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Opportunities Continue for GSA to Improve Pricing of Multiple Award Schedules Contracts

Statement of David E. Cooper, Director
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Highlights of [GAO-05-911T](#), a report to the Subcommittee on Federal Financial Management, Government Information, and International Security, Committee on Homeland Security and Governmental Affairs, U.S. Senate

Why GAO Did This Study

Each year, federal agencies spend billions of dollars to buy commercial products and services through the General Service Administration's (GSA) Multiple Award Schedules program. The program has grown significantly over the past several years. Currently, federal agencies can directly purchase, through more than 16,000 schedule contracts, over 8 million products from more than 10,000 commercial vendors. In fiscal year 2004, purchases from these contracts totaled more than \$32 billion.

The multiple award schedules program is designed to take advantage of the government's significant buying power. To maximize savings, GSA negotiates discounts that are equal to or greater than those given to the vendor's most favored customers. This testimony focuses on GSA's historic use of two proven negotiation tools to improve the pricing of schedules contracts—pre-award audits and postaward audits of pre-award information. Pre-award audits allow GSA to avoid potential overpricing by verifying vendor pricing information before contracts are awarded. Postaward audits allow GSA to identify overpricing of awarded contracts and recover overcharges.

What GAO Recommends

In its February 2005 report, GAO made three recommendations aimed at improving the multiple award schedules contracts pricing.

www.gao.gov/cgi-bin/getrpt?GAO-05-911T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact David E. Cooper at (202) 512-4841 or cooperd@gao.gov.

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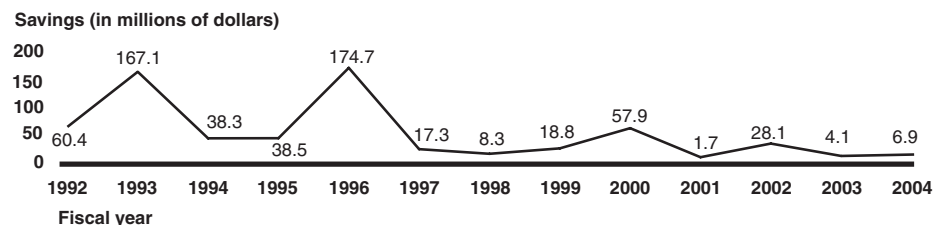
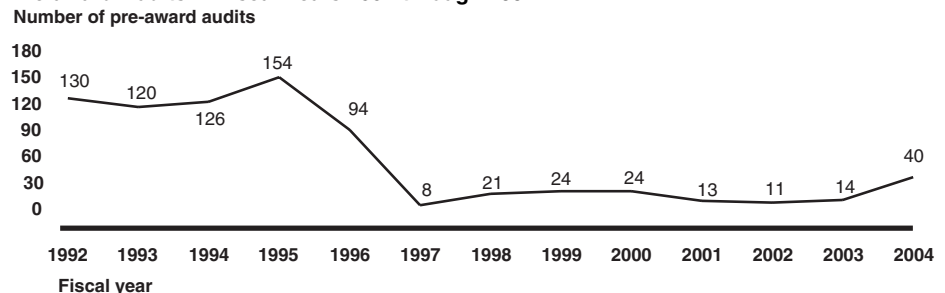
Opportunities Continue for GSA to Improve Pricing of Multiple Award Schedules Contracts

What GAO Found

Historically, GSA has used pre-award and postaward audits sporadically, thereby minimizing its ability to avoid excessive pricing and recover overcharges and potentially save millions of federal dollars. For more than 25 years, GAO has reported on GSA's multiple award schedules program pricing problems. In March 1977, we reported that pre-award information on 6 of 15 contract proposals was not accurate, complete, or current. In 1979, we again reported that pricing information submitted by some vendors was unreliable. Moreover, only 1 pre-award audit and 10 postaward audits had been conducted during fiscal years 1977 and 1978 of which 9 found inaccurate sales information had been reported by vendors or the availability of better discounts had not been disclosed. These problems continued throughout the 1980s. In the early 1990s, GSA made good use of pre-award and postaward audits, negotiating nearly \$480 million in cost savings and recovering about \$90 million in vendor overcharges over 5 years.

However, in August 1997, GSA revised its acquisition regulations and effectively eliminated the use of postaward audits. While GSA expected pre-award audits to increase, this increase never materialized. In August 2001, the GSA Inspector General reported that GSA was not consistently negotiating most favored customer pricing. For just one contract, the Inspector General projected that over the contract's term, GSA customers would pay nearly \$40 million more than they should have. In February 2005, we completed our most recent review of the multiple award schedules program and found that pricing problems persist and that the number of pre-award audits continued to decline. We concluded that GSA was continuing to miss opportunities to save hundreds of millions of dollars.

Pre-award Audits in Fiscal Years 1992 through 2004



Source: GSA Inspector General data.

Chairman Coburn and Members of the Subcommittee:

Thank you for inviting me here today to discuss the General Services Administration's (GSA) use of pre-award and postaward audits in pricing its multiple award schedules contracts. Each year, federal agencies spend billions of dollars to buy commercial products and professional services through GSA's multiple award schedules program. The program is designed to take advantage of the government's significant buying power when purchasing a wide range of commercially available products—such as office furniture and supplies, personal computers, and tools—and a variety of professional services. Through more than 16,000 contracts, federal agencies can directly purchase more than 8 million products from more than 10,000 commercial vendors. The multiple award schedules program has grown significantly over the past several years. In fiscal year 2004, federal agencies purchased more than \$32 billion of products and services through the program.

To get the most out of each taxpayer dollar, GSA seeks to leverage the government's immense buying power by negotiating discounts from the vendor's price list that are equal to or greater than the vendor's most favored customers.¹ These negotiations have a direct bearing on how economically government agencies procure products and services. Today, my statement will focus on GSA's historic use of two proven negotiation tools to improve the pricing of schedules contracts—pre-award audits and postaward audits of pre-award information. Pre-award audits allow GSA contract negotiators to avoid potential vendor overpricing by verifying pricing information before contracts are awarded. Postaward audits allow negotiators to identify overpricing of awarded contracts and recover overcharges.

In summary, GSA has used these two key price negotiation tools on a limited basis. When GSA has used pre-award and postaward audits, it has been able to avoid or recover hundreds of millions of dollars in overcharges. In recent years, however, the use of these pricing tools has declined dramatically—despite dramatic increases in program sales. Consequently, GSA has less assurance that vendor-supplied pricing information is accurate, complete, and current, and its ability to deter overpricing and recover overcharges has been minimized. By delaying

¹The most favored customer is a customer or category of customers that receives the best discounts from the vendor's commercial price list. 48 C.F.R. 538.270(a).

action to address its contract pricing problems, GSA continues to miss opportunities to minimize prices paid for goods and services and save significant sums of federal dollars.

Background

GSA established the Federal Supply Schedule (FSS) program in 1949 to facilitate federal agencies' purchase of common products and services from commercial vendors through schedule contracts. The multiple award schedules program, the largest FSS program, was designed to provide agencies with a simplified method for purchasing varying quantities of a wide range of commercially available products, such as office furniture and supplies, personal computers, scientific equipment, network support, and various professional services.² The schedules program provides advantages to both federal agencies and vendors. By using this simplified method of procurement, agencies can avoid using other more time-consuming and administratively costly procurement methods. Vendors receive wider exposure of their commercial products and services and expend less effort to sell them.

In administering the multiple award schedules program, GSA is responsible for ensuring that negotiated prices reflect the government's aggregate buying power. GSA contracting officials seek discounts from a vendor's price list that are equal to or greater than the vendor's most favored customer's discounts. GSA awards contracts to multiple vendors supplying comparable commercial products and services. Federal agencies order products and services directly from the vendors that best meet their needs. Prices paid by federal agencies include a fee for GSA to recover program costs, including contract administration and program support.³

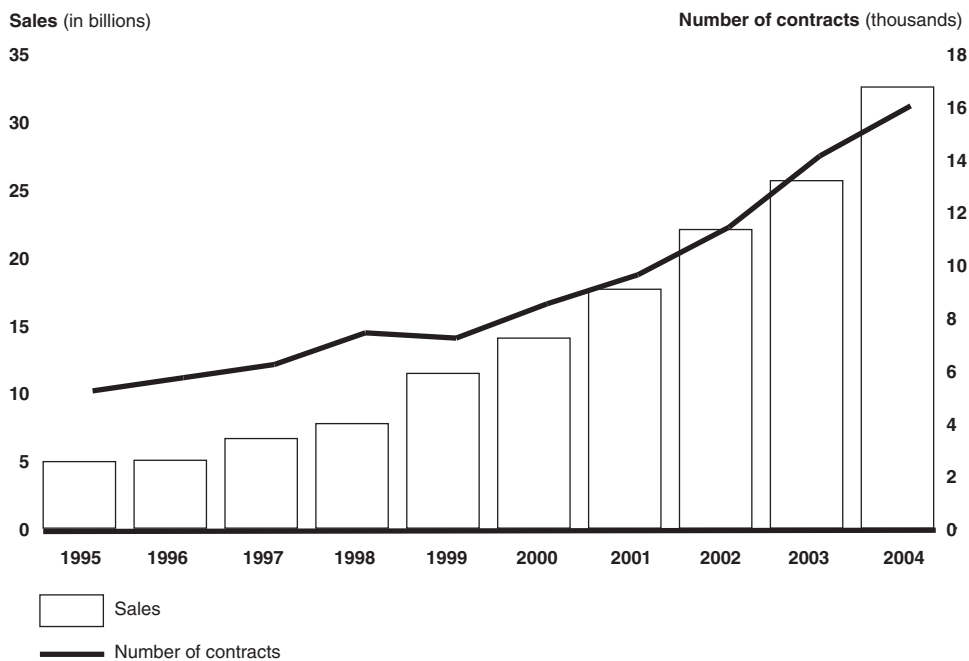
In the mid-1990s, GSA had about 5,200 schedules contracts. By fiscal year 2004, this number had increased to over 16,000 contracts. As the number of contracts offering products and services to federal agencies increased, the sales volume skyrocketed. Between fiscal years 1995 and 2004,

²In 1960, GSA delegated authority to the Veterans Administration to manage and award schedules contracts for all medical products and services needed throughout the federal healthcare system.

³The GSA schedule fee in fiscal year 2005 is 0.75 percent of negotiated item or service price. 68 Fed. Reg. 41286 (July 11, 2003).

program sales increased more than sixfold, from \$4.9 billion to about \$32.5 billion (see fig. 1).

Figure 1: Multiple Award Schedules Sales Volume and Contracts, Fiscal Years 1995 through 2004



Source: GAO analysis of GSA data.

Because prices that agencies pay for schedule products and services are the result of negotiations between GSA and individual vendors, the pricing of products and services being offered is key to the contract negotiation process. GSA contracting officials use various tools to analyze vendor offers and establish negotiation objectives. Tools commonly used include market research, sales histories, invoices and references, and competitor price lists. Of all the pricing tools available for contract negotiation, two tools—pre-award audits and postaward audits of pre-award information—are specifically designed to protect the government from overpricing. Pre-award audits enable contract negotiators to verify that vendor-supplied pricing information is accurate, complete, and current before the contract is awarded. Postaward audits serve as a deterrent to overpricing and a primary tool for recovering vendor overcharges.

Historically, GSA Has Not Consistently Made Good Use of Pre-award and Postaward Audits

GSA's use of pre-award audits and postaward audits of pre-award information has been sporadic—a finding we have reported for more than 25 years. For example, in March 1977, we reported that although sales from multiple award schedules contracts amounted to \$840 million, vendor proposals were rarely independently audited and the veracity of the information submitted was suspect.⁴ We found that sales and discount information submitted on 6 of 15 contract proposals was not accurate, complete, and current. Further, we found that 25 pre-award audits done in fiscal years 1973 and 1974 had resulted in recommendations of \$962,000 in savings. Eighteen postaward audits done in the same years resulted in GSA claims of more than \$1.4 million. In 1979, we again reported that price information submitted by some vendors was unreliable.⁵ Also, our comparison of 29 products available through four states' annual contracts, as well as GSA schedules, found that prices were on average 20 percent to 57 percent lower under the state contracts. We estimated that had GSA obtained the same discounts as did the states, \$5.8 million would have been saved in fiscal year 1978 on purchases of calculators, dictating equipment, typewriters, and lamps from the same manufacturers. Moreover, of the 11 audits (1 pre-award and 10 postaward) that had been done during fiscal years 1977 and 1978, all but 2 found inaccurate sales information had been reported by vendors or the availability of better discounts had not been disclosed.

Pricing problems continued throughout the 1980s, and GSA's use of pre-award audits and postaward audits of pre-award information was limited. For example, in 1986, we again reviewed GSA's price negotiations for the multiple award schedules program, which at that time consisted of about 3,300 contracts with sales of about \$2.3 billion. Our review of 20 contracts found that while the prices GSA obtained appeared to be fair and reasonable, action was needed to obtain better prices.⁶ On one multiple award schedules contract, where the vendor did not offer the government discounts comparable to the most favored customer, a reopening of contract negotiations resulted in an estimated savings of \$1.6 million. We also found that the number of pre-award audits decreased between fiscal

⁴GAO, *Federal Supply Service Not Buying Goods at Lowest Possible Price*, [PSAD-77-69](#) (Washington, D.C.: Mar. 4, 1977).

⁵GAO, *Ineffective Management of GSA's Multiple Award Schedule Program—A Costly, Serious, And Longstanding Problem*, [PSAD-79-71](#) (Washington, D.C.: May 2, 1979).

⁶GAO, *GSA Procurement: Are Prices Negotiated for Multiple Award Schedules Reasonable?*, [GAO/GGD-86-99BR](#) (Washington, D.C.: July. 8, 1986).

years 1984 and 1985. The decrease was attributed to reductions in the Inspector General's staff, a shift in resources to audits of higher dollar value contracts, and the change from single-year to multiple year contracts. In response to our concern about the continuing decline in the number of pre-award audits, GSA agreed to take actions to provide adequate audit coverage, including shifting resources from other GSA offices to the Inspector General's office, as well as within the office, and an increase in the Inspector General's fiscal year 1987 budget.

In the early 1990s, schedules sales remained relatively stable, ranging between \$4 billion and \$5 billion, annually. During this period, GSA successfully performed a significant number of pre-award and postaward audits. For example, from fiscal years 1992 through 1996, the GSA Inspector General conducted 624 pre-award audits—an average of 125 each year. These pre-award audits resulted in nearly \$480 million in negotiated cost savings for GSA's customers. Additionally, from fiscal years 1990 through fiscal year 1994, the GSA Inspector General reported that it recovered an average of \$18 million each year in vendor overcharges. Most of these postaward audit recoveries were the result of vendor failure to provide accurate, complete, and current information in the negotiation of their contracts and their failure to report and offer price reductions.

Despite Skyrocketing Sales, Pricing Problems and the Overall Decline in the Use of Pre-award Audits Have Continued

In August 1997, GSA revised its acquisition regulations to expand access to commercial products and services and implement greater use of commercial buying practices. As part of this revision, GSA specifically removed⁷ language from the examination of records clause that automatically granted postaward audit rights for pre-award pricing information in every schedules contract.⁸ To offset the reduction in these postaward audits, GSA proposed to increase emphasis on the use of pre-award audits. According to GSA, this approach would provide the contracting officer a mechanism for verifying information submitted by vendors and avoid pricing problems instead of uncovering problems after contract award. However, recent GSA Inspector General and GAO reviews have shown that GSA's long-standing pricing problems have continued and the plan to increase the use of pre-award audits never materialized.

GSA's Inspector General and GAO Continue to Identify Pricing Problems

In August 2001, the GSA Inspector General reported that while schedules program sales had grown dramatically, certain program fundamentals—including pricing objectives and other pricing tools—had been marginalized.⁹ Specifically, the Inspector General found that contracting officers were not consistently negotiating most favored customer pricing or adequately performing price analyses. For example, the Inspector General reported that a major distributor of information technology products sold its top 10 GSA-selling models to commercial customers at an average price that was 6 percent lower than the price offered to federal agencies. The Inspector General projected that over the contract's term, GSA customers would pay nearly \$40 million more for these products than they should.

In February 2005, we completed our most recent review of the multiple awards schedules program and found that contract pricing continues to be

⁷The revised regulations allow the contracting officers to modify contract language to provide for postaward access to vendor-supplied information if they determine there was a likelihood of significant harm to the government without such access, and obtain the senior procurement executive's approval.

⁸GSA, however, retained the right to conduct postaward audits for overbilling, billing errors, and compliance with the Price Reduction and Industrial Funding Fee clauses. GSAR 552.215-71.

⁹General Services Administration, Office of Inspector General, *MAS Pricing Practices: Is FSS Observing Regulatory Provisions Regarding Pricing?* (Washington, D.C.: Aug. 24, 2001).

a problem.¹⁰ Table 1 summarizes the extent of the problems found with 62 contracts in June 2004.

Table 1: Contract Documentation Weaknesses of Schedules Contracts by Acquisition Center

| Acquisition center | Contracts reviewed | Contracts that did not meet pricing documentation requirements ^a | Contracts with inadequate price analysis | Contracts that did not fully document price negotiations | Contracts that did not identify most favored customer price |
|--|--------------------|---|--|--|---|
| Center for Facilities Maintenance & Hardware | 2 | 2 | 0 | 0 | 0 |
| General Products Acquisition Center | 10 | 5 | 5 | 0 | 0 |
| Information Technology Center | 10 | 8 | 5 | 7 | 4 |
| Management Services Center | 10 | 10 | 9 | 9 | 4 |
| National Furniture Center | 10 | 2 | 1 | 2 | 1 |
| Office Supplies & Administrative Services Acquisition Center | 10 | 9 | 6 | 6 | 2 |
| Services Acquisition Center | 10 | 1 | 0 | 0 | 1 |
| Total^b | 62 | 37 | 26 | 24 | 12 |

Source: GAO analysis of GSA data.

^aContract file documentation is to clearly establish that the vendor-supplied pricing information was accurate, complete, and current; that the vendor information was relied upon during the negotiations; adequate price analysis was conducted; reasonable negotiation objectives were established; the leverage of the total government's requirements was considered in negotiating prices; and the prices awarded were determined fair and reasonable.

^bEach contract could have all, some, or none of the weaknesses listed in each of the columns.

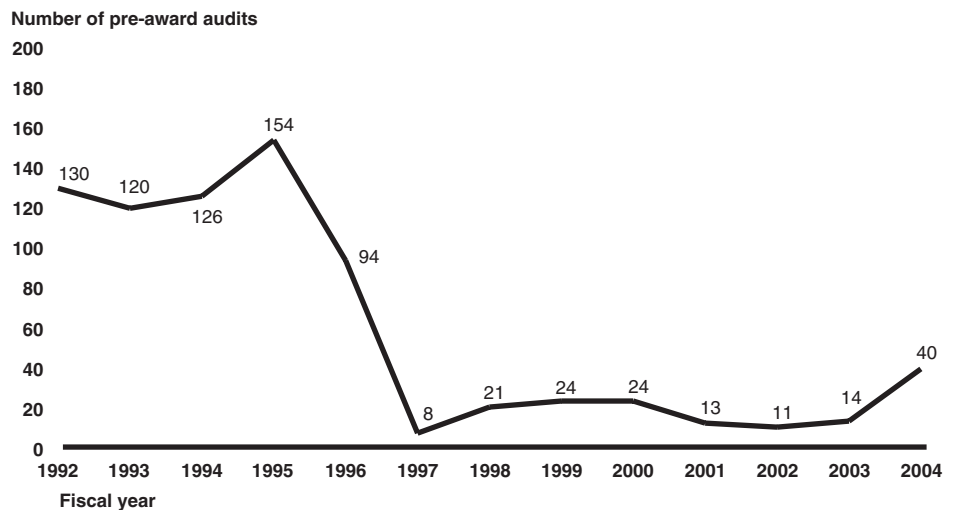
We found that a GSA review of 62 contract files identified 37 contracts—nearly 60 percent—that lacked sufficient documentation to clearly establish that the contracts were effectively negotiated. Twenty-six of the 62 contracts—roughly 40 percent—lacked adequate price analyses or price negotiation documentation.

¹⁰GAO, *Contract Management: Opportunities to Improve Pricing of GSA Multiple Award Schedules Contracts*, GAO-05-229 (Washington, D.C.: Feb. 11, 2005).

Decline of Pre-award Audits Continued

Between fiscal years 1997 and 2004, GSA completed only 155 pre-award audits—an average of about 19 each year, compared to the average of 125 pre-award audits annually for the prior 5 years (see fig. 2). During this same 8-year period, schedules sales increased nearly five-fold from about \$6.6 billion in fiscal year 1997 to \$32.5 billion in fiscal year 2004.

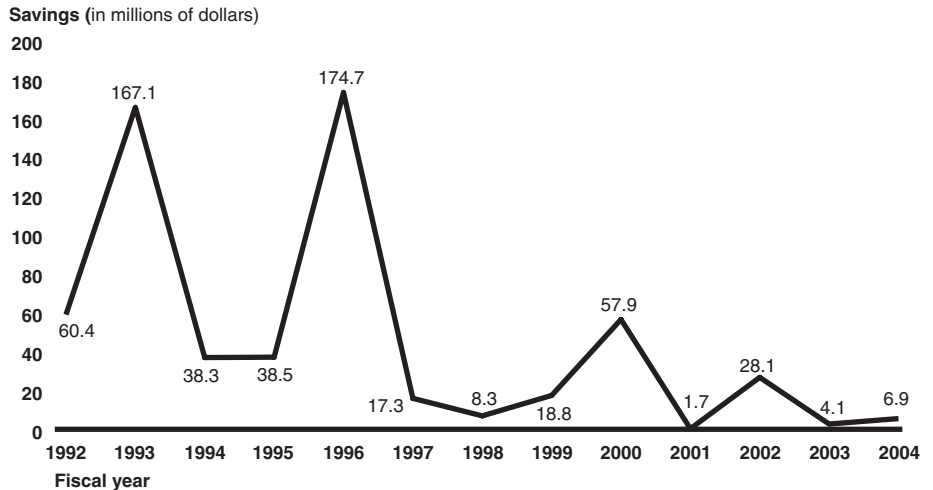
Figure 2: Pre-award Audits Conducted in Fiscal Years 1992 through 2004



Source: GSA Inspector General data.

As the number of pre-award audits performed continued to decline, so too did the amount of negotiated cost savings. Between fiscal years 1992 and 1997, the GSA Inspector General reported a total of nearly \$496 million in savings—an average of nearly \$83 million per year. Between fiscal years 1998 and 2004, the total savings reported had dropped to about \$126 million—an average of only \$18 million per year (see fig. 3).

Figure 3: Negotiated Cost Savings from Pre-award Audits Conducted in Fiscal Years 1992 through 2004



Source: GSA Inspector General data.

According to GSA Inspector General and contracting officials, the decline in pre-award audits was largely due an organizational culture that stresses making award decisions quickly and because pre-award audits were not emphasized institutionally in GSA. Also, GSA management officials told us that they believe increasing the contract length from 1 year in the mid-1990s to the 5 years of today has also limited pre-award audits because the number of opportunities for pre-award audits has been reduced. We believe, however, that the potential for pre-award audits is substantial. Since the mid-1990s, the number of schedules contracts awarded increased from about 5,200 in fiscal year 1995 to over 16,000 in fiscal year 2004, significantly increasing the potential for pre-award audits.

While conducting our review, we tested GSA's assertion that longer-term contracts reduced the opportunity for pre-award audits, applying GSA's guidance¹¹ to contract negotiators on when to request audit assistance. As we reported in February 2005, we found that 71 contracts awarded or extended in fiscal year 2003 met the pre-award audit threshold, but GSA

¹¹Procurement Information Bulletin (PIB) 03-4: Audit Assistance—Multiple Award Schedule (MAS) Contracts; General Services Administration, June 20, 2003. This guidance instructs contract negotiators to request audit assistance when the dollar value for estimated sales of a contract offer or extension exceeds \$25 million for the 5-year contract period.

only completed 14 pre-award audits—57 fewer than we identified as potential audits. In fiscal year 2004, GSA selected 55 contract offers for pre-award audits. The GSA Inspector General completed 40 of these audits.

In our most recent review, we also found that GSA has not conducted postaward audits of pre-award information since 1997—when GSA revised its policy on the use of such audits. The revised policy had the effect of eliminating the use of postaward audits. With the dramatic increase in sales and the continuing decline in pre-award audits, the potential for significant recoveries of vendor overcharges could be substantial.

Recent GSA Actions to Improve Price Negotiations

In our February 2005 report, we made three recommendations aimed at helping GSA ensure that prices are effectively negotiated for schedules contracts. We recommended that the GSA Administrator (1) ensure that pre-award audits are conducted when the threshold is met for both new contract offers and contract extensions, (2) develop guidance to help contracting officers determine when postaward audits are needed, and (3) direct GSA program management to revise its quality control program to (a) determine the underlying causes for contract pricing deficiencies and (b) develop appropriate plans to implement corrective actions.

GSA management officials agreed with our recommendations, and stated that GSA would

- continue to work with the Inspector General to increase and improve the number of pre-award audits,
- publish an advance notice of proposed rulemaking in the *Federal Register* to request comments on the role of postaward audit reviews in the acquisition process,¹² and
- evaluate the results of the fiscal year 2004 contract file review and that this evaluation would involve a discussion and identification of the underlying reasons for any weaknesses.

¹²GSA published advance notice of proposed rulemaking in the *Federal Register* on March 11, 2005, requesting comments on whether postaward audit provisions should be included in its FSS contracts and governmentwide acquisition contracts. The *Federal Register* notice was amended on March 17, 2005 (70 FR 13005) and again on April 12, 2005 (70 FR 19051) to extend the comment period until May 10, 2005, and to add further comments concerning the Examination of Records clause at GSAR 552.215-71.

We believe that GSA's actions are a good first step toward addressing its long-standing pricing problems with multiple award schedules contracts. However, unless these actions are effectively implemented the risk of pricing problems will continue.

In conclusion, while GSA's schedules program has provided the government with a more flexible and cost-effective approach to buying commercial items, our work has shown that the program has long been fraught with problems of contract overpricing—resulting in millions of taxpayer dollars being wasted. Historically, pre-award and postaward audits have proven their value in deterring overpricing and recovering vendor overcharges. Until GSA takes steps to ensure the appropriate use of available pricing and negotiation tools, it will continue to miss opportunities to save the government hundreds of millions of dollars in the procurement of goods and services.

Mr. Chairman and Members of the Subcommittee, this concludes my prepared statement. I will be happy to address any questions you may have at this time.

Contact and Acknowledgments

For further information, please contact David E. Cooper at (202) 512-4841 or by e-mail at cooperd@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this testimony. Individuals making key contributions to this testimony include James Fuquay, Sanford Reigle, Victoria Klepacz, Karen Sloan, and Sylvia Schatz.

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