

Department of Homeland Security **Office of Inspector General**

Department of Homeland Security Compliance
with the Federal Acquisition Regulation
Revisions on Proper Use and Management of
Cost-Reimbursement Contracts





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Department of Homeland Security

Washington, DC 20528 / www.oig.dhs.gov

SEP 28 2012

MEMORANDUM FOR: Nick Nayak
Chief Procurement Officer
Department of Homeland Security

FROM: Anne L. Richards *Anne L. Richards*
Assistant Inspector General for Audits

SUBJECT: *Department of Homeland Security Compliance with the
Federal Acquisition Regulation Revisions on Proper Use and
Management of Cost-Reimbursement Contracts*

Attached for your action is our final report, *Department of Homeland Security Compliance with the Federal Acquisition Regulation Revisions on Proper Use and Management of Cost-Reimbursement Contracts*. We incorporated the formal comments from the Office of the Chief Procurement Office in the final report.

The report contains two recommendations aimed at improving the Department's use and management of other than firm-fixed-price contracts. Your office concurred with the recommendations. Based on information provided in your response to the draft report, we consider the recommendations resolved. Once your office has fully implemented the recommendations, please submit a formal closeout letter to us within 30 days so that we may close the recommendations. The memorandum should be accompanied by evidence of completion of agreed-upon corrective actions.

Consistent with our responsibility under the *Inspector General Act*, we are providing copies of our report to appropriate congressional committees with oversight and appropriation responsibility over the Department of Homeland Security. We will post the report on our website for public dissemination.

Please call me with any questions, or your staff may contact John E. McCoy II, Deputy Assistant Inspector General for Audits, at (202) 254-4100.

Attachment



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Abbreviations

COR	Contracting Officer Representative
COTR	Contracting Officer Technical Representative
DCMA	Defense Contract Management Agency
DHS	Department of Homeland Security
FAC-COR	Federal Acquisition Certification for Contracting Officer Representative
FAC-COTR	Federal Acquisition Certification for Contracting Officer Technical Representative
FAR	Federal Acquisition Regulation
FY	fiscal year
OIG	Office of Inspector General
OMB	Office of Management and Budget



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Executive Summary

Cost-reimbursement contracts and other non-firm-fixed price contracts provide limited incentive for contractors to control costs. In the past, these types of contracts have been used without appropriate justification or sufficient management and oversight. As a result, these contract vehicles pose a high risk for wasting or misusing taxpayer funds.

Federal Acquisition Regulation Case 2008-030, *Proper Use and Management of Cost Reimbursement Contracts*, responded to Congressional and Presidential requirements to revise the Federal Acquisition Regulation to include guidance over the use and management of other than firm-fixed-price contracts, to include cost-reimbursement, time-and-material, and labor-hour. This case amended the Federal Acquisition Regulation to require documentation justifying the selection of contract type, and the assignment of acquisition workforce resources to support other-than-firm-fixed-price contracts. We reviewed the Department's compliance with the Federal Acquisition Regulation Case 2008-030, to address a Congressional mandate in the *Duncan Hunter National Defense Authorization Act* for fiscal year 2009.

The Department of Homeland Security (DHS) did not always comply with the revisions in the Federal Acquisition Regulation Case 2008-030, *Proper Use and Management of Cost Reimbursement Contracts*. DHS did not always document required information to justify the selection of other than firm-fixed-price contract-types and did not always assign acquisition workforce resources to manage other-than-firm-fixed-price contracts in accordance with the revisions. These conditions existed because DHS policies do not completely align with the Federal Acquisition Regulation Case requirements, or in some instances, because acquisition personnel did not comply with existing policies. As a result, DHS may not award or manage these contracts properly, increasing the risk associated with the procurement of goods and services.

We made two recommendations intended to improve the Department's use of other than firm-fixed-price contracts. DHS concurred with our recommendations and is taking steps to implement them.



Background

In fiscal year (FY) 2010, Federal agencies collectively spent more than \$535 billion through contracts to acquire goods and services in support of their missions. Agencies obligated more than 35 percent of this total using other than firm-fixed-price contracts. Due to their nature, other-than-firm-fixed-price contracts increase the risks of inefficiency and waste. With the United States facing increasing fiscal pressures, there is a growing need to ensure that Federal agencies make the most efficient and effective use of their resources. To address these concerns, both Congress and the Administration recently strengthened controls over the use and management of other than firm-fixed-price contracts.

Contract-Type Selection

The Federal Acquisition Regulation (FAR) identifies a wide selection of contract types available to the Government, including firm-fixed price, cost-reimbursement, and time-and-materials contracts. The objective is to select a contract-type that results in reasonable contractor risk and provides the contractor with the greatest incentive for economical performance.

The FAR states that the firm-fixed-price contract provides for a price that is not subject to any adjustment on the basis of the contractor's cost experience in performing the contract. Usually, the firm-fixed-price contract is the contract-type best suited for minimizing risk and maximizing value for the Government because it provides the contractor with the greatest incentive for economical performance. It also imposes the minimal administrative burden upon the contracting parties.

While the firm-fixed-price contract is preferred, the Government may award an other than firm-fixed-price contract-type when uncertainties cannot be managed by the contractor within economically reasonable bounds. For example, the FAR allows the government to award:

- Cost-reimbursement contracts when circumstances do not allow the agency to define its requirements sufficiently or when uncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy; and
- Time-and-materials and labor-hours contracts only when it is impossible, at the time of placing the contract, to estimate accurately the extent or duration of the work or to anticipate costs with any reasonable degree of confidence.



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These other than firm-fixed-price contract-types require the Government to absorb a greater portion of the risk up front, but they can help avoid costly contingencies that contractors would pass on to taxpayers if forced to offer their services on a fixed-price basis. Under cost-reimbursement contracts, the Government pays the contractor based on allowable incurred costs rather than the delivery of a completed product or service. Under time-and-materials contracts, the Government pays the contractor fixed hourly rates that include wages, overhead, general and administrative expenses, and profit; based on the number of labor hours billed by the contractor. These terms provide contractors with limited incentive to control costs. In the past, these types of contracts have been used without appropriate justification or sufficient management and oversight. Furthermore, these contract types increase the Government's administration costs. Excessive reliance on other than firm-fixed-price contracts increases the risk that funds will not be properly safeguarded.

In FY 2009, DHS obligated \$2.53 billion (17.7 percent of all contracts) for cost-reimbursement contracts and \$2.54 billion (17.8 percent of all contracts) for time-and-materials and labor-hour contracts. In FY 2010, DHS obligated \$2.62 billion (19.3 percent of all contracts) for cost-reimbursement contracts and \$2.54 billion (18.7 percent of all contracts) for time-and-materials and labor-hour contracts.

Use and Management of Other Than Firm-Fixed-Price Contracts

Recently, the Government has increased efforts to regulate the use and management of other than firm-fixed price contracts. Congress addressed cost-reimbursement contracts in section 864 of the *Duncan Hunter National Defense Authorization Act* for Fiscal Year 2009. Specifically, the Act required the FAR be revised to include guidance regarding 1) when and under what circumstances cost-reimbursement contracts are appropriate; 2) the acquisition plan¹ findings necessary to support a decision to use cost-reimbursement contracts; and 3) the acquisition workforce resources necessary to award and administer cost-reimbursement contracts. The Act also required each agency's Inspector General to determine the agency's compliance with the new requirements. Addressing similar themes, President Obama issued a Presidential Memorandum on Government Contracting on March 4, 2009, directing agencies to become more fiscally responsible in their contract actions and cut contract costs. Additionally, in July 2009, the Office of Management and Budget (OMB) directed agencies to reduce the use of high-risk contracts (i.e. cost-reimbursement, time-and-material, and labor-hour).

¹ As defined by the Defense Acquisition University, an acquisition plan is a written document that addresses all technical, business, management, and other significant considerations that will control an acquisition.



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To implement the Act and the Presidential Memorandum, the Department of Defense, the General Services Administration, and the National Aeronautics and Space Administration jointly issued FAR Case 2008-030 interim rule (*Proper Use and Management of Cost-Reimbursement Contracts*) on March 16, 2011 with immediate implementation. FAR Case 2008-030 broadened the Act's scope to include all other than firm-fixed-price contracts including time-and-material and labor-hour contracts, which share similar risks as cost-reimbursement contracts. It introduced requirements that fall into two broad categories: 1) acquisition planning and contract-type selection, and 2) assignment of acquisition workforce resources.

On March 2, 2012, the regulators adopted the interim rule as final with a few minor revisions that did not change the substance of the interim rule's requirements. The final rule became effective on April 2, 2012.

Results of Audit

DHS did not always comply with the revisions in FAR Case 2008-030 (FAR Case), *Proper Use and Management of Cost Reimbursement Contracts*. DHS did not always document required information to justify the selection of other than firm-fixed-price contract types, and did not always assign acquisition workforce resources to manage other than firm-fixed-price contracts in accordance with the revisions. This occurred because DHS policies do not completely align with the FAR Case requirements, or in some instances, because acquisition personnel did not comply with existing policies. As a result, DHS may not award or manage these contracts properly, increasing the risk associated with the procurement of goods and services.

Contract-Type Selection Requirements

DHS' written acquisition plans did not always contain required contract-type selection information and contracting officers did not always ensure the adequacy of contractors' accounting systems. This occurred because DHS policy does not completely align with the FAR or acquisition personnel (i.e. preparers and reviewers/approvers of the required documentation) did not comply with existing policies. As a result, DHS may not award or manage these contracts properly, increasing the risk associated with the procurement of goods and services.



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DHS' Acquisition Plans

FAR Case 2008-030 requires agencies to develop written acquisition plans for other than firm-fixed-price contracts. These plans shall include specific information on why the particular contract-type was selected and be approved at least one level above the contracting officer. We reviewed a judgmental sample of 59 DHS other than firm-fixed price contracts with a total value of about \$1.5 billion to evaluate DHS' compliance with requirements.² All 59 DHS other than firm-fixed-price contracts did not comply with these requirements as follows:

- The written acquisition plans for 29 of the 59 contracts in our sample did not contain contract-type selection information.

The Homeland Security Acquisition Manual establishes different types of written acquisition plans depending on the acquisition dollar thresholds. The acquisition planner must develop a Formal Written Acquisition Plan for acquisitions of \$10 million or more. For acquisitions of less than \$10 million, acquisition personnel must develop an Advance Acquisition Plan or an Abbreviated Acquisition Plan if the acquisition contains sensitive information. Both the Formal Written Acquisition Plan and the Abbreviated Acquisition Plan require contract-type selection information in accordance with FAR Case 2008-030. However, DHS policy does not require such information to be included in the Advanced Acquisition Plan.

These 29 contracts required Advance Acquisition Plans and therefore did not contain all the required contract-type discussions in FAR Case 2008-030. For 15 of the 29 contracts, some information regarding contract-type selection was included in the Determination and Findings document, which have been required prior to the FAR Case to justify the selection of time-and-materials and labor-hour contract-types. However, Determinations and Findings are not required for all other than firm-fixed-price contracts and they do not require FAR Case 2008-030's specific, targeted discussions and analyses. For example, Determinations and Findings do not require discussions of:

- Government's additional risk and the burden to manage the contract-type selected;

² Details about the selection methodology and sampled contracts are presented in Appendix A.



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- Government resources necessary to plan for, award, and administer the contract-type selected; and
 - Actions planned to minimize the use of other than firm-fixed-price contracts on future acquisitions for the same requirement and to transition to firm-fixed price contracts to the maximum extent possible for non-commercial time-and-materials and labor-hour contracts.
- Twelve written acquisition plans, covering 27 of the 59 contracts in our sample, contain some, but not all of the required contract-type selection information as shown in table 1.

Table 1: FAR Case 2008-030 Requirements of which Formal Written Acquisition Plans were Not Compliant (More than \$10 million)

<u>FAR Case 2008-030 Requirement</u>	<u>FAR Reference</u>	<u>Acquisition Plans Not Compliant</u>	<u>% Not Compliant</u>
Explain how additional risks of the contract-type were identified	16.103(d)(1)(ii)(A)	10 of 12	83%
Discuss plans to transition to firm-fixed-price contracting for future acquisitions of the same requirement	16.103(d)(1)(iv)(D)	9 of 12	75%
Discuss the additional risk of contract type and how the risks would be mitigated	16.103(d)(1)(ii)(B),(C)	9 of 12	75%
Analyze facts and reasoning supporting the selection of the contract-type	16.103(d)(1)(iv)(A),(B)	5 of 12	42%
Explain fee provision, if applicable	16.103(d)(1)(v)	4 of 4	100%
Approval one level above the contracting officer	7.103(j)	3 of 12	25%
Assess the government resources needed to plan, award, and administer the contract-type selected	16.103(d)(1)(iv)(C)	3 of 12	25%

Source: DHS OIG.

The plans we reviewed were formal written acquisition plans covering acquisitions of \$10 million or more. The Homeland Security Acquisition



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Manual issued by DHS Office of the Chief Procurement Officer required contract-type selection information in the formal acquisition plan prior to the FAR Case. For the most part, this information met the FAR Case requirements. DHS expanded its existing policy in June 2011 to include FAR Case provisions not previously covered.

Nine of the twelve plans were approved one level above the contracting officer. However, the documented contract-type selection information did not include all required FAR Case requirements. We concluded that approving officials did not ensure these required elements were included prior to approving the plans.

- 3 of the 59 contracts did not have a written plan.

The contracting officer assigned to these 3 contracts said there was no formal written acquisition plan for these contracts because they were “bridge” contracts to continue the performance of the existing contracts until the follow-on contracts were awarded.

Adequacy of Contractor’s Accounting System

FAR Case requires that prior to agreeing on an other than firm-fixed-price contract type, the contracting officer shall ensure that the contractor’s accounting system will permit timely development of all necessary cost data in the form required by the proposed contract type. We reviewed 13 or 100 percent of the cost-reimbursement contracts in our sample of 59 contracts, and for 6 (46.2 percent) of these the contracting officer did not properly ensure the adequacy of the contractors’ accounting system.

For one contract, the contracting officer used a Defense Contract Management Agency (DCMA) letter as evidence of the contractor’s accounting system validation. The letter stated that DCMA’s approval of the contractor’s accounting system was contingent on verification of the effectiveness of corrective actions implemented for deficiencies noted. The contracting officer did not demonstrate adequate consideration of the issue by documenting the accounting system deficiencies as an additional risk of selecting a cost-reimbursement contract and identifying contract monitoring activities to mitigate the risk, as required by the FAR.

The evidence supporting the validation of the accounting system for another cost-reimbursement contract was based on a checklist completed by the contractor as opposed to a third party. The contracting officer relied on the



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contractor's self-assessment and did not seek any additional information on the adequacy of the accounting system before awarding the contract.

Furthermore, the contracting officers for three additional contracts confirmed they did not ensure the adequacy of the contractors' accounting systems. For one of these contracts, the contracting officer said he erroneously omitted the evaluation. Another contracting officer, responsible for two of these contracts, said he did not ensure the adequacy of the contractor's accounting system because of extreme time pressure. For the last of the seven contracts, we found no evidence of the validation of the contractor's accounting system in the file and the contracting officers provided no explanation for this lapse.

The adequacy of the contractor's accounting system affects the quality and validity of the contractor data upon which the Government must rely for its oversight of the contractor and contract performance. By not ensuring the adequacy of contractors' accounting systems, DHS may reimburse contractors for unallowable costs.

Assignment of Acquisition Workforce Resources

DHS did not always designate Contracting Officer Representatives (COR) prior to contract awards. DHS' CORs were not always properly certified or qualified by training and experience, and were not always nominated by the requirements officials. Also, DHS' COR designation letters did not always include all the elements required by FAR Case. For example, some designation letters did not specify the period covered by the designation, or that the COR may be personally liable for unauthorized acts. This occurred because DHS' acquisition workforce policies are inconsistent—both internally and with FAR Case — and DHS' acquisition personnel did not always comply with existing policies. Not properly designating resources to oversee and support other than firm-fixed-price contracts increases the risk that funds will not be properly safeguarded. DHS needs to improve controls to ensure timely assignment of adequate and proper resources to support the award and administration of other than firm-fixed-price contracts.

COR Nomination by Requirements Officials

FAR Case requires the acquisition planner to ensure that the requirements official, responsible for identifying, developing and/or managing the acquisition requirement, nominates a COR as early as practicable in the acquisition process. Current DHS procedures require a COR nomination package to be included with



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the procurement request, but does not explain what shall be included in the nomination package. Some components have created forms and procedures specifying what will be included with the nominations, while others have not yet developed or updated their procedures.

Twenty-three (40 percent)³ of 59 contracts in our sample, did not have COR nomination packages and/or evidence of the CORs' nomination by the requirements official. CORs should be selected based on nomination packages by the requirements official demonstrating the COR's certification level, training, and experience. This process facilitates the timely appointment of a properly certified COR with the training and experience commensurate with the responsibilities and helps ensure that the COR will have the tools needed to perform his assigned duties.

COR Designation Prior to Contract Award

CORs are qualified individuals designated and authorized by the contracting officer to assist in the technical monitoring and administration of the contract. For other than firm-fixed-price contracts, FAR Case requires agencies to designate and authorize in writing a properly trained COR prior to contract award. Additionally, the FAR Case states involvement of the program office at the early stages of the acquisition facilitates proper contract management and oversight, especially for other than firm-fixed-price contracts.

Twenty-four (41 percent)³ of 59 contracts in our sample, did not have CORs designated in writing prior to contract award. DHS designated a COR after contract award for 23 of these 24 contracts. Sixty-eight was the average number of days between contract award and COR designation. In two cases, DHS designated the COR after our review identified that a COR was not assigned. Additionally, one contract did not have a COR designated before the contract was cancelled.

DHS Acquisition Workforce Policy, which existed prior to the FAR changes, stated that appointing a COR early in the definition phase of the requirement was "desirable." DHS issued new procedures on the required timing of COR designations in its COR Essential Elements Guidebook in September 2011, 6 months after the FAR changes. The COR Guidebook, which is still in place,

³ Percentage is based on our review of 58 contracts. The contracting officer for one of the 59 contracts in our review retained contracting officer representative's duties, as allowed by the FAR Case. Therefore, this contract was not reviewed for this provision.



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requires DHS' contracting officers to designate CORs "upon" contract award. In addition, on January 30, 2012, DHS revised its Acquisition Workforce Policy, stating that the contracting officer "should" appoint a COR early in the contract definition phase of the requirement for all contracts. However, the policy did not provide a specific mandate requiring the appointment of a COR prior to contract award for other than firm-fixed-price contracts.

COR Certification, Training, and Experience

FAR Case requires the contracting officer to designate and authorize a COR who: (a) is certified and maintains certification in accordance with the Office of Management and Budget (OMB) memorandum titled "The Federal Acquisition Certification for Contracting Officer Technical Representative" (FAC-COTR) dated November 26, 2007; and (b) is qualified by training and experience commensurate with the responsibilities to be delegated in accordance with department/agency guidelines. Subsequent to the FAR Case, the FAC-COTR memorandum was superseded by a new OMB memorandum "The Federal Acquisition Certification for Contracting Officer Representative" (FAC-COR) issued on September 6, 2011 with an implementation date of January 1, 2012.⁴

- Federal Acquisition Certification for Contracting Officer Technical Representative

The FAC-COTR required 40 hours of training before an individual is certified as a COR. To maintain certification, the COR needed to earn 40 continuous learning points every 2 years. Thirty-seven of the 59 contracts in our sample had a COR assigned prior to January 1, 2012; and of these, all were certified in accordance with OMB FAC-COTR memorandum.

- The Federal Acquisition Certification for Contracting Officer Representative

OMB's revised memorandum, effective January 1, 2012, established a three-tiered certification, with each tier requiring a different level of training and experience. The memorandum included a COR Appointment Criteria Matrix to help contracting officers select a COR with the appropriate level of training and experience. It stated that one risk factor to consider when selecting a COR is contract-type and listed other than

⁴ The term "COTR" changed to "COR" to align with the FAR.



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firm-fixed-price contract types as a significant or high risk. The memorandum invited agencies to add criteria to the matrix as appropriate for their situations and gave agencies the option to “grandfather” COTRs in as Level II CORs. The policy required agencies to develop guidance to ensure their CORs were FAC-COR certified.

On January 30, 2012, DHS developed its risk-based COR certification level program in its Acquisition Workforce Policy. This policy provided the minimum mandatory training for FAC-COR certification at DHS. The policy requires the appointed COR to have a Level III FAC-COR for high-risk contracts. This rule applies to existing and new contracts. For existing contracts, contracting officers were required to reappoint the CORs after ensuring they were certified at a Level III. Appointment letters for both reappointments and new appointments need to indicate the required and current level of COR certification. Additionally, the revised Acquisition Workforce Policy requires the appointed COR to have appropriate and current certification at the time of appointment.

We reviewed the certification and appointment letters for CORs appointed before and after January 1, 2012.⁵ The CORs appointed to these contracts were not in compliance with the DHS policy established to meet the OMB FAC-COR certification requirements as follows:

- The appointment letters for all contracts did not indicate the required and/or current COR certification level. DHS requires acquisition personnel to use an appointment letter template included in DHS’ Homeland Security Acquisition Manual when designating a COR; however, this template has not yet been updated to include the COR certification level requirement.
- Only the CORs appointed to six contracts were certified at a Level III. We talked to selected contract acquisition personnel for these contracts and they said that they were not aware of the requirement for Level III.
- At the time of our review, none of the CORs appointed prior to January 2012 had been reappointed (37 contracts in our sample).
- The certification for 2 of the 18 CORs appointed after January 1, 2012, had expired prior to their appointment. For the first contract that did not have a properly certified COR, we identified

⁵ At the time of our review, a COR had not been appointed to four contracts in our sample. Therefore, these four contracts were not reviewed and this reduced our sample size for this section to 55.



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that the certification had expired 4½ months before appointment. Based on our conversation with the COR's supervisor 6 months after appointment, the COR was still trying to complete required hours to maintain certification. As a result of our review, a new properly certified COR was appointed to the contract.

The certification for the COR appointed to the second contract had expired 7 months prior to appointment. Based on our conversation with the COR and the component's acquisition specialist, they believed that the training requirement was for every 4 years instead of every 2 years. This COR was assigned to the contract for 4 months without proper certification. As a result of our inquiry, this COR obtained the required hours.

As stated in the OMB FAC-COR memorandum, strengthening the acquisition workforce is critical to ensuring that the Government gets the best value for the goods and services it procures annually. Appointing a properly trained and experienced COR will help ensure that payment is only made to contractors who perform in accordance with contract terms and conditions, and that contract performance will address program needs.

COR Designation Letters

For all other than firm-fixed-price contracts, FAR Case requires the contracting officer to designate a COR in writing with copies furnished to the contractor and the contract administration office. The written designation shall:

- Specify the extent of the COR's authority to act on behalf of the contracting officer;
- Identify the limitations of the COR's authority;
- Specify the period covered by the designation;
- State that the authority is not re-delegable; and
- State that the COR may be personally liable for unauthorized acts.

On April 6, 2011, DHS issued a COR designation letter template that addresses each of the required elements in its Homeland Security Acquisition Manual. DHS requires acquisition personnel to use this template when preparing COR appointment letters to ensure format consistency across DHS.



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In most instances, DHS ensured that its COR designation letters complied with FAR Case. Of the 55 COR designation letters reviewed, 6 (10.9 percent) did not contain all the required elements in the FAR Case. Of these 6 letters, one did not state that the COR's authority is not re-delegable, while another did not state that the COR may be personally liable for unauthorized acts. Three more letters did not include either of these two requirements. One designation letter only included the period covered by the designation. Contracting Officers did not prepare these letters using the COR designation letter template in the Homeland Security Acquisition Manual.

A designation letter that complies with the FAR requirements is important for ensuring that the COR understands the responsibilities and limitations of the COR designation. Not understanding the COR authority could lead to unauthorized commitments and contractual and legal disputes with the contractor.

Conclusion

DHS did not always comply with the requirements in the FAR Case for the proper use and management of other-than-firm-fixed-price contracts. DHS written acquisition plans did not always contain all required information justifying the selection of other-than firm-fixed-price contracts, and contracting officers did not always ensure the adequacy of the contractors' accounting systems. Also, DHS did not always nominate and designate properly certified and trained CORs to manage and oversee other than firm-fixed-price contracts. As a result, DHS risks awarding contracts that are wasteful or otherwise not well designed to serve the Federal Government's needs, paying for unallowable costs, and not being able to manage the risk associated with the goods and services being procured.

Recommendations

We recommend that the Chief Procurement Officer:

Recommendation #1:

Updates Department of Homeland Security acquisition policies to comply with all Federal Acquisition Regulation Case 2008-030 requirements for proper use and management of other-than-firm-fixed-price contracts, ensuring Department of Homeland Security policy:



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- Requires that acquisition plans for all other than firm-fixed-price contracts contain all required information to support the selection of contract type;
- Describes the type of documentation to be included as part of the Contracting Officer Representative nomination package and requires that it is included in the contract file to demonstrate nomination by the requirements official; and
- Requires that Contracting Officer Representatives are designated and authorized in writing prior to contract award for all other-than-firm-fixed-price contracts and orders.

Recommendation #2:

Reaffirm guidance (e.g. Homeland Security Acquisition Manual and Acquisition Workforce Policies) to ensure acquisition personnel understand how the Federal Acquisition Regulation Case 2008-030 requirements affect existing and future contracts and orders. In doing so, ensure to communicate the following:

- Other than firm-fixed-price acquisition plans shall be approved and signed at least one level above the contracting officer, and before approval, these plans shall contain required information supporting the selection of contract type;
- Contracting officers shall ensure that the contractor's accounting system will permit timely development of all necessary cost data in the form required by the proposed contract type;
- Contracting officers shall appoint properly certified, trained, and experienced Contracting Officer Representatives to support other than firm-fixed-price contracts and remove those who fail to meet these requirements; and
- Contracting officers shall use the Contracting Officer Representative designation letter template in Appendix W of the Homeland Security Acquisition Manual to ensure compliance with the FAR Case requirements.

Management Comments and OIG Analysis

DHS provided formal comments to our report. DHS also provided technical comments which were incorporated in the final report where appropriate. DHS concurred with both of our recommendations. Appendix B includes a copy of the management comments in their entirety. Our evaluation of DHS' response to the draft report follows.



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Management Response to Recommendation #1: The CPO concurs with this recommendation and is developing updated policy and guidance to require that acquisition plans for other than firm-fixed-price contracts properly address contract type selection. Additionally, DHS will issue Homeland Security Acquisition Manual and Contracting Officer Representative Guidebook revisions to clarify DHS implementation of FAR Case 2008-03, Proper Use and Management of Cost Reimbursement Contracts, changes to reinforce statutory, regulatory, and policy requirements.

OIG Analysis: We consider this recommendation resolved because steps are being taken to implement it. However, it will remain open until DHS provides documentation to support that the planned corrective actions are completed.

Management Response to Recommendation #2: The CPO concurs with this recommendation and states that it: 1) updated Acquisition Workforce policy, 2) will update the Homeland Security Acquisition Manual and Contracting Officer Representative Guidebook policy, and 3) has issued policy reminders and e-mail notices to DHS acquisition personnel reaffirming guidance to ensure that acquisition personnel understand how the FAR Case 2008-030 requirements affect existing and future contract orders.

OIG Analysis: We consider this recommendation resolved because steps are being taken to implement it. However, it will remain open until DHS provides documentation to support that the planned corrective actions are completed.



Appendix A

Objectives, Scope, and Methodology

The Department of Homeland Security (DHS) Office of Inspector General (OIG) was established by the *Homeland Security Act of 2002* (Public Law 107-296) by amendment to the *Inspector General Act of 1978*. This is one of a series of audit, inspection, and special reports prepared as part of our oversight responsibilities to promote economy, efficiency, and effectiveness within the Department.

This report provides the results of our work to determine whether DHS complied with revisions to the FAR on the use of cost-reimbursement contracts, as prescribed in the FAR Case 2008-030. To accomplish our objective, we reviewed applicable Federal laws, regulations, and sections of the FAR revised by FAR Case 2008-030, to identify requirements for the use and management of other-than-firm-fixed-price contracts.

To gain an understanding of internal controls significant within the context of the audit objective and to determine compliance with the FAR Case 2008-030, we evaluated Department and component-specific procurement policies and procedures. We also interviewed representatives from the Department's Office of the Chief Procurement Officer and Components (i.e. Federal Emergency Management Agency, U.S. Coast Guard, Office of Procurement Operations, Immigration and Customs Enforcement, U.S. Customs and Border Protection, Citizenship and Immigration Services, and the Transportation Security Administration) to obtain an understanding of their processes and internal controls to ensure compliance with the new FAR changes.

We judgmentally selected a sample of 59 DHS contracts solicited and awarded between the dates of March 17, 2011 to March 16, 2012, to determine whether contract-type and Contracting Officer Representative documentation complied with requirements promulgated by FAR Case 2008-030. The sampled contracts were of the following types:

- Cost-Reimbursement - used only when circumstances do not allow the agency to define its requirements sufficiently to allow for a fixed-price type contract or uncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy to use any type of fixed-price contract. In this type of contract, the Government assumes the inherent risks, which are uncertain and speculative labor hours, labor mix, and/or material requirements.
- Time-and-Materials - provide for acquiring supplies or services on the basis of (1) direct labor hours at specified fixed hourly rates that include wages, overhead, general and administrative expenses, and profit; and (2) actual cost for materials.



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- Labor-Hours - are a variation of the time-and-materials contract, differing only in that materials are not supplied by the contractor.
- Indefinite-delivery - used to acquire supplies and/or services when the exact times and/or exact quantities of future deliveries are not known at the time of contract award. There are three types of indefinite-delivery contracts: definite-quantity, requirements, and indefinite-quantity.

Our sample covered six procurement offices within DHS: Federal Emergency Management Agency, U.S. Coast Guard, Office of Procurement Operations, Immigration and Customs Enforcement, U.S. Customs and Border Protection, and the Transportation Security Administration; we did not review classified contracts. We selected contracts with a total base and all options dollar value equal to or greater than \$750,000, with the exception of Office of Procurement Operations’ contracts whose dollar value was equal to or greater than \$1 million. The 59 contracts totaled approximately \$1.5 billion in total base and all options value. We determined whether contract documentation complied with the following guidance promulgated under the FAR Case 2008-030:

FAR Reference	Requirement
1.602-2(d) and 7.104(e)	Written evidence the contracting officer has designated and authorized a contracting officer’s representative (COR) on all contracts and orders that are other than firm-fixed-price. The contracting officer shall verify the COR or COTR is a Government employee, qualified by training and experience in accordance with department/agency guidelines, and certified in accordance with the Office of Management and Budget memorandum. Additionally, the contracting officer will ensure the COR or COTR has been delegated the appropriate responsibility and will identify any limitations on the authority of the COR/COTR;
1.604* 1.602-2(d)(4)*	COR needs to maintain a file for each assigned contract. A COR may not be delegated functions that have been delegated to a contract administration office.
7.103(d), (e), (f) and (j) 7.105(b)(3)	Review of policy prescribed by the agency head or its designee to ensure compliance with 7.103(d), (e), (f), and (j). Evidence that acquisition planners documented the files to support the selection of the contract type in accordance with the following paragraph from Subpart 16.1: the statement of work is closely aligned with the performance outcomes and cost estimates; a written plan was prepared for other than firm-fixed-price contracts; established criteria and thresholds on the level of detail for written acquisition plans; acquisition plans comply with FAR 7.104 and Part 16; and acquisition plans for other-than-firm-fixed-price contracts are reviewed and approved at least one level above the contracting officer.
7.105(b)(5)(iv)	Documentation of the strategy to transition from other-than-firm-fixed-price contracts to firm-fixed-price contracts.
16.103(d)	Additional documentation when other than a firm-fixed-price contract type is selected.



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16.104	Contracting Officer's consideration of combining contract types if the entire contract cannot be firm-fixed-price.
16.301-2	Circumstances in which to use cost-reimbursement and the documented rationale for selecting an other than firm-fixed-price contract type.
16.301-3 16.104 (i) 42.302(a)(12)	When a cost-reimbursement contract may be used, documentation that the contracting officer considered all factors per FAR 16.104, including the adequacy of the contractor's accounting system; and documentation that the contracting officer has ensured that adequate Government resources are available to award and manage other than firm-fixed-price contract awards.

Source: FAR *We did not verify compliance with FAR 1.604 and 1.602-2(d)(4) during this review.

We conducted this performance audit between April and July 2012, pursuant to the *Inspector General Act of 1978*, as amended, and according to 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 upon our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based upon our audit objectives.



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Appendix B
Management Comments to the Draft Report


U.S. Department of Homeland Security
Washington, DC 20528



**Homeland
Security**

September 26, 2012

MEMORANDUM FOR: Anne L. Richards
Assistant Inspector General for Audits
Office of the Inspector General

FROM: Jim H. Crumpacker 
Director, Departmental GAO-OIG Liaison Office

SUBJECT: Draft OIG Report: "Department of Homeland Security
Compliance with the Federal Acquisition Regulation Revisions on
Proper Use of Cost-Reimbursement Contracts" (Project No. 12-
135-AUD-DHS)

Thank you for the opportunity to review and comment on this draft report. The U.S. Department of Homeland Security (DHS) appreciates the Office of Inspector General's (OIG's) work in conducting its review and issuing this report.

The draft report contained two recommendations with which the Department concurs. Specifically, the OIG recommended that the DHS Chief Procurement Officer (CPO):

Recommendation 1: Update Department of Homeland Security acquisition policies to comply with all Federal Acquisition Regulation Case 2008-030 requirements for proper use and management of other-than-firm-fixed-price contracts, ensuring Department of Homeland Security policy:

- Requires that acquisition plans for all other-than-firm-fixed-price contracts contain all required information to support the selection of contract type;
- Describes the type of documentation to be included as part of the Contracting Officer Representative nomination package and requires that it is included in the contract file to demonstrate nomination by the requirements official; and
- Requires that Contracting Officer Representatives are designated and authorized in writing prior to contract award for all other-than-firm-fixed-price contracts and orders.

Response: Concur. The CPO agrees that updated policy and guidance are necessary to ensure compliance with Federal Acquisition Regulation (FAR) requirements for proper use of and management of other-than-firm-fixed-price contracts. On August 15, 2012, the CPO

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Acquisition, Policy and Legislation (APL) Division issued updated policy and guidance to require that acquisition plans for other-than-firm-fixed-price contracts properly address contract type selection.

Additionally, APL will issue Homeland Security Acquisition Manual (HSAM) and Contracting Officer Representative (COR) Guidebook revisions to clarify DHS implementation of FAR Case 2008-03, Proper Use and Management of Cost Reimbursement Contracts, changes to reinforce statutory, regulatory, and policy requirements. Changes will include:

- Clarifying the procurement request requirements in HSAM 3004 to include the COR nomination package, and describing the contents of the package;
- Changing the requirement in HSAM 3007 and associated Acquisition Planning Guide to require FAR compliant Acquisition Plans for all non-firm-fixed-price contracts above the simplified acquisition threshold;
- Removing all references in the HSAM and other policy documents to the Acquisition Planning Forecast System as a complete substitute for a FAR compliant Acquisition Plan for all non-firm-fixed-price contracts above the simplified acquisition threshold; and
- Adding additional information in HSAM 4042 and Appendix W to ensure that CORs are appointed prior to contract award, that the Contracting Officer receive a full COR nomination package and the Contracting Officer's appointment of the COR includes the certification level and an explanation of why that certification level is necessary for the tasks to be performed during contract administration. Estimated Completion Date (ECD): October 31, 2012.

Recommendation 2: Reaffirm guidance (e.g., Homeland Security Acquisition Manual and Acquisition Workforce Policies) to ensure acquisition personnel understand how the Federal Acquisition Regulation Case 2008-030 requirements affect existing and future contracts and orders. In doing so, ensure to communicate the following:

- Other-than-firm-fixed-price contract acquisition plans shall be approved and signed at least one level above the Contracting Officer and before approval, these plans shall contain required information supporting the selection of contract type;
- Contracting Officers shall ensure that the contractor's accounting system will permit timely development of all necessary cost data in the form required by the proposed contract type;
- Contracting Officers shall appoint properly certified, trained, and experienced Contracting Officer Representatives to support other-than-firm-fixed-price contracts and remove those who fail to meet these requirements; and
- Contracting Officers shall use the Contracting Officer Representative designation letter template in Appendix W of the Homeland Security Acquisition Manual to ensure compliance with the FAR Case requirements.



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Response: Concur. The CPO agrees that DHS needs to reaffirm guidance to ensure that acquisition personnel understand how the FAR Case 2008-03 requirements affect existing and future contract orders.

APL issued Regulatory Reminder 12-02 "Planning and Approving Non-Fixed Priced Actions" on August 15, 2012. This reminder listed each important FAR change incorporated by FAR Case 2008-030 and gave instructions on what was necessary for Contracting Officers to comply with each of these new policies. This regulatory reminder was designed to make required FAR compliance easier and simplify the means of compliance, all with a goal of ensuring that Contracting Officers and Components comply with the statutory, regulatory, and policy requirements of the new FAR policies.

CPO's Acquisition Workforce division issued an e-mail notice, entitled "COR Appointment Requirements and Revised Policy" on August 10, 2012, reminding contract specialists and Contracting Officer to adhere to the COR certification requirements outlined in September 2011 Office of Federal Procurement Policy guidance.

Concurrent with the reminder e-mail, Acquisition Workforce also updated and published the revised COR certification policy, entitled "DHS Federal Acquisition Certification for Contracting Officer's Representatives Policy." The revised policy clarifies that for other-than-firm-fixed-price contracts, Contracting Officers must appoint a Level III certified COR.

Additionally, as stated under Recommendation 1, APL will issue HSAM and COR Guidebook revisions to clarify DHS implementation of FAR Case 2008-03, Proper Use and Management of Cost Reimbursement Contracts changes to reinforce statutory, regulatory, and policy requirements. One of the changes to the Guidebook will be an update to Appendix W to ensure compliance with the FAR case requirements. ECD: October 31, 2012.

Again, thank you for the opportunity to review and comment on this draft report. Technical comments were submitted previously under separate cover. Please feel free to contact me if you have any questions. We look forward to working with you in the future.



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Department of Homeland Security

Appendix C
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Appendix D
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