the fee base. They said that contractors deserved to be paid fees for their services relating to negotiating and administering leases.

These Idaho Falls and Albuquerque officials said that they believed they were complying with the handbook because it only states that lease costs are generally excluded. However, the Richland and Albuquerque officials also said that the handbook could be clearer regarding the exclusion of lease costs.

Operations offices did not always
observe guidance requiring adjustments
to construction contract fees

DOE's handbook instructs procurement officials to exclude certain costs from construction fee bases, such as contingency

and engineering allowances, and to reduce the maximum calculated construction fees for factors such as excessive subcontracting. Specifically, DOE's handbook advises procurement officials that:

"The fee base on which a fee percentage is to be applied is the adjusted estimated cost of construction. . . . Exclude the cost of land, cost of engineering, contingency allowance and estimated prime contractor's fee."

However, we found instances where operations offices did not follow these instructions. In these cases, the calculated maximum fees were inflated for the contractors and may have resulted in paying inappropriately high fees.

Engineering and contingency allowances
were not always excluded

At the Richland operations office, engineering and contingency allowances were excluded from the fee base of one contract we reviewed but not from the other. The Chief, Contracts Management Branch, said that this occurred because different divisions computed the fee bases, the divisions used different practices, and the divisions were unaware that they were computing contractor's construction fee bases differently.

The Deputy Manager and other officials of the Albuquerque operations office said that engineering and contingency allowances were included in the fee bases of both contracts we reviewed because the contractors managed the work and deserved a fee. One of the two contracts we reviewed at the Idaho Falls operations office also included a construction fee base. According to that office's procurement branch chief, the office excluded engineering and contingency allowances from that fee base. We could not confirm that the exclusions were actually made, however, because procurement officials did not exclude specific amounts for these costs. Instead, they excluded a lump-sum amount that they estimated was sufficient to include all required deductions. The procurement branch chief told us that procurement officials estimated the amount to reduce the fee, rather than follow the instructions in the DOE handbook, because they were very busy and DOE's procedures required time-consuming calculations.

Excessive subcontracting costs
were not always excluded

DOE's handbook instructs procurement officials using construction fee schedules to adjust fees downward to reflect factors such as reduced work complexity and excessive subcontracting. Specifically, the handbook states:

"If an excessive amount of work is to be subcontracted, some downward adjustment in the prime contractor's fee will be necessary to reflect the reduction in services required."

The handbook describes subcontracting over 45 percent of the contract work as excessive and provides detailed instructions describing how officials should compute necessary fee adjustments.

On the two contracts we reviewed at the Richland operations office, procurement officials reduced the maximum available construction management fees of about \$1.6 million by more than \$500,000 to account for excessive subcontracting--about 87 and 95 percent of the contract construction work--and reduced work complexity. On the other hand, Albuquerque and Idaho Falls operations office officials did not always comply with the instructions.

A contract specialist in the Idaho Falls operations office said that the lump-sum reduction from the fee base for construction was also intended to account for any excessive subcontracting. Because of this, procurement officials did not specifically determine if subcontracting to be performed under the contract would meet the excessive subcontracting criterion.

Maximum available construction management fees of about \$630,000 were not reduced on the two contracts we reviewed at the Albuquerque operations office. Although the two contracts contained provisions requiring the operating contractors to subcontract 100 percent of the construction work, the Albuquerque operations office did not reduce the maximum calculated construction management fees for subcontracting in excess of 45 percent. Instead, after determining the fee bases, the operations office calculated maximum allowable fees and submitted them to the contractors as the government's initial fee proposals without adjusting the amounts downward. Documentation in the contract files reported that the contractors agreed to the proposed maximum allowable fees and that "Due to travel fund restrictions there were no formal meetings with the contractor."

In commenting on this example, the Director of Albuquerque's Contracts and Industrial Relations Division said judgment must be used in applying the handbook instructions for calculating allowable construction management fees. He said that he believes operating contractors are expected to bring more engineering and administrative effort to the construction work than is expected of construction contractors and subcontractors. Furthermore, he said that fee adjustment provisions only apply to construction contractors and not to operating contractors assigned construction management responsibilities.

However, the Chief of DOE's Contract Pricing Branch in the Procurement and Assistance Management Directorate told us that if an operations office elects to compute operating contractors fees using the construction fee schedule, it must follow DOE's hand-book instructions for computing construction fees, including reducing fees for excessive subcontracting, where applicable.

DOE headquarters found that operations offices used "innovative methods" to calculate fees at or near maximum amounts

On several occasions during our review management and procurement officials of the three operations offices we visited told us that they generally believe their contractors have not been receiving fair and reasonable fees for the work they perform. DOE Procurement and Assistance Management Directorate officials are aware of these views and of procurement officials' practices to increase allowable fees.

For example, the fee study done by DOE's Procurement and Assistance Management Directorate reported that operations office procurement officials were using "innovative methods" to increase available fees. According to the study, methods used to increase available fees included

- Allocating the estimated contract cost to more than one fee schedule. This keeps the total estimated cost assigned to any one fee schedule low where the fee rate is higher.
- Calculating the fee base on an annual, rather than contract life, basis. This keeps the estimated contract cost closer to the beginning of the fee schedule where the fee rate is higher.
- Considering additional assigned work as new work. In this way, the allowable fee is calculated on the basis of the beginning of the fee schedule where the fee rate is higher.
- Including costs other than those incurred directly by the contractor in the fee base.

The study did not give details, present specific examples, or comment on how widespread the use of these "innovative methods" was. It appears, however, that the examples discussed above may not be isolated occurrences.

MORE IN-DEPTH PROCUREMENT REVIEWS
NEEDED TO CORRECT INCONSISTENCIES IN
ESTABLISHING FEE OBJECTIVES

The Procurement and Assistance Management Directorate's Office of Procurement Review periodically evaluates all

significant aspects of procurement operations at each operations office. However, these reviews have not included evaluations of the detailed calculations that operations offices use to establish fee objectives in sufficient depth to detect the inconsistent and possibly inequitable practices we have discussed.

About every 2 or 3 years, according to the Acting Director of Procurement Management Review, review teams assess each operations office's procurement operations to (1) measure the effectiveness and efficiency of the DOE procurement process, (2) promote consistent application of policy, and (3) cross feed information and ideas among field locations and headquarters to enhance the overall procurement process. Over a number of years, these procurement reviews are expected to cover all significant aspects of the procurement operation, such as organization, management, staffing, career development, policies and procedures, contracting authority, and pricing. Not all of these aspects are covered in each review.

In 1982, the Office of Procurement Review assessed procurement operations at the Albuquerque, Idaho Falls, and Richland operations offices. The Acting Director of Procurement Management Review told us that review teams had included only limited evaluations of the fee-setting practices of these operations offices. He added that the overall fee-pricing systems were evaluated to assure that a pricing system existed and reviews and documentation were appropriate. However, the reviewers did not examine such details as how fee bases were computed because review staffs were shorthanded. Finally, he said that because of limited staffing, review teams generally reviewed procurement systems and only evaluated details when reviewing officials believed there was an important reason to do so.

CONCLUSIONS

We found instances where operations office procurement officials did not comply with instructions contained in DOE's procurement regulations and procurement handbook. In some cases, this noncompliance was caused by unclear handbook instructions. In other instances, it was caused by procurement officials who did not follow the instructions either because they believed contractors deserved larger fees or because following instructions was too time-consuming.

Procurement officials generally believed that the fee schedules in effect before August 1, 1983, did not provide adequate compensation to contractors because the schedules had not been adjusted for about 20 years. Therefore, some of them developed what DOE characterizes as "innovative methods" to increase fees. These methods include allocating the cost of work to the highest fee rate portions of the fee schedules, interpreting procurement guidance in ways that increase amounts included in fee bases, and not following guidance prescribing downward adjustments in calculated maximum fees. In other instances, operations offices made

interpretations that apparently were not motivated by a desire to increase fees, rather by the vagueness of the instructions.

DOE headquarters routine procurement reviews of operations offices' procurement practices did not identify the non-compliance with procurement guidelines for calculating maximum allowable fees because the reviews were not of sufficient depth. Headquarters procurement review officials attributed this oversight to lack of sufficient staff.

Procurement officials need clear guidance regarding the appropriate procedures to follow in computing maximum fees and setting fee objectives. Clear guidance can improve procurement performance in establishing fee objectives and negotiating fair and reasonable contract prices. Moreover, this is especially important now that DOE has revised its fee schedules to permit larger maximum allowable fees.

Furthermore, in view of the new fee schedules permitting calculation of higher maximum allowable fees, DOE headquarters procurement reviews should be expanded to include evaluations of how operations offices are computing fee bases and maximum available fees.

RECOMMENDATIONS TO THE SECRETARY OF ENERGY

We recommend that, to aid DOE procurement officials in establishing fee objectives for negotiating award-fee contracts that will produce fair and reasonable prices and the lowest ultimate overall cost to the government, the Secretary of Energy

- clarify guidance for calculating fee negotiation objectives to help eliminate inconsistent practices among operations offices and
- include evaluations of how operations offices compute fee bases and maximum available fees in Procurement Management and Assistance Directorate reviews of operations offices' procurement activities.

COMMENTS OF RESPONSIBLE AGENCY OFFICIALS

We obtained oral comments from DOE's Director, Procurement and Assistance Management, and members of his staff. These officials agreed with our conclusions and recommendations and stated that they are taking steps to clarify procurement guidance, monitor operations office calculations of allowable fees, and include occasional in-depth reviews of fee-setting practices in their periodic reviews of operations offices' procurement activities.

These officials also suggested that our report recognize that DOE's August 1, 1983, changes to its fee schedules and procedures represent the first revision to the fee schedules in about 20 years. Finally, they suggested that the discussions of the periodic DOE headquarters procurement reviews be revised to better reflect the broad nature of these reviews. We changed our report as we believed appropriate to reflect these suggestions.

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