

June 2009

# CONTRACT MANAGEMENT

## Minimal Compliance with New Safeguards for Time-and- Materials Contracts for Commercial Services and Safeguards Have Not Been Applied to GSA Schedules Program



GAO

Accountability \* Integrity \* Reliability



Highlights of [GAO-09-579](#), a report to congressional committees

## Why GAO Did This Study

Federal agencies have used time-and-materials (T&M) contracts to purchase billions of dollars in services. These contracts are risky because the government bears the risk of cost overruns. Effective February 2007, the Federal Acquisition Regulation (FAR) was revised, pursuant to a statutory change, to allow T&M contracts to be used to acquire commercial services under FAR Part 12, which uses a streamlined procurement process. Certain safeguards were included in FAR Part 12, including a requirement that contracting officers prepare a detailed determination and findings (D&F) that no other contract type is suitable. Based on a mandate to review the use of T&M contracts for commercial services, we assessed (1) agencies' reported use of such contracts and what they acquired, (2) the degree to which agencies complied with the new safeguards, and (3) the applicability of the safeguards to General Services Administration (GSA) schedule contracts. GAO reviewed contracts and orders at DOD and civilian agencies and spoke with contracting officials.

## What GAO Recommends

GAO recommends that OFPP take steps to clarify the FAR regarding labor-hour contracts and to explicitly apply the Part 12 safeguards to the GSA schedules program, and that it provide guidance to contracting officials on the Part 12 D&F. In oral comments, OFPP agreed with our recommendations. The other six agencies in our review also concurred or had no comment.

View [GAO-09-579](#) or [key components](#).  
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## CONTRACT MANAGEMENT

### Minimal Compliance with New Safeguards for Time-and-Materials Contracts for Commercial Services and Safeguards Have Not Been Applied to GSA Schedules Program

#### What GAO Found

From February 2007 to December 2008, agencies reported using commercial item procedures under FAR Part 12 to buy a variety of services through T&M contracts; examples include emergency nursing services on Indian reservations and gunsmith services for the FBI. The reported value of these contracts was \$4.4 billion—or less than 1 percent of the total federal dollars obligated for services during this period. Of the \$4.4 billion, \$3.1 billion had gone through GSA's schedules program. GAO identified about another \$6 billion, in addition to the \$3.1 billion, in T&M obligations for commercial services under GSA schedule contracts. The reliability of the data reported as T&M contracts using FAR Part 12 procedures is questionable. Of the 149 contracts GAO reviewed, 28 had been miscoded as acquiring commercial services or as T&M contracts. Another issue that indicates a potential underreporting of T&M contracts for commercial services is that contracting officials across the agencies had the mistaken impression that the fixed labor rate in T&M contracts makes these contracts fixed-price. GAO raised this issue with officials from the Office of Federal Procurement Policy (OFPP)—chair of the federal acquisition regulatory council—who agreed that clarification on what constitutes a fixed-price versus labor hour contract would be beneficial. Further, GAO found that contracting officials had different opinions of what generally constitutes a commercial service. Some viewed services intended to meet a specific government requirement as noncommercial, while others viewed similar services as commercial.

The Part 12 D&F was rarely used for the contracts GAO reviewed. The D&F must incorporate four elements, such as a description of the market research conducted. Of 82 contracts reviewed that were explicitly subject to this D&F requirement, only 5 included all the required elements, and 9 partially met the requirement. Of the remaining contracts, 33 had no D&F at all and 35 included the less stringent D&F applicable to noncommercial T&M services. GAO found a general lack of awareness of the Part 12 D&F requirement at the agencies in this review. Agencies' internal management and legal reviews generally did not detect the failure to include the D&F. OFPP officials expressed concern about the lack of compliance with the D&F requirement.

The Part 12 D&F requirement has not been applied to the GSA schedules program. GSA officials stated that the GSA Administrator has discretion about what procedures apply to the program. In a legal opinion to GAO on whether the statutory changes regarding T&M contracts for commercial services apply to the schedules program, GSA concluded that the applicability is uncertain but stated that existing regulations satisfy concerns about use of T&M under the schedules program. GAO notes that these regulations do not require the same level of detailed analysis as does the Part 12 D&F. Further, there is no indication that the statutory requirements cannot apply to items or services under the schedules program. GSA officials said they are in the process of developing a Part 12 D&F for the entire schedules program, but it is not clear how this D&F will act as a safeguard when T&M orders are used.

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## Abbreviations

ANPR	advanced notice of proposed rulemaking
CMS	Centers for Medicare and Medicaid Services
D&F	determination and findings
DFARS	Defense Federal Acquisition Regulation Supplement
DOD	Department of Defense
DOJ	Department of Justice
FAR	Federal Acquisition Regulation
FASA	Federal Acquisition Streamlining Act
FBI	Federal Bureau of Investigation
FPDS-NG	Federal Procurement Data System-Next Generation
GSA	General Services Administration
HHS	Department of Health and Human Services
NASA	National Aeronautics and Space Administration
OFPP	Office of Federal Procurement Policy
SARA	Services Acquisition Reform Act
T&M	time-and-materials
VA	Department of Veterans Affairs

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United States Government Accountability Office  
Washington, DC 20548

June 24, 2009

## Congressional Committees

Time-and-materials (T&M) and labor-hour contracts are used to purchase billions of dollars in services across the federal government. Under these contracts, payments to contractors are based on the number of labor hours billed at a fixed hourly rate—which includes wages, overhead, general and administrative expenses, and profit—and the cost of materials if applicable. These contracts are considered high risk for the government because the contractor’s profit is tied to the number of hours worked. Thus, the government bears the risk of cost overruns. The cost growth on T&M and labor-hour contracts can be significant; we and agency inspectors general have reported numerous instances in which the costs grew to more than double the original value—in one case a contract increased to almost 19 times the original price.<sup>1</sup> Although these contracts may be appropriate in certain circumstances, we reported in 2007 that contracting officers used this contract type for ease and flexibility in the face of unclear requirements or funding uncertainties and did not adequately determine, as required, that no other contract type was suitable.<sup>2</sup>

Until recently, the Federal Acquisition Regulation (FAR) prohibited use of any other contract type except fixed-price for the acquisition of commercial items. Under FAR procedures for acquisition of commercial items and services, government agencies can acquire goods or services via a streamlined procurement process based on the idea that market forces will help ensure good prices.<sup>3</sup> The question of whether or not T&M contracts could be used for commercial services had been the subject of

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<sup>1</sup> See GAO, *Defense Contracting: Improved Insight and Controls Needed over DOD’s Time-and-Materials Contracts*, [GAO-07-273](#) (Washington, D.C.: June 29, 2007).

<sup>2</sup> In this report, we use the term “T&M” to refer to both T&M and labor-hour contracts, as labor-hour contracts differ from T&M contracts only in that the contractor does not supply materials.

<sup>3</sup> The FAR definition of commercial item includes commercial services, which are defined as services of a type offered and sold competitively in substantial quantities in the commercial marketplace based on established catalog or market prices. FAR § 2.101. For the purpose of this report, we are focused on the acquisition of commercial services. In addition, we use the term fixed-price to refer to both firm-fixed-price and fixed-price with economic price adjustment.

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debate and an issue of some contention. Proponents believed that increased use of T&M contracts for commercial services would encourage more commercial firms to compete for government business, while others, such as the Department of Defense Inspector General, opposed expanded use of this high-risk contract type. In 2003, the Services Acquisition Reform Act<sup>4</sup> (SARA) explicitly provided that the FAR shall include authority for the use of T&M contracts for the procurement of commercial services. Part 12 of the FAR, “Acquisition of Commercial Items,” was subsequently amended, effective February 2007, to reflect this change.

The FAR Part 12 revisions included procedural safeguards to ensure that T&M contracts for commercial services are used only when no other contract type is suitable and that cost growth is monitored due to the inherent risks to the government of this contract type.<sup>5</sup> Contracting officers using FAR Part 12 procedures to buy commercial services under T&M contracts are required to conduct additional, more detailed analysis than is required when buying noncommercial services using T&M contracts.<sup>6</sup> For example, the contracting officer must prepare a detailed justification, called a determination and findings (D&F), to explain why no other contract type is suitable for the procurement. The justification is required to contain several elements, including a discussion of market research conducted for the procurement and a description of actions planned to maximize the use of fixed-price contracts on future acquisitions for the same requirements. Additionally, the contracting officer is to include in the contract a ceiling price, which the contractor exceeds at its own risk, and any subsequent change in the ceiling price may be made only after the contracting officer determines that such a change is in the best interest of the procuring agency.

The Part 12 D&F requirement is not explicitly mentioned in FAR Subpart 8.4, which sets forth procedures pertaining to the General Services Administration’s (GSA) federal supply schedules program. Under the

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<sup>4</sup> Pub. L. No. 108-136, § 1436 (2003), which amended section 8002(d) of the Federal Acquisition Streamlining Act of 1994, Pub. L. No. 103-355.

<sup>5</sup> Our June 2007 report did not assess compliance with this requirement, as it was implemented after our review was underway.

<sup>6</sup> On November 24, 2008, DOD revised its acquisition regulation, the Defense Federal Acquisition Regulation Supplement (DFARS), to establish D&F requirements for all T&M contracts for noncommercial services similar to those required by section 12.207 of the FAR for T&M contracts for commercial services. DFARS § 216.601.

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schedules program, GSA establishes long-term, governmentwide contracts for commercially available goods and services, under which federal agencies can issue orders. Even prior to the February 2007 changes to the FAR, GSA had schedule contracts under which agencies were issuing T&M orders for commercial services. According to GSA, it allowed this practice based on its interpretation of the Federal Acquisition Streamlining Act of 1994 (FASA), which provided that fixed-price contracts be used to the “maximum extent practicable” for acquisition of commercial items and was silent on whether T&M contracts could be used.<sup>7</sup>

The Conference Report for the National Defense Authorization Act for Fiscal Year 2004 directed us to report on the use of T&M contracts for commercial services across government agencies.<sup>8</sup> Accordingly, we (1) identified the extent to which agencies have reported using T&M contracts and GSA schedule T&M orders for commercial services and what they are acquiring using this contract type, (2) evaluated the degree to which agencies complied with the FAR Part 12 safeguards, and (3) determined the applicability of the safeguards to the GSA schedules program.

To identify the extent to which agencies have acquired commercial services under T&M contracts and orders and to determine what services they are buying, we analyzed obligations coded in the Federal Procurement Data System-Next Generation (FPDS-NG) as having used commercial item procedures, i.e., FAR Part 12 procedures.<sup>9</sup> We selected those agencies with the greatest reported use of this contract type during the period from October 1, 2001, to June 30, 2008. Our primary focus was on contracts outside of the GSA schedules program because the FAR Part 12 D&F requirement was explicitly applicable to those contracts. However, because the FPDS-NG data showed that a large percentage of the reported dollars and actions were through GSA schedule orders (under FAR Subpart 8.4), we also reviewed T&M orders issued under GSA schedule contracts at each agency in our review. Further, based on data

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<sup>7</sup> Pub. L. No. 103-355, § 8002(d).

<sup>8</sup> Our review was directed by the conferees in the Conference Report accompanying the National Defense Authorization Act for Fiscal Year 2004. Although the Conference Report directed us to report on these issues within 1 year of enactment of the act, we initiated our review after the February 2007 FAR rule implementing the National Defense Authorization Act for Fiscal Year 2004 provision went into effect.

<sup>9</sup> These obligations are indicated in data element 10H in FPDS-NG, “Commercial Item Acquisition Procedures.”

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reported in FPDS-NG, we reviewed a limited number of T&M contracts for commercial services that had been awarded prior to the February 2007 changes to FAR Part 12 commercial procedures to better understand the circumstances of those procurements. In total, we reviewed 149 contract files. At the Department of Defense (DOD), we selected one location for each military service with high reported obligations for T&M commercial services. Our sample represents all of the T&M contracts for commercial services reported in FPDS-NG at the Departments of Justice (DOJ), Health and Human Services (HHS), and Veterans Affairs (VA), as well as the National Aeronautics and Space Administration (NASA) during the October 2001 to June 2008 time period. These 5 agencies represent 97 percent of obligations coded as T&M contracts awarded using commercial item procedures from October 2001 to June 2008.

To corroborate that the contracts in our sample were T&M and that commercial services were acquired as indicated in FPDS-NG, we reviewed the contracts and orders for commercial or T&M clauses and other contract documentation as necessary, or, when documentation was not sufficient, spoke with the contracting officer. To determine the government's use of T&M contracts for commercial services relative to its obligations for services as a whole, we analyzed FPDS-NG data from February 12, 2007 (when the new FAR rule was implemented) to December 31, 2008.

To determine the degree to which agencies' use of T&M contracts for commercial services complied with the FAR Part 12 D&F requirement, we reviewed contract files and interviewed over 100 contracting and procurement policy officials. We requested and received a legal opinion from GSA as to whether the statutory change allowing the use of T&M contracts for commercial services and the FAR D&F requirement are applicable to the GSA schedules program.<sup>10</sup> Appendix I contains additional details on our scope and methodology and our sample. We conducted this performance audit from September 2008 to June 2009, in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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<sup>10</sup> FASA § 8002(d) and FAR § 12.207.

## Background

Federal agencies can choose from among several different contract types, including T&M contracts, to acquire products and services. This choice is the principal means that agencies have for allocating cost risk between the government and the contractor. The government's basis for payments, contractor's obligations, and the party assuming more risk for cost overruns changes depends upon the type of contract used—fixed-price, T&M, or cost-reimbursement.

**Table 1: Contract Types**

Fixed-price	T&M	Cost-reimbursement
<p><b>Government</b> pays a fixed price and is guaranteed an end item or service whether actual total cost of product or service falls short of or exceeds the contract price. May also pay an award or incentive fee related to performance.</p> <p><b>Contractor</b> provides an acceptable deliverable at the time, place, and price specified in the contract.</p> <p><b>Who assumes risk of cost overrun?</b> Contractor.</p>	<p><b>Government</b> pays fixed per-hour labor rates that include wages, overhead, general and administrative costs, and profit; government may reimburse contractor for other direct costs, such as travel and materials costs. Government is not guaranteed a completed end item or service within the ceiling price.</p> <p><b>Contractor</b> makes good faith effort to meet government's needs within the ceiling price.</p> <p><b>Who assumes risk of cost overrun?</b> Government.</p>	<p><b>Government</b> pays contractor's allowable costs, which do not include profit. Also pays a fee, which may be related to performance. Government is not guaranteed a completed end item or service within the estimated cost.</p> <p><b>Contractor</b> makes good faith effort to meet government's needs within the estimated cost.</p> <p><b>Who assumes risk of cost overrun?</b> Government.</p>

Sources: FAR, Defense Federal Acquisition Regulation Supplement, DOD Contract Pricing Preference Guide (data); GAO (presentation and analysis).

T&M contracts constitute a high risk to the government.<sup>11</sup> The contractor provides its best efforts to accomplish the objectives of the contract up to the maximum number of hours authorized under the contract. Each hour of work authorizes the contractor to charge the government an established labor rate which includes profit. These contracts are considered high risk for the government because the contractor's profit is tied to the number of hours worked. Thus, the government bears the risk of cost overruns. Therefore the FAR provides that appropriate government monitoring of contractor performance is required to give reasonable assurance that efficient methods and effective cost controls are being used. Further, because of the risks involved, the FAR directs that T&M contracts may only be used when it is not possible at the time of award to estimate accurately the extent or duration of the work or to anticipate costs with

<sup>11</sup> The FAR provides that a time-and-materials contract provides no positive profit incentive to the contractor for cost control or labor efficiency. T&M contracts exhibit some characteristics of fixed-price contracts in that T&M contracts contain fixed hourly labor rates and a ceiling price which the contractor exceeds at its own risk. FAR § 16.601.

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any reasonable degree of confidence.<sup>12</sup> For many years, federal regulations have required contracting officers to justify in writing that no other contract type (such as fixed-price) is suitable before using a T&M contract.<sup>13</sup>

Commercial services comprise services for support of commercial items and services of a type offered and sold competitively in substantial quantities in the commercial marketplace based on established catalog or market prices.<sup>14</sup> During the 1990s, Congress enacted a number of laws to increase the government's use of commercial practices to make government buying more efficient. The benefits of using commercial practices were seen as creating greater access to commercial markets (products and service types) with increased competition, better prices, and new market entrants and/or technologies. Commercial acquisition practices also present several advantages to contractors when doing business with the government, such as generally not being required to submit cost or pricing data. While the acquisition procedures in FAR Part 12 for purchasing commercial services allow for a streamlined process, prices are accepted based on competition and availability in the marketplace rather than the government's review of a contractor's cost and pricing data. Improperly classifying an acquisition as commercial can leave the government vulnerable to accepting prices that may not have been established by the marketplace.<sup>15</sup>

FASA authorized the use of fixed-price contracts for the acquisition of commercial items, but it did not explicitly authorize the use of T&M

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<sup>12</sup> FAR § 16.601(c).

<sup>13</sup> FAR § 16.601(d).

<sup>14</sup> Commercial items include items that are of a type customarily used by the general public or nongovernmental entities for purposes other than governmental purposes and have been sold, leased, or licensed to the general public or have been offered for sale, lease or license to the general public. 41 U.S.C. § 403(12); FAR § 2.101, definition of commercial item.

<sup>15</sup> Contracting officers may not request cost or pricing data if they determine that prices have been subject to adequate price competition, prices are set by law or regulation, or when a commercial item is acquired. FAR § 15.403-1(b). The government is permitted to obtain pricing information from sources other than the offering contractor to support a determination of price reasonableness. If this information proves inadequate, the government can require the offering contractor to provide additional information, known as information other than cost or pricing data, although the government must, to the maximum extent practicable, limit the scope of the request to include only information in a form regularly maintained by the offering contractor. FAR § 15.403-3.

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contracts for such acquisitions.<sup>16</sup> SARA specifically authorized the use of T&M contracts for the acquisition of commercial services with certain safeguards to ensure proper use of these contracts.<sup>17</sup> The implementing regulations included additional requirements as safeguards under FAR Part 12.<sup>18</sup>

Table 2 summarizes the FAR safeguards when using T&M contracts under FAR Part 12 acquisition procedures for commercial items; under FAR Part 16, acquisition procedures for noncommercial services; and under FAR Subpart 8.4, GSA schedule contracts.

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<sup>16</sup> Pub. L. No. 103-355, § 8002(d).

<sup>17</sup> Section 1432 of SARA, which is Title XIV of the National Defense Authorization Act for Fiscal Year 2004, Pub. L. No. 108-136, (2003), amended section 8002(d) of FASA.

<sup>18</sup> FAR § 12.207.

**Table 2: Summary of Relevant FAR Provisions Pertaining to T&M Contracts and to Orders Under the GSA Schedule Program.**

<b>Justification for using T&amp;M</b>	<b>Requirements for T&amp;M contracts for commercial services. FAR Section 12.207(b)</b>	<b>Requirements for T&amp;M contracts for noncommercial services. FAR Section 16.601(d)</b>	<b>Requirements when ordering off the GSA schedule. FAR Section 8.405-2(e)</b>
	<p>The contracting officer must execute a D&amp;F for the contract that no other contract type is suitable.</p> <p>At a minimum, the D&amp;F shall—</p> <ul style="list-style-type: none"> <li>(i) Include a description of the market research conducted;</li> <li>(ii) Establish that it is not possible at the time of placing the contract or order to accurately estimate the extent or duration of the work or to anticipate costs with any reasonable degree of certainty;</li> <li>(iii) Establish that the requirement has been structured to maximize the use of firm-fixed-price or fixed-price with economic price adjustment contracts on future acquisitions for the same or similar requirements; and</li> <li>(iv) Describe actions planned to maximize the use of firm-fixed-price or fixed-price with economic price adjustment contracts on future acquisitions for the same requirements.</li> </ul> <p>The D&amp;F shall be signed by the contracting officer prior to the execution of the base period or any option periods of the contracts and approved by the head of the contracting activity prior to the execution of the base period when the base period plus any option periods exceeds three years.</p>	<p>The contracting officer must prepare a D&amp;F that no other contract type is suitable.</p> <p>The D&amp;F shall be signed by the contracting officer prior to the execution of the base period or any option periods of the contracts and approved by the head of the contracting activity prior to the execution of the base period when the base period plus any option periods exceeds three years.</p>	<p>The ordering activity shall document the rationale for using other than a firm-fixed-price order.</p>
<b>Ceiling Prices</b>	<p>The contracting officer must include a ceiling price in the contract or order that the contractor exceeds at its own risk and authorize any subsequent change in the ceiling price only upon a determination, documented in the contract file, that it is in the best interest of the procuring agency to change the ceiling price.</p>	<p>The contract must include a ceiling price that the contractor exceeds at its own risk. The contracting officer shall document the contract file to justify the reasons for and amount of any subsequent change in the ceiling price.</p>	<p>No requirement specified.</p>

Source: FAR.

Note: It is important to note that, as of November 24, 2008, T&M contracts for noncommercial services awarded by DOD require similar procedures, including the more detailed D&F described in FAR Part 12, as that required for T&M contracts using acquisition procedures for commercial items and services. DFARS § 216.601. This requirement went into effect after the time frame of our contract sample for this review. It has not been applied to civilian agencies with respect to T&M contracts for noncommercial services.

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The FAR Part 12 revisions also added safeguards for agencies using T&M pricing on indefinite-delivery contracts for commercial services.<sup>19</sup> Specifically, indefinite-delivery contracts for commercial services awarded using Part 12 procedures may allow for the use of fixed-price or T&M orders, and contracting officers are required to execute the Part 12 D&F for each order placed on a T&M basis. If the contract only allows for the issuance of orders on a T&M basis, the Part 12 D&F is required to be executed to support the basic contract and also explain why using an alternative fixed-price structure is not practicable. The D&F for this type of contract is required to be approved one level above the contracting officer. By contrast, the section of FAR Part 16 pertaining to T&M services does not explicitly address the D&F requirement for indefinite-delivery contracts.<sup>20</sup>

Concerns by DOD and Congress over the increased use of T&M contracts have sparked some actions to curb DOD's use of T&M in general and for the acquisition of commercial services in particular. In June 2007, we reported that DOD's use of T&M contracts had steadily increased and that contracting officials frequently failed to ensure that this contract type was used only when no other contract type was suitable.<sup>21</sup> Little effort had been made to convert follow-on work to a less risky contract type when historical pricing data existed, despite guidance to do so. Based on our recommendations for improved oversight, DOD's Defense Procurement and Acquisition Policy office, in March 2008, began requiring military departments and defense agencies to establish procedures for analyzing whether T&M contracts and orders under indefinite-delivery contracts are used when other contract types are suitable. Each department or agency was to provide an assessment of the appropriate use of T&M contracts for any contracting activity that obligated more than 10 percent of its total fiscal year 2007 obligations for services using T&M contracts or orders. The assessment was to include actions that will be taken to reduce the use of T&M contracts whenever possible.

Further, the Acquisition Improvement and Accountability Act of 2007 required DOD to revise its acquisition regulation to require contracting officers to determine in writing that the offerer has submitted sufficient

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<sup>19</sup> FAR §12.207(c).

<sup>20</sup> FAR §16.601.

<sup>21</sup> [GAO-07-273](#).

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information to evaluate price reasonableness for commercial services that are not offered and sold competitively in substantial quantities in the commercial marketplace but are “of a type” offered and sold competitively in substantial quantities in the commercial marketplace. The act also specifies that DOD’s revised regulation shall ensure that the procedures applicable to T&M contracts for commercial services may be used only for the following:

- services procured for support of a commercial item;
- emergency repair services;
- any other commercial services only to the extent that the head of the agency approves a determination in writing by the contracting officer that
  - the services to be acquired are commercial services;
  - the offeror has submitted sufficient information to evaluate the price reasonableness of the services, if they are not offered and sold competitively in substantial quantities in the commercial marketplace;
  - such services are commonly sold to the general public through use of T&M or labor-hour contracts; and
  - the use of a T&M or labor-hour contract type is in the best interest of the government.<sup>22</sup>

We did not assess DOD’s compliance with these provisions because they have not yet been implemented.<sup>23</sup>

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<sup>22</sup> 41 U.S.C. § 403 (12).

<sup>23</sup> See section 805 of Title VIII of the National Defense Authorization Act for Fiscal Year 2008. Pub. L. No. 110-181. As of May 29, 2009, the DFARS case that will implement this provision had not been issued. The National Defense Authorization Act for Fiscal Year 2009, enacted October. 14, 2008, directed that the FAR be modified within 180 days of enactment to include a similar provision, which would be applied to all government agencies. Pub. L. 110-417 § 868 (2008). As of May 29, 2009, the FAR had not been revised to include the provisions.

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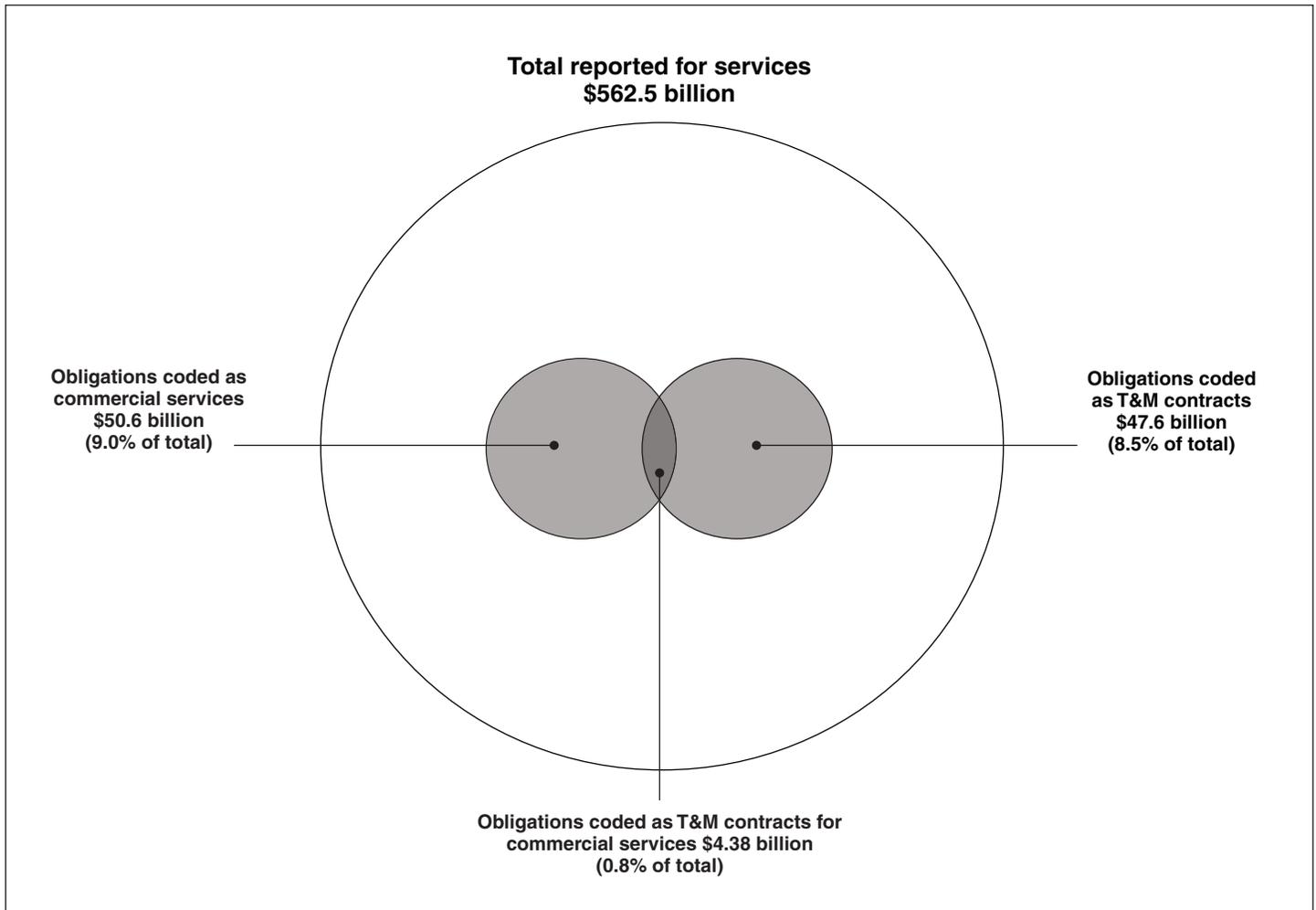
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## Federal Agencies Have Reported Limited Use of T&M Contracts for Commercial Services but Reliability of Data Is in Doubt

Federal agencies have reported relatively limited use of T&M contracts and GSA schedule T&M orders to purchase commercial services, based on those obligations coded in FPDS-NG as using T&M contracts and orders under commercial item procedures. From February 12, 2007, when the FAR change that allowed T&M acquisitions for commercial services was implemented, to December 31, 2008, \$4.4 billion—less than 1 percent of total federal obligations for services—was reported.

Figure 1 presents information on the total reported obligations for services (i.e., commercial and noncommercial) compared to obligations coded as (1) having acquired commercial services, (2) as T&M contracts for services, and (3) as T&M contracts for commercial services from February 12, 2007, to December 31, 2008.

**Figure 1: Total Reported Obligations for Services Compared to Obligations Coded as (1) Having Acquired Commercial Services, (2) as T&M Contracts for Services, and (3) as T&M Contracts for Commercial Services From February 12, 2007 to December 31, 2008**



Source: FPDS-NG for data; GAO for presentation.

Note: T&M dollars include labor-hour contracts and orders.

The vast majority of the \$4.4 billion in obligations coded as T&M for commercial services were for services actually acquired under GSA schedule contracts (\$3.1 billion). The FPDS-NG user manual defines commercial item procedures as those that use FAR Part 12 acquisition procedures, but our analysis of FPDS-NG data showed that these orders had been issued through FAR Subpart 8.4, pertaining to GSA schedule contracts, and thus had been miscoded based on the definition in the user

manual.<sup>24</sup> Although our overall focus was on nonschedule T&M orders for commercial services, we identified additional obligations under T&M orders placed on GSA schedule contracts. From February 2007 to December 2008, approximately \$6 billion of the \$47.6 billion in obligations coded as T&M contracts were through the GSA schedule program, in addition to the \$3.1 billion that had been miscoded as having used FAR Part 12. Thus, the full picture of the government’s use of T&M for commercial services for this time period was approximately \$10.4 billion—about 90 percent of which was under GSA schedule contracts.

Agencies reported purchasing a variety of commercial services using T&M contracts and orders during this time period. The top 10 types of commercial services reported as purchased using T&M contracts were as shown in table 3.

**Table 3: Top 10 Commercial Services Coded as Using T&M Contracts and Orders to Acquire Commercial Items from February 12, 2007, to December 31, 2008**

<b>Type of commercial services</b>	<b>Dollars obligated</b>	<b>Percent of total dollars obligated under T&amp;M contracts and orders for commercial services</b>
Other Automatic Data Processing & Telecommunications Services	\$686,044,403	15.7
Engineering and Technical Services	647,682,748	14.8
Other Professional Services	478,541,816	10.9
Program Management/Support Services	357,981,397	8.2
Automated Information System Services	225,187,839	5.1
Management Services/Contract and Procurement Support	201,641,198	4.6
Logistics Supports Services	189,831,359	4.3
Other Management Support Services	186,479,109	4.3
Automatic Data Processing Systems Analysis Services	182,481,817	4.2
Automatic Data Processing Systems Development Services	\$120,849,955	2.8

Source: FPDS-NG for data; GAO for presentation.

<sup>24</sup> We brought this issue to the attention of officials at the Office of Federal Procurement Policy and GSA, who said they would look into the matter.

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Our sample of 149 contracts and orders provides additional details on the variety of commercial services procured under T&M contracts. For example:

- The Army purchased patent legal services for inventions resulting from biomedical, chemical, and other research.
- The Indian Health Service, within HHS, entered into a contract for emergency nursing services and inpatient nursing services for a healthcare center.
- The Navy contracted for repair services for a Navy vessel undergoing overhaul at the Norfolk Naval Shipyard.
- The VA purchased project management services for its MyHealthVet Web site, which provides access to health information, tools, and services.
- The Federal Bureau of Investigation (FBI) purchased certified gunsmith services to repair and perform preventative maintenance on firearms.
- NASA entered into a contract for translation, interpretation, visa processing, and logistical support services.

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### Errors, Misunderstandings, and Differing Opinions Cast Doubt on Reliability of Reported Data

Maintaining accurate data is an essential component of good oversight and helps lead to informed decisions. In our sample of T&M contracts for commercial services, we found that the quality of the data reported in FPDS-NG was compromised in several ways.

First, 28 of the 149 contracts and orders in our sample from October 1, 2001, to June 30, 2008, were incorrectly coded in FPDS-NG. Our review of the contract files revealed that 19 were coded as having acquired commercial services when they did not, and 10 were coded as T&M contracts when they were fixed-price, as shown in table 4.<sup>25</sup>

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<sup>25</sup> To confirm that the contracts in our sample were correctly coded as having acquired commercial services or as T&M, we reviewed the contracts and documentation in the contract files. For example, we looked for relevant FAR clauses (FAR 52.212-4—Contract Terms and Conditions- Commercial Items) in the contract to confirm that commercial services were acquired. Where the documentation was not clear, we spoke with contracting officers.

**Table 4: Contracts and Orders from our Sample Incorrectly Coded in FPDS-NG as Having Acquired Commercial Services or as T&M**

Agency	Miscoding Type	
	Incorrectly coded as having acquired commercial services	Incorrectly coded as T&M
Air Force	9	0
Army	0	0
Navy	0	6
DOJ	4	1
HHS	4	1
NASA	1	0
VA	1	2
<b>Total<sup>a</sup></b>	<b>19</b>	<b>10</b>

Source: GAO file reviews.

Note: This table does not address the overall coding errors, discussed above, where GSA schedule orders had been coded as using FAR Part 12 procedures.

Twelve of the 28 contracts or orders were awarded prior to the February 2007 FAR change pertaining to the use of T&M contracts for commercial services.

<sup>a</sup>One contract at DOJ was incorrectly coded as both T&M and as having acquired commercial services.

Several of the contracting officers we interviewed attributed these miscodings to errors made during input of data into the federal procurement data system. For example, the Air Force had planned to establish indefinite-delivery/indefinite-quantity contracts for advisory and assistance services using FAR Part 12 acquisition procedures for commercial services. However, because cost-reimbursement orders were contemplated under the contracts—which the FAR prohibits for commercial services—the Air Force decided not to award the contracts using FAR Part 12 acquisition procedures. Agency officials stated that the contracts were then mistakenly coded as having used acquisition of commercial item procedures.

In addition, we found that T&M contracts for commercial services may be underreported based on a misunderstanding about contract type among contracting officials in most of the government agencies in our review. Some contracting officers had the incorrect belief that the fixed labor rate

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component of T&M contracts renders them fixed-price.<sup>26</sup> In fact, some contracts in our sample were referred to in the contract file as “firm fixed price labor hour,” a contract type that does not exist. Despite the fact that labor rates are fixed under T&M contracts, the overall ceiling price is not a firm, fixed price because the contractor will be paid based on the number of hours worked (up to the ceiling price). Some contracting officers acknowledged having coded other similar contracts outside of those in our sample as fixed-price, thus potentially understating the use, and correlated risk to the government, of T&M contracts. Following are some examples that highlight contracting officials’ confusion about fixed-price versus labor-hour contracts (even though these contracts in our sample had been correctly coded as labor-hour).

- Contracting officers at HHS’s Indian Health Services stated that although a few of their contracts for medical professionals had been coded as labor-hour, these contracts were typical of the contracts they usually code as fixed-price. One contracting officer explained that if the hours are reasonably well known in advance—“shift labor,” for example—then the estimated hours written into the contract are considered fixed-price. However, another contracting officer explained that Indian Health Services pays contractors for actual hours worked, regardless of the estimate written into the contract.
- A contracting officer at HHS’s Program Support Center told us that a contract in our sample, for maintenance and repair services, had mistakenly been entered as a labor-hour contract in FPDS-NG. He believed it should have been coded as fixed-price because the dollars obligated reflected a fixed hourly rate multiplied by the hours worked, but later conceded that the contract was actually a labor-hour contract.
- An FBI contracting officer maintained that a labor-hour contract in our sample, for gunsmith services, should have been coded as fixed-price because the labor rate was fixed. The contract purchases the services of one person to repair and maintain firearms for FBI training teams. Although the contract requires these services during “normal business hours” 5 days a week, it also allows the contractor to bill for preapproved overtime when necessary and includes a maximum number of hours to be billed on the contract.

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<sup>26</sup> A fixed-price contract provides for a firm price or, in appropriate cases, an adjustable price. FAR § 16.201.

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When we raised this confusion about contract type with officials from the Office of Federal Procurement Policy (OFPP), they agreed that clarification to the contracting community on what constitutes a fixed price versus a labor hour contract would be beneficial.<sup>27</sup>

We also spoke with contracting officers about how they generally define a service as commercial and found that individuals had different opinions about whether or not certain services are commercial, which may be contributing to issues with data reliability in FPDS-NG.<sup>28</sup> Many contracting officers defined a commercial service as being readily available in the commercial marketplace. However, several officials told us that in certain cases, a service could reasonably be considered either commercial or noncommercial. For example, a DOD official stated that a contract for aircraft repair services could be considered either a commercial or noncommercial purchase depending on the contracting officer's interpretation. On the other hand, Air Force officials we spoke with view aircraft maintenance—even on military aircraft—as predominantly commercial since aircraft mechanics are broadly available commercially. Some contracting officers stated they would consider services that require specific knowledge of government requirements to be noncommercial. For example, a DOJ procurement policy official told us that although a contracting officer used FAR Part 12 commercial acquisition procedures to award a contract for technical services, including the installation of modules for DOJ's financial management system (one of the T&M contracts in our sample), he did not consider the service to be commercial because it was specific to DOJ's needs. He cited a contract for trash pick-up as an example of a commercial contract. In another example, a Navy contracting officer explained that although the majority of her purchases are for commercial items or services, if a purchase is completely exclusive to the Navy—such as for equipment used on submarines or Navy ships—she would consider it noncommercial.

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<sup>27</sup> The OFPP Administrator serves as chair of the Federal Acquisition Regulatory Council (FAR Council). The FAR Council—whose members include the DOD Director of Defense Procurement and Acquisition Policy, NASA's Associate Administrator for Procurement, and the GSA Chief Acquisition Officer—oversees development and maintenance of the FAR.

<sup>28</sup> Our discussions with contracting officers on this matter were of a general nature. For specific procurements, market research is an essential element for the acquisition of commercial items and is used to establish the foundation for the agency description of need, the solicitation, and resulting contract. FAR § 12.202.

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In addition, although all services available on the GSA schedule are described as commercial in the FAR, we found cases where agencies ordering these services did not consider them to be commercial.<sup>29</sup> GSA officials confirmed that they consider everything under the schedules program to be commercial, even if items or services are slightly modified to meet specific requirements. However, they acknowledged that if significant modifications are made, the items ordered may be out of scope of the underlying GSA contract. The following are some examples from our review where agency officials used the GSA schedules program but considered the procurement to be noncommercial.

- At one Air Force location, contracting officers told us that they did not consider any of their seven GSA orders in our sample, such as an order for program management and technical support for the Air Force's telecommunications monitoring and assessment program, to be commercial. They only discovered that these orders were being automatically coded in FPDS-NG as having used commercial procedures when we identified them in our sample for review.
- NASA had purchased environmental management and safety support services under a GSA schedule contract, but, according to NASA contracting officers, the actual services ordered were so technical and specialized that they did not consider them to be commercial services. They had used the GSA schedule primarily to identify qualified commercial vendors who could perform this specialized work.
- The Centers for Medicare and Medicaid Services (CMS) at HHS issued an order under a GSA schedule contract for the design and build of a knowledge management system for CMS's Center for Beneficiary Services. According to the contracting officer, because the system was custom-designed for CMS, it is not commercial.

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## FAR Safeguards for T&M Contracts for Commercial Services Rarely Used

Under FAR Part 12, T&M contracts or orders may be used to acquire commercial services if the contracting officer executes a D&F which sets forth sufficient facts and rationale to justify that no other contract type is suitable. At a minimum, the D&F must:

1. include a description of the market research conducted;

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<sup>29</sup> FAR Section 8.402(a).

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2. establish that it is not possible at the time of placing the contract or order to accurately estimate the extent or duration of the work or to anticipate costs with any reasonable degree of certainty;
  3. establish that the requirement has been structured to maximize the use of fixed-price on future acquisitions for the same or similar requirements; and
  4. describe actions planned to maximize the use of fixed-price contracts on future acquisitions for the same requirements.

Of the 149 contracts and orders in our sample, 82 were subject to this D&F requirement.<sup>30</sup> Of these 82 contracts and orders, only 5 had a FAR Part 12 D&F that addressed each required element. No D&F had been prepared for many of the contracts and orders. Further, for almost half of the contracts and orders, contracting officials had improperly used the less rigorous Part 16 D&F instead of the Part 12 D&F for commercial services. We found a general lack of awareness of the Part 12 D&F requirement at the agencies in our review. Many contracting officials, including some policy officials, across the agencies in our review were unfamiliar with this Part 12 safeguard. We raised this issue with officials from OFPP, who were concerned at the general lack of compliance with this key safeguard pertaining to T&M contracts for commercial services.

Table 5 sets forth the breakdown of D&Fs for the 82 contracts and orders in our sample that were subject to the Part 12 D&F.

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<sup>30</sup> These 82 contracts and orders were confirmed as (1) T&M contracts or orders for commercial services (2) having been awarded after the FAR revisions to Part 12 took effect on February 12, 2007, and (3) not having been awarded through GSA schedule contracts.

**Table 5: Number and Type of D&Fs for Non-GSA Contracts and Orders in Our Sample Subject to the FAR Part 12 D&F Requirement**

Agency	Non-GSA contracts and orders				Total
	Complete Part 12 D&F	Partial Part 12 D&F	Part 16 D&F	No D&F	
Air Force	2	1	5	0	8
Army	0	2	18	8	28
Navy	2	2	8	4	16
DOJ	0	2	3	2	7
HHS	1	2	0	14	17
NASA	0	0	1	0	1
VA	0	0	0	5	5
<b>Total</b>	<b>5</b>	<b>9</b>	<b>35</b>	<b>33</b>	<b>82</b>

Source: GAO analysis of data from agency contract files.

Note: We determined that a D&F was complete if it made reference to FAR Section 12.207 and at least mentioned all of the four required elements of the D&F. For example, if a D&F stated the outcomes of the market research conducted but did not describe the research conducted, we still gave credit for having addressed the requirement in FAR Section 12.207(b)(1) to describe the market research conducted. A partial Part 12 D&F included some but not all of the four required elements.

Sixteen of the contracts and orders in our Army sample had the same Part 16 D&F that was used to award a multiple award contract for patent legal services.

In some cases, contracting officers had incorrectly concluded that a D&F was not necessary. For example, two contracting officers at the Navy told us that they did not complete a D&F because they did not believe contracts below the simplified acquisition threshold required a D&F—which is inconsistent with the FAR.<sup>31</sup> In another instance, an Air Force contracting officer who had included Part 12 D&Fs in two contracts in our sample executed only a Part 16 D&F for a third contract because he believed that a Part 12 D&F was not required for a simplified acquisition.

The nine D&Fs in our sample that had some but not all of the discrete elements required by FAR Part 12 typically omitted a description of the market research conducted or actions planned to maximize use of fixed-price contracts for future acquisitions for the same or similar services. For

<sup>31</sup> There is no indication in the FAR that FAR Section 12.207 does not apply to contracts below the simplified acquisition threshold, which is generally \$100,000. FAR Section 12.207 does not, however, apply to purchases below the micropurchase threshold, which is generally \$3,000. See FAR Section 2.101 definition of the simplified acquisition and micropurchase threshold.

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example, one D&F for a DOJ contract for consulting services for the National Prison Rape Elimination Commission, awarded on a sole-source basis, included information on the services needed but did not describe the market research conducted. The D&F states that neither the scope of work nor the contractor's level of effort can be determined with a degree of accuracy necessary to develop a reliable cost estimate on which to base a fixed-price award. It further states that the work entails professional and other administrative services for which no reliable specifications exist, and the precise method of accomplishment cannot be established in advance. However, the D&F does not describe actions planned to maximize the use of fixed-price contracts on future acquisitions for the same requirements.

The five FAR Part 12 D&Fs we found that addressed all the required elements included the rationale for a T&M contract and discussed how future requirements could potentially shift to a fixed-price contract. For example, in preparing a D&F for a Navy contract for the overhaul and repair of naval vessels, contracting officials not only described the market research, but thoroughly documented the market survey performed, including a description of applicable services provided by potential bidders in the marketplace. They also described how they would employ fixed pricing for stable labor expenses and monitor the volatility of other labor categories to determine if the services could be purchased on a fixed-price basis in the future. In another example, at HHS, a contracting officer completed a Part 12 D&F for a contract for less than 6 months of network administrative support services. The D&F stated that the market research had identified an 8(a) company to provide the services.<sup>32</sup> It also explained that the requirement had been structured to maximize fixed pricing by limiting the period of performance and that there was no anticipated need for this service to continue in the future. In yet another example, at the Air Force, the contracting officer prepared a complete Part 12 D&F for a contract for intelligence support services that addressed all of the required elements. The D&F explained that a small business was identified as the best option for the procurement and described the outcome of the market research conducted. Further, the D&F stated that information obtained from the procurement would be used to develop

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<sup>32</sup> The 8(a) program is one of the federal government's primary means for developing small businesses owned by socially and economically disadvantaged individuals. Firms approved as 8(a) participants can receive business development assistance from the Small Business Administration.

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fixed pricing for future procurements, which would be better defined and more concise.

In addition to a more detailed D&F, the FAR also requires the contracting officer to document that each change to the ceiling price of a T&M contract for commercial services is in the best interest of the procuring agency. In general, the contracts in our sample that were subject to the FAR Part 12 requirements did not have increases in the ceiling price. However, in the instances where an increase did occur, contracting officers did not always follow the FAR requirement. A contract at HHS for financial services management more than doubled in value over the original “estimated not-to-exceed” cost. No written justification was provided for why this increase was in the best interest of the procuring agency. The contracting officer stated that the not-to-exceed amount on the contract was only an estimate and had not identified a separate ceiling price—which is required by the FAR Part 12. On the other hand, some contracts with ceiling price increases did include a description of why the increase was necessary.<sup>33</sup> For example, we reviewed three orders at the Army for patent legal services that documented why ceiling price increases were necessary—which was essentially due to a change in the acquisition strategy for obtaining these services. After establishing a multiple award contract with 23 vendors, contractors were asked to submit proposals to complete ongoing work that, according to contracting officials, was previously purchased on government credit cards. In one case, a task order increased from approximately \$100,000 to \$500,000 because the contractor had initially misunderstood the request for proposals and submitted a proposal for only a limited scope of work; it subsequently revised its proposal to address all of the Army’s stated requirements. In another example at the U.S. Marshals Service, the ceiling price on a contract for aircraft maintenance services increased from \$250,000 to \$400,000 through three successive modifications, and all the modifications included a detailed description of the need for additional funds.

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<sup>33</sup> FAR Section 12.207 (b)(ii) provides that the contracting officer authorize any subsequent change in the ceiling price only upon a determination, documented in the contract file, that it is in the best interest of the procuring agency to change the ceiling price. In the examples presented here, the contracting officer did not always include the statement that this change was in the best interest of the procuring agency in the documentation, but nevertheless did include information on the rationale for the ceiling price change.

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## Agency Training and Contract Review Processes Did Not Include FAR Part 12 Safeguards

Clear guidance and training are needed to successfully introduce and implement changes to regulations. The DOD offices we visited were the only locations in our review that provided general training seminars or guidance on the changes to FAR Part 12 permitting the use of T&M contracts for commercial services, but none provided written guidance or training on the more detailed D&F requirement. Navy contracting officials recognized this omission during our visit and subsequently provided additional training to their contracting officials.<sup>34</sup> Army officials told us that they had discussed the new D&F requirement in a meeting with contracting officers but had not issued any written guidance. None of the civilian agencies in our review had provided formal guidance or training to their contracting officers on the safeguards.

Officials who were aware of the Part 12 safeguards frequently found out through their own initiative. For example, in our sample of 17 HHS contracts subject to the FAR Part 12 D&F requirement, 2 contained partial D&Fs and 1, issued by the Program Support Center, contained all of the D&F elements. The contracting officer responsible for the complete D&F indicated that he became aware of the D&F requirement through his own FAR research and had not received guidance from headquarters. The other 2 partial Part 12 D&Fs were issued by another HHS component, the Food and Drug Administration. The head of contracting who signed these D&Fs said that she had also learned of the Part 12 D&F requirement by researching the FAR. At DOJ, officials at the Office of Justice Programs explained that they became aware of the FAR Part 12 D&F requirement through a paid subscription for updates to a contract checklist from an outside vendor. When awarding a contract for consulting services, a contracting officer from that office prepared a Part 12 D&F in the file, but it did not address all of the required elements. Several contracting officials at different agencies noted that their contracting staff is very overworked or inexperienced, which may have contributed to the general lack of awareness of the new D&F requirement.

Internal controls, such as contract reviews, administered by informed agency personnel can also help ensure that policies and processes are translated into practice. In some cases, the contracts in our sample had been reviewed by staff, including legal officials, who did not detect that the required Part 12 D&Fs were missing. For example, while six of the

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<sup>34</sup> In addition, Navy headquarters issued a memo on March 31, 2009, reminding contracting officials that the D&F is required for T&M contracts for commercial services.

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eight contracts at the Air Force were reviewed by attorneys or contract management officials, five contract files still contained the incorrect Part 16 D&F rather than the Part 12 D&F for commercial acquisitions. At the Navy, one attorney reviewing a contract file identified the need to include the Part 12 D&F, but another attorney reviewing a different Navy contract failed to do so. In another example at NASA, an attorney and associate division chief had reviewed the contract and did not identify that the Part 12 D&F was missing, but the associate division chief did inquire as to whether part of the work could be fixed-price. In other cases, contract reviews either failed to ensure that any D&F was included in the contract file or there was no evidence that reviews of the acquisition approach had occurred. Four of the five VA contracts we reviewed were subject to internal reviews by VA technical and legal staff based on factors such as value and contract type, yet none contained a D&F of any type. At the Army location we visited, there was no indication that the contracts' acquisition approach had been reviewed, and most of the contracts in our sample contained the Part 16 D&F or had no D&F at all. However, this Army contracting activity updated its internal contract review checklist in December 2008, after our visit, to include a reference to the Part 12 D&F requirement.

Our review of contract files and interviews with agency officials further revealed that awareness of the new D&F requirement even varied among the staff of a single contracting office. For example, three T&M contracts for commercial services were issued during a 6-month period by U.S. Marshals Service contracting officials for aircraft maintenance and pilot services in Puerto Rico. One contract file contained a partial Part 12 D&F, one contained a Part 16 D&F, which is less rigorous, and the third had no D&F.

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## FAR Part 12 Safeguards Have Not Been Applied to GSA Schedules Program

The vast majority of reported obligations for commercial services acquired through T&M contracts went through GSA's schedules program from February 2007 to December 2008, but the FAR Part 12 D&F requirement has not been applied to the use of schedule contracts. The February 2007 revisions to FAR Part 12 did not specifically address the applicability of the D&F provisions to GSA schedule contracts or orders issued under them.<sup>35</sup> Further, the section of the FAR that governs ordering procedures for GSA schedules contracts does not refer to the Part 12 D&F requirement to either make it explicitly applicable or inapplicable as it does with other FAR provisions.<sup>36</sup> GSA has not incorporated the D&F requirement in its own acquisition manual, for use by its contracting officers, and has not instructed ordering agencies to comply with the Part 12 D&F requirement when issuing T&M orders under its schedule contracts. For example, the Part 12 D&F is not discussed in GSA's ordering guidance for schedule contracts or in the frequently asked questions on the schedules program Web site. Accordingly, there is uncertainty in the contracting community about the extent to which the Part 12 D&F is required for schedule orders. Our file review revealed that only 2 of the 19 GSA orders we reviewed that were awarded after the February 2007 FAR changes contained the Part 12 D&F. Eleven of the orders contained the less rigorous FAR Part 16 version which would be properly used in conjunction with the purchase of noncommercial services using T&M contracts, and 6 had no D&F, as shown in table 6.

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<sup>35</sup> 71 Fed. Reg. 74,667 (Dec. 12, 2006). We note that the September 20, 2004, advance notice of proposed rulemaking (ANPR), which solicited comments that could be used to assist in implementing section 1432 of the National Defense Authorization Act for Fiscal Year 2004 stated that "This ANPR is not intended to affect the special ordering procedures issued by the GSA pursuant to FAR 8.402.... [Schedules program] policies regarding the placement of orders on a T&M and [labor hour] basis will be conformed to the FAR when FAR coverage is finalized." 69 Fed. Reg. 56,316 (Sept. 20, 2004).

<sup>36</sup> See Subpart 8.4.

**Table 6: Number and Type of D&Fs for GSA Orders in our Sample Awarded After the FAR Part 12 D&F Requirement Became Effective.**

Agency	GSA schedule orders				Total
	Complete Part 12 D&F	Partial Part 12 D&F	Part 16 D&F	No D&F	
Air Force	0	0	0	0	0
Army	0	0	4	1	5
Navy	0	0	4	1	5
DOJ	1	0	0	0	1
HHS	0	0	0	0	0
NASA	0	0	0	0	0
VA	1	0	3	4	8
<b>Total</b>	<b>2</b>	<b>0</b>	<b>11</b>	<b>6</b>	<b>19</b>

Source: GAO analysis of data from agency contract files.

Note: FAR Subpart 8.4 does not specifically require a D&F. However, GSA ordering procedures require the ordering agency to make a determination that it is not possible at the time of placing the order to estimate accurately the extent or duration of the work or to anticipate costs with any reasonable degree of confidence.

Further, the FAR Part 12 requirement to document ceiling price changes on T&M contracts is not included in FAR Subpart 8.4, which pertains to schedule purchases. We found a few GSA orders at the VA location we visited that had ceiling price increases with no documentation on why the increase was in the best interest of the VA. For example, one order for information technology support services increased from \$3.5 million to almost \$4.8 million with minimal explanation as to why this increase occurred.

GSA policy officials told us that the statutory authority that created the schedules program is unique and allows the administrator the flexibility to decide what procedures to apply to the schedules program.<sup>37</sup> They noted, however, that they were planning to issue a procurement information notice in the spring of 2009 to put in place a Part 12 D&F for the entire GSA schedules program. It is not clear how this D&F will address the specific elements required by Part 12 of the FAR, or how it will act as a safeguard to ensure that each agency using GSA's schedule contracts has made the necessary determination that no other contract type is suitable.

<sup>37</sup> 40 U.S.C § 501.

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On March 6, 2009, we requested a legal opinion from GSA on the applicability of FASA section 8002(d), as amended by section 1432 of SARA, and the implementing FAR section 12.207(b) D&F requirement to the GSA schedules program. In its April, 15, 2009, response, GSA stated that the statutory language of FASA is not explicit and is unclear regarding applicability of the FASA provisions to the GSA schedules program, and therefore concluded that applicability is uncertain with regard to T&M commercial services contracts and orders under the program. In this regard, GSA recognized congressional concerns expressed regarding the use of T&M contracts for commercial services, which in some cases have led to inefficient and costly procurements. Specifically, GSA recognized the concern of the Senate Armed Services Committee that T&M commercial services contracts “are potentially subject to abuse because . . . it [is] very difficult to ensure that prices are fair and reasonable.” GSA stated, however, that it “has exercised the agency’s authority over the Schedules program to create safeguards so as to mitigate the issues presented by T&M commercial services contracts” and that existing provisions in the GSA Acquisition Regulation (GSAR) and FAR Subpart 8.4 “satisfy any concerns about the use of T&M orders in the Schedules program.”

It is not apparent to us that the regulations cited by GSA provide the government with risk mitigation equivalent to that provided by the Part 12 D&F requirement that T&M contracts will only be used when no other contract type is suitable. For example, GSA points to the FAR Section 8.4 requirement for the ordering activity to document the rationale for using other than a firm-fixed price order for services.<sup>38</sup> This documentation requirement is minimal, requiring only the “rationale” for using other than a firm-fixed price order rather than the more detailed rationale required in FAR Part 12 to demonstrate that there is no other suitable contract type. GSA also points to two existing price reasonableness requirements as safeguards: (1) the GSAR requirement that before a schedule contract is awarded, the GSA contracting officer must determine that the prices offered are fair and reasonable<sup>39</sup> and (2) the FAR requirement that the ordering activity contracting officer must consider the level and mix of labor proposed and determine that the total price of the schedule order is

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<sup>38</sup> FAR § 8.405-2.

<sup>39</sup> GSAR § 538.270.

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reasonable.<sup>40</sup> Again, these provisions do not address the more detailed rationale required in FAR Part 12.

We see no reason why the concerns which led Congress to require the Part 12 safeguards for the use of T&M contracts would be any less compelling in those instances in which an agency proposes to use a GSA schedule to obtain commercial services on a T&M basis. GSA did not provide any rationale why T&M contracts and orders for commercial services should be treated differently under the GSA schedules program, or be subject to fewer safeguards than those purchased outside of the GSA schedules program where the more heightened FAR section 12.207 requirements would be required. Further, we note that in section 8002(d) of FASA, as amended, there is no indication that the D&F requirement cannot apply to the purchase of any commercial item or service to include items or services available for purchase under the GSA schedules program.

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## Conclusion

The FAR Part 12 D&F requirement for the use of T&M contracts to acquire commercial services helps to ensure that this contract type is used only when no other contract type is suitable and to instill discipline in the determination of contract type with a view toward managing the risk to the government. The general lack of awareness of this requirement among contracting officers across all agencies in our review—more than 2 years after its implementation—coupled with the failure of management to detect the lack of compliance with this key safeguard suggests that further actions are necessary. In addition, miscoding of labor-hour contracts as fixed-price, when based on a misunderstanding about this contract type, potentially understates the risk to the government. Further, the fact that the safeguards put in place by Congress are not applied to GSA schedule contracts or orders raises concerns that the safeguards are not being used for the vast majority of T&M contracts for commercial services. When these safeguards are not used, the government may be assuming more risk than necessary.

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<sup>40</sup> FAR § 8.405-2(d).

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## Recommendations for Executive Action

To help ensure that the risks associated with T&M contracts are understood and that safeguards are followed and to ensure consistency in the use of T&M contracts regardless of which part of the FAR authorizes their use, we recommend that the Administrator of the Office of Federal Procurement Policy take the following three actions:

- Take steps to:
  - amend FAR Subpart 16.6 (T&M, Labor-Hour and Letter Contracts) and FAR Subpart 16.2 (Fixed-Price Contracts) to make it clear that contracts with a fixed hourly rate and an estimated ceiling price are T&M or labor-hour contracts, not fixed-price-type contracts and
  - amend FAR Subpart 8.4 (pertaining to the GSA schedules program) to explicitly require the same safeguards for commercial T&M services—i.e., the FAR Part 12 D&F and the justification for changes to the ceiling price—that are required in FAR section 12.207.
- Provide guidance to contracting officials on the requirements in FAR section 12.207 for the detailed D&F for T&M or labor-hour contracts for commercial services and encourage agencies to provide training regarding the D&F requirement.

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## Agency Comments and Our Evaluation

We requested comments on a draft of this report from OFPP, NASA, HHS, GSA, DOD, VA, and DOJ. In oral comments on a draft of this report, OFPP's Acting Administrator concurred with our recommendations. In written comments, included in appendix II, NASA stated that the report provides a balanced view of the issues. HHS also provided written comments. Although our recommendations were directed at OFPP, HHS stated that it agrees with them and outlined several steps it is taking to reinforce the need for its acquisition community to comply with requirements for T&M and other contract types. HHS's comments are included in appendix III. In comments provided via e-mail, DOD's Director, Defense Procurement and Acquisition Policy, concurred with our findings related to DOD contracts. The Director stated that DOD fully supports the objectives of promoting awareness and compliance with existing requirements related to the safeguards employed to ensure that T&M contracts are used only when justified.

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GSA, DOJ, and VA provided no comments.

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We are sending copies of this report to interested congressional committees; the Secretaries of Defense, Justice, Veterans Affairs, and Health and Human Services; the Administrators of the General Services Administration, Office of Federal Procurement Policy, and NASA. In addition, this report will also be available at no charge on GAO's Web site at <http://www.gao.gov>.

If you or your staff have any questions about this report or need additional information, please contact me at (202) 512-4841 or [huttonj@gao.gov](mailto:huttonj@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Staff acknowledgements are provided in appendix IV.



John Hutton, Director  
Acquisition and Sourcing Management

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*List of Committees*

The Honorable Carl Levin  
Chairman  
The Honorable John McCain  
Ranking Member  
Committee on Armed Services  
United States Senate

The Honorable Joseph I. Lieberman  
Chairman  
The Honorable Susan M. Collins  
Ranking Member  
Committee on Homeland Security and Governmental Affairs  
United States Senate

The Honorable Ike Skelton  
Chairman  
The Honorable Howard P. McKeon  
Ranking Member  
Committee on Armed Services  
House of Representatives

The Honorable Edolphus Towns  
Chairman  
The Honorable Darrell Issa  
Ranking Member  
Committee on Oversight and Government Reform  
House of Representatives

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# Appendix I: Scope and Methodology

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The objectives of this review were to assess (1) the extent to which agencies have reported using time-and-materials (T&M) contracts and General Services Administration (GSA) schedule T&M orders for commercial services and what they are acquiring using this contract type, (2) the degree to which agencies complied with the FAR Part 12 safeguards and (3) the applicability of these safeguards to the GSA schedule program. To address these objectives, we identified through the Federal Procurement Data System-Next Generation (FPDS-NG) all reported T&M contracts and orders—including GSA schedule orders—that were coded as using commercial item acquisition procedures from October 1, 2001, to June 30, 2008. We then selected five federal departments to review—based primarily on their high-dollar obligations and high numbers of contract actions—which represent 97 percent of total obligations coded as T&M contracts awarded using commercial item procedures for this time period:

- Department of Defense (DOD)
- Department of Health and Human Services (HHS)
- Department of Justice (DOJ)
- National Aeronautics and Space Administration (NASA)
- Department of Veterans Affairs (VA)

While the focus of our engagement was non-GSA contracts awarded after the February 2007 changes to the FAR, we also reviewed some GSA orders and contracts awarded by selected defense and civilian agencies prior to the FAR changes to get a better understanding of the circumstances of those procurements—such as whether the contracts were miscoded. We corroborated contract file information by interviewing over 100 contracting and policy officials at all of the selected agencies.

At DOD, we selected Air Force, Army, and Navy locations that had high reported obligations for commercial services using T&M contracts, coupled with the geographic location of the contracting activities. At each DOD location, we conducted a preliminary review of the contracts through the department’s electronic database system to corroborate FPDS-NG information. We conducted file reviews and interviewed contracting officials at the following locations:

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Army	<ul style="list-style-type: none"><li>• U.S. Army Medical Research Acquisition Activity, Fort Detrick; Frederick, Maryland</li></ul>
Air Force	<ul style="list-style-type: none"><li>• Air Force Intelligence, Surveillance, and Reconnaissance Agency, Lackland Air Force Base; San Antonio, Texas</li><li>• Air Combat Command Acquisition Management and Integration Center, Langley Air Force Base, Virginia (Contracts at this location were awarded prior to the FAR change)</li></ul>
Navy	<ul style="list-style-type: none"><li>• Fleet Industrial Supply Center, Norfolk; Norfolk, Virginia; Philadelphia, Pennsylvania; Portsmouth, New Hampshire; Millington, Tennessee; and Great Lakes, Illinois.</li></ul>

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At the Army's Medical Research Acquisition Activity, we randomly selected 20 non-GSA schedule contracts awarded after the February 2007 FAR Part 12 change, 5 non-GSA contracts awarded prior to the FAR change, and 5 GSA schedule orders issued after the FAR change. Ten of the 20 non-GSA contracts were indefinite-delivery contracts and 2 were blanket purchase agreements. For these, we reviewed 13 T&M orders under the indefinite-delivery contracts and 3 orders that had been placed under 1 of the blanket purchase agreements. At the Navy, we reviewed all of the non-GSA schedule contracts awarded during our selected time period of October 1, 2001, to June 30, 2008, which included 20 contracts awarded after the FAR change and 5 awarded prior to the FAR change.<sup>1</sup> We also reviewed 5 randomly selected GSA schedule orders that were awarded after the FAR change. At Lackland Air Force Base, we reviewed all non-GSA schedule contracts reported as T&M using commercial items acquisition procedures, including 1 awarded prior to the FAR change. We reviewed all 7 GSA schedule orders awarded after the FAR change that were reported as using T&M contracts for commercial services. At Langley Air Force Base, which had the largest obligations reported as T&M contracts for commercial services prior to the enactment of the Services Acquisition Reform Act in November 2003, we selected and reviewed 2 non-GSA T&M orders awarded prior to November 2003 that had been

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<sup>1</sup> We eliminated three Navy contracts that had been coded as non-GSA schedule contracts awarded by the Norfolk location from our review for different reasons: one turned out to be a blanket purchase agreement under a GSA schedule contract; one had been awarded by a different Navy location according to DOD's electronic contract database system; and finally, contracting officers at the Norfolk Navy Shipyard could not locate the third contract file.

recently modified to better understand the circumstances of these contracts. These 2 orders turned out to have been miscoded in FPDS-NG as having used commercial items acquisition procedures.

For the civilian agencies included in our scope, we reviewed all of the T&M contracts for commercial services reported in FPDS-NG during the October 2001 to June 2008 time period. We conducted file reviews and interviewed contracting officials at the following civilian agency components:

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Department of Justice	<ul style="list-style-type: none"><li>• Bureau of Alcohol, Tobacco, Firearms, and Explosives; Washington, D.C.</li><li>• Drug Enforcement Agency; Arlington, Virginia</li><li>• Federal Bureau of Investigation; Washington, D.C.</li><li>• Justice Management Division; Washington, D.C.</li><li>• Office of Justice Programs; Washington D.C.</li><li>• U.S. Marshals Service; Washington, D.C. and Oklahoma City, Oklahoma</li></ul>
Health and Human Services	<ul style="list-style-type: none"><li>• Centers for Disease Control and Prevention; Atlanta, Georgia</li><li>• Food and Drug Administration; Rockville, Maryland</li><li>• Health Resources and Services Administration; Rockville, Maryland</li><li>• Indian Health Service; Oklahoma City, Oklahoma; Phoenix, Arizona, and Window Rock, Arizona</li><li>• National Institutes of Health; Bethesda, Maryland and Research Triangle Park, North Carolina</li><li>• Program Support Center; Rockville, Maryland; Kansas City, Missouri; and Perry Point, Maryland</li><li>• Substance Abuse and Mental Health Services Administration; Rockville, Maryland</li><li>• Centers for Medicare and Medicaid Services; Baltimore, Maryland</li></ul>
NASA	<ul style="list-style-type: none"><li>• John H. Glenn Research Center; Cleveland, Ohio</li><li>• Goddard Space Flight Center; Greenbelt, Maryland</li></ul>
Veterans Affairs	<ul style="list-style-type: none"><li>• Cleveland Business Center; Cleveland, Ohio</li><li>• Acquisition Management Section; Austin, Texas</li></ul>

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Table 7 contains details about the distribution of our contract sample across the agencies in our review.

**Table 7: GAO Sample of T&M Contracts and Orders for Commercial Services Awarded Prior to and After the February 2007 FAR Change**

Agency	Non-GSA contracts and orders		GSA schedule orders		Total
	Pre-FAR change	Post-FAR change	Pre-FAR change	Post-FAR change	
Air Force	3	8	0	7	18
Army	5	28	0	5	38
Navy	4	20	0	5	29
Justice	5	7	0	1	13
Health and Human Services	2	20	4	0	26
NASA	0	1	1	0	2
Veterans Affairs	1	5	7	10	23
	<b>Total non-GSA contracts and orders</b>	<b>109</b>	<b>Total GSA schedule orders</b>	<b>40</b>	
<b>Total contracts and orders in sample</b>					<b>149</b>

Source: GAO file reviews.

Note: Our sample of contracts and orders was selected from FPDS-NG data from October 1, 2001, to June 30, 2008. "Pre-FAR change" means that the contract or order was awarded prior to the changes to FAR Part 12 effective on February 12, 2007; "Post-FAR change" means the contract or order was awarded after the FAR change effective date.

To identify the extent to which agencies have reported using T&M contracts and GSA schedule orders for commercial services, we used FPDS-NG data to determine the obligations reported as T&M awarded using FAR Part 12 commercial items acquisitions procedures between February 12, 2007, when the FAR change authorizing T&M contracts for commercial services went into effect, and December 31, 2008. We compared this figure to total reported federal obligations for services, obligations coded as having acquired commercial services, and obligations coded as T&M contracts and orders during the same time period in order to demonstrate the relative magnitude of T&M contracts for commercial services. We discovered that many GSA schedule orders for T&M services had been miscoded as having used FAR Part 12 procedures (when they had actually used procedures under FAR Subpart 8.4) and brought this issue to the attention of the Office of Federal Procurement Policy officials. To determine the full picture of T&M obligations for commercial services, we identified GSA schedule T&M orders that had not been coded as having used commercial item procedures. We also used FPDS-NG data to assess what proportion of the total reported T&M contracts for commercial services was purchased through the GSA schedules program.

To test the reliability of FPDS-NG data, we used information from the contract file and discussions with contracting officials. We confirmed that a contract was used to acquire commercial services by reviewing the contract for relevant commercial clauses (52.212-4—Contract Terms and Conditions—Commercial Items) and other contract file documentation—such as the acquisition plan or the standard contract form for commercial item acquisitions (SF 1449)—that indicated that commercial services were purchased. In some cases, in which the evidence in the files was not sufficient to make this determination, we confirmed that commercial services were acquired by speaking with the contracting officer. To confirm that a contract was T&M, we reviewed relevant contract documentation such as contract line item notations (CLIN) and invoices, spoke with contracting officers, and applied FAR descriptions of T&M or labor-hour contracts. To identify the types of services agencies are acquiring using T&M contracts for commercial services, we used FPDS-NG data to identify the top 10 commercial services purchased under T&M contracts from February 12, 2007, to December 31, 2008. We also analyzed the statements of work from selected contracts in our sample to provide more detailed examples of the types of services agencies are acquiring using these contracts.

When we discovered that some contracting officers had mistakenly interpreted the fixed labor rate component of T&M contracts to mean that these contracts are fixed-price type contracts, we decided to review a nonrepresentative sample of contracts labeled as fixed-price in FPDS-NG that were coded for the same types of services as the T&M contracts for commercial services identified in our sample. Using DOD's electronic database, we conducted a preliminary review of 60 DOD contracts that had been coded as fixed-price contracts and selected 16 that possibly could have been T&M, based primarily on our interpretation of language in the contract that suggested that the contract was not fixed-price. To confirm whether these contracts were T&M, we spoke with contracting officials and requested additional contract documentation for 10 contracts at Lackland Air Force Base and 6 managed by the Fleet and Industrial Supply Center at Norfolk Naval Base. Of these 16 contracts, 3 were confirmed to be incorrectly coded as fixed-price in FPDS-NG due to data entry errors, and should have been coded as T&M contracts.

To determine the degree to which agencies' use of FAR Part 12 to acquire T&M services complies with the safeguards as incorporated in the FAR, we reviewed the contract files for our sample contracts. Specifically, we assessed: 1) whether the files contained a determination and findings (D&F) stating that no other contract type is suitable; 2) if applicable, the

extent to which the D&F included FAR Part 12 or Part 16 requirements for T&M contracts; and 3) whether ceiling price increases included written documentation from the contracting officer that they were in the best interest of the procuring agency. We determined that a D&F met all the criteria if it made reference to FAR Section 12.207 and at least mentioned all of the required elements. For example, if a D&F stated the outcomes of the market research conducted but did not describe the research conducted, we still gave credit for having addressed the requirement in FAR Section 12.207 to describe the market research conducted. A partial Part 12 D&F included some but not all of the four required elements. We also reviewed federal and agency-specific acquisition guidance and regulations.

To determine the applicability of these safeguards to the GSA schedules program, we reviewed GSA's ordering guidance to agencies and to its own contracting officers and interviewed GSA policy and legal officials. We also sent a letter on March 6, 2009, to GSA's General Counsel seeking an opinion on the applicability of Section 8002(d) of FASA, as amended, and FAR Section 12.207 to the GSA schedules contracts. We received a response on April 15, 2009. Finally, we reviewed relevant past GAO and Inspectors General reports on T&M contracts and commercial contracts for context.

We conducted this performance audit from September 2008 to June 2009, in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

# Appendix II: Comments from NASA

National Aeronautics and  
Space Administration  
**Headquarters**  
Washington, DC 20546-0001



June 11, 2009

Reply to AIAA 09- Contract Management Division

Mr. John P. Hutton  
Director, Acquisition and Sourcing Management  
United States Government Accountability Office  
Washington, DC 20548

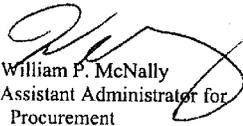
Dear Mr. Hutton:

Thank you for the opportunity to review draft report, "CONTRACT MANAGEMENT: Minimal Compliance with New Safeguards for Time-and-Materials Contracts for Commercial Services and Safeguards Have Not Been Applied to GSA Schedules Program," (GAO-09-579).

We found the report to be complete, concise, and accurate. In our opinion, it provides a balanced view of the issues related to the additional safeguards required to offset the potential risks associated with using time-and-material contracts to purchase commercial services. We do not have any technical comments to the draft report.

Again, thank you for the opportunity to provide comments on the draft report and for your continued interest in improving Government contract management.

Sincerely,

  
William P. McNally  
Assistant Administrator for  
Procurement

# Appendix III: Comments from the Department of Health and Human Services



DEPARTMENT OF HEALTH & HUMAN SERVICES

OFFICE OF THE SECRETARY

Assistant Secretary for Legislation  
Washington, DC 20201

JUN 5 2009

John P. Hutton  
Director  
Acquisition and Sourcing Management  
U.S. Government Accountability Office  
441 G Street NW  
Washington, DC 20548

Dear Mr. Hutton:

Enclosed are comments on the U.S. Government Accountability Office's (GAO) report entitled: "Contract Management: Minimal Compliance with New Safeguards for Time-and-Materials Contracts for Commercial Services and Safeguards Have Not Been Applied to GSA Schedules Program" (GAO-09-579).

The Department appreciates the opportunity to review this report before its publication.

Sincerely,

A handwritten signature in cursive script that reads "Barbara Pisaro Clark".

Barbara Pisaro Clark  
Acting Assistant Secretary for Legislation

Attachment

**GENERAL COMMENTS OF THE DEPARTMENT OF U.S. HEALTH AND HUMAN SERVICES (HHS) ON THE GOVERNMENT ACCOUNTABILITY OFFICE'S (GAO) DRAFT REPORT ENTITLED, "CONTRACT MANAGEMENT: MINIMAL COMPLIANCE WITH NEW SAFEGUARDS FOR TIME-AND-MATERIALS CONTRACTS FOR COMMERCIAL SERVICES AND SAFEGUARDS HAVE NOT BEEN APPLIED TO GSA SCHEDULES PROGRAM" (GAO-09-579)**

HHS agrees with GAO's recommendations to the Administrator of the Office of Federal Procurement Policy. We will reinforce the need for our acquisition community to comply with requirements for T&M and other contract types. This will be accomplished through: (a) conducting additional training; (b) discussing GAO's findings and sharing successful practices at our quarterly Executive Committee for Acquisition meetings; (c) incorporating Commercial Acquisition and FAR Part 12 D&F requirements in our Procurement Management Review protocols; and (d) verifying applicable FPDS coding.

Further, HHS issued mandatory, standardized contract file checklists to its acquisition community in May 2009. These checklists are intended to: (a) facilitate the consistent and logical placement of required supporting documentation in contract files; (b) expedite the review of acquisition files and the conduct of procurement management reviews; (c) serve as a learning tool for contracting staff; and (d) foster consistent implementation of acquisition regulations, policies, and procedures. The checklists encompass all relevant Federal and HHS acquisition guidance, including guidance pertaining to the requirements identified in GAO's draft report (e.g., FAR Part 12 D&F).

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# Appendix IV: GAO Contact and Staff Acknowledgements

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## GAO Contact

John Hutton, (202) 512-4841 or [huttonj@gao.gov](mailto:huttonj@gao.gov)

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## Acknowledgements

In addition to the individual named above, Michele Mackin, Assistant Director; Nicholas Alexander; Keya Chateaufeuf; and Tatiana Winger made key contributions to this report. Marie Ahearn, Arthur James, Jr., Julia Kennon, and Kenneth Patton also made contributions.

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