

July 2005

INTERAGENCY CONTRACTING

Franchise Funds Provide Convenience, but Value to DOD is Not Demonstrated



GAO

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Highlights of [GAO-05-456](#), a report to congressional committees

Why GAO Did This Study

The Department of Defense (DOD) is the largest user of other federal agencies' contracting services. The availability of these contracting services has enabled DOD and other departments to save time by paying other agencies to award and administer contracts for goods and services on their behalf. DOD can access these contracting services a number of ways, such as ordering directly from interagency contracts for commonly needed items. DOD also can pay someone else to do the work. For example, DOD uses franchise funds, which are government-run, fee-for-service organizations that provide a portfolio of services, including contracting services. As part of a congressional mandate, GAO assessed whether franchise funds ensured fair and reasonable prices for goods and services, whether DOD analyzed purchasing alternatives, and whether DOD and franchise funds ensured value by defining contract outcomes and overseeing contractor performance.

What GAO Recommends

GAO recommends that DOD, the departments of the Interior and the Treasury, and the Office of Management and Budget improve the manner in which franchise funds are utilized to ensure value and to ensure compliance with procurement regulations. The agencies concurred with GAO's recommendations and identified actions they have taken or plan to take to address them.

www.gao.gov/cgi-bin/getrpt?GAO-05-456.

To view the full product, including the scope and methodology, click on the link above. For more information, contact David E. Cooper at (202) 512-4125 or cooperd@gao.gov.

INTERAGENCY CONTRACTING

Franchise Funds Provide Convenience, but Value to DOD Is Not Demonstrated

What GAO Found

GovWorks and FedSource, two of the franchise funds that DOD has relied on for contracting services, have not always ensured fair and reasonable prices while purchasing goods and services. The franchise funds also may have missed opportunities to achieve savings from millions of dollars in purchases, including engineering, telecommunications, or construction services. In the course of its review, GAO examined \$249 million worth of orders and work assignments from the contracts the franchise funds used to make purchases on DOD's behalf. In many cases, GovWorks sought but did not receive competing proposals. GovWorks added substantial work—as much as 20 times above the original value of a particular order—without determining that prices were fair and reasonable. FedSource generally did not ensure competition for work, did not conduct price analyses, and sometimes paid contractors higher prices for services than established in contracts with no justification provided in the contract files.

For its part, DOD—in the absence of clear guidance on the proper use of other agencies' contracting services—chose to use franchise funds on the basis of convenience without analyzing whether using franchise funds' contracting services was the best method for meeting purchasing needs. DOD also lacks information about purchases made through other agencies contracts, including franchise funds, which makes it difficult to make informed decisions about the use of these types of contracts. The franchise funds' business-operating principles require that they maintain and evaluate cost and performance benchmarks against their competitors. However, the franchise funds did not perform analyses that DOD could have used to assess whether the funds deliver good value. The funds' performance measures generally focus on customer satisfaction and generating revenues. These measures create an incentive to increase sales volume and meet customer demands at the expense of ensuring proper use of contracts and good value.

DOD and the franchise funds—which share responsibility for ensuring value through sound contracting practices such as defining contract outcomes and overseeing contractor performance—did not adequately define requirements. Without well-defined requirements, DOD and the franchise funds lacked criteria to measure contractor performance effectively. On a separate oversight-related issue, GAO found that the departments of the Interior and the Treasury—each of which has responsibility in the successful operation of the respective franchise funds—and the Office of Management of Budget have performed little oversight of GovWorks and FedSource.

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Abbreviations

DOD	Department of Defense
FAR	Federal Acquisition Regulation
GSA	General Services Administration

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United States Government Accountability Office
Washington, DC 20548

July 29, 2005

Congressional Committees

In recent years, federal agencies have made increasing use of other agencies' contracting services to purchase goods and services in less turnaround time. Use of these services, generally referred to as interagency contracting, has enabled federal agencies to reduce the time they spend awarding and administering contracts in the face of acquisition workforce reductions and growing workloads. Although these services have grown rapidly and have helped streamline purchasing, using the many types of contracts demands a high degree of business acumen and contracting knowledge. Federal agencies can obtain contracting services through entrepreneurial, fee-for-service organizations, which are government-run but operate like businesses. Franchise funds are one such type of organization.

We have reported on the challenges of using other agencies' contracting services and have cited the need to effectively manage this contracting environment. Indeed, we and the inspectors general of some federal agencies have found instances in which interagency contracts have been improperly used. Furthermore, we have reported that the agencies that provide and the agencies that use interagency contracting assistance—such as franchise funds—should be subject to improved oversight and controls, clearer lines of accountability, and better policies, processes, and implementation. It is for these reasons that we have designated management of interagency contracting as a governmentwide high-risk area.¹

The Department of Defense (DOD) is the largest customer for other agencies' contracting services for purchases, typically ranging from office supplies to information technology. Use of interagency contracts has allowed DOD to focus more of its contracting offices' time and attention on the acquisition of specialized, highly sophisticated defense equipment. DOD uses two franchise funds in particular to make purchases on its behalf—GovWorks, which is run by the Department of the Interior, and FedSource, run by the Department of the Treasury. In fiscal year 2004,

¹GAO, *High Risk Series: An Update*, [GAO-05-207](#) (Washington, D.C.: January 2005).

DOD paid these franchise funds more than \$1.2 billion for purchases of goods and services. (See figure 1.)

The Conference Report accompanying the National Defense Authorization Act for Fiscal Year 2004 directed us to report on DOD's use of franchise funds.² We assessed (1) whether franchise funds ensured fair and reasonable prices for goods and services; (2) whether DOD analyzed alternatives to determine the best method for acquiring certain goods and services; and (3) whether DOD and franchise funds ensured value through other sound contracting practices, such as defining contract outcomes, and overseeing contractor performance.

To fulfill these objectives, we examined DOD's largest projects that involved contracting assistance from GovWorks and FedSource in fiscal year 2003, the most recent year for which complete data were available at the time we were planning our review. We reviewed 17 projects, including the interagency contracts used, and orders and work assignments representing \$249 million in fiscal year 2003 DOD funding. We interviewed DOD customers and officials at the two franchise funds and reviewed documentation to assess the contracting practices used to place orders for goods and services. The results of our review cannot be generalized to all types of interagency contracts that DOD and the franchise funds used; however, we believe we have sufficient information to make informed judgments on the matters in this report. Appendix I provides details on our scope and methodology. We conducted our work from June 2004 through June 2005 in accordance with generally accepted government auditing standards.

Results in Brief

In providing contracting services to DOD customers, the GovWorks and FedSource franchise funds did not always obtain the full benefits of competitive procedures, did not otherwise ensure fair and reasonable prices, and may have missed opportunities to achieve savings on millions of dollars in purchases. In half of the GovWorks orders we reviewed, we found that GovWorks sought, but did not receive, competing proposals. In more than half of the orders, GovWorks requested that contractors perform substantial, additional work without determining that prices were fair and reasonable. FedSource generally did not ensure competition for work, did not conduct and document price analyses, and sometimes paid

²H.R. Conf. Rep. No. 108-354 at 775-76 (2003).

contractors higher prices for services than were justified. In addition, FedSource relied on administrative personnel who were not trained as contracting officers to ensure that potential contractors had opportunities to submit offers.

In the absence of clear guidance on the proper use of other agencies' contracting services, DOD customers did not perform analyses of contracting alternatives and chose to use the franchise funds on the basis of convenience rather than as part of an acquisition plan. DOD also lacks basic information about purchases made through franchise funds. Without this data, it is difficult to assess whether franchise funds' contracting services provide DOD value. For their part, although franchise funds' business-operating principles require them to maintain and evaluate cost and performance benchmarks against their competitors, the funds did not perform analyses that DOD could use to assess whether the funds deliver good value. Their performance measures generally focus on customer satisfaction and generating revenues, rather than compliance with contracting regulations. The fee-for-service arrangement provides incentives to emphasize customer service to ensure sustainability of the contracting operation at the expense of proper use of contracts and good value.

DOD, GovWorks, and FedSource paid little attention to sound contracting practices for which they shared responsibility to help ensure value: carefully defining contract outcomes and specific criteria against which contractor performance can be measured and providing effective contractor oversight. DOD customers did not provide franchise funds with detailed information about their needs. Without this information, the franchise funds did not translate DOD's needs into well-defined contract requirements that contained criteria to determine whether the contractor performed successfully. In the absence of well-defined outcomes, DOD, GovWorks, and FedSource lacked criteria to provide effective contractor oversight. Regarding a separate oversight issue, the oversight of GovWorks and FedSource themselves, we found that the departments of the Interior and the Treasury and the Office of Management of Budget, each of which has responsibility in the successful operation of these franchise funds, have performed little oversight.

DOD and the franchise funds have undertaken a number of corrective actions during the course of our review. To enhance their initiatives, we are making recommendations to the Secretary of Defense to develop a methodology for determining whether franchise funds' contracting services are in the best interest of the government and to monitor and

evaluate DOD's use of these services. We also recommend that the Secretaries of the Interior and the Treasury develop procedures and performance measures to ensure that franchise funds' contracting officers fulfill the requirements of procurement regulations while maintaining their focus on customer service. To improve oversight of franchise funds, we recommend that the Director of the Office of Management and Budget expand its monitoring and reporting to include franchise funds' contracting services and develop guidance to clarify roles and responsibilities of customers and franchise funds in the contracting process. In comments on a draft of this report, DOD, the departments of the Interior and the Treasury, and the Office of Management and Budget concurred with our recommendations and identified actions they have taken or plan to take to address them. Written comments from DOD and the Department of the Treasury are reproduced in their entirety in appendices IV and V, respectively.

Background

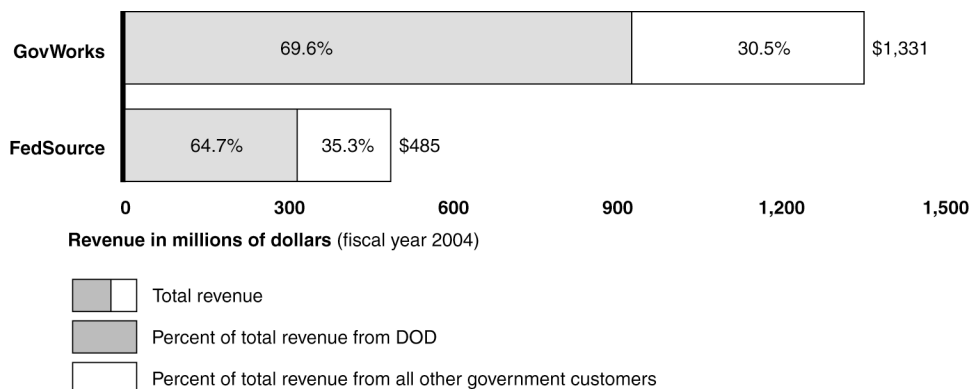
Franchise funds are government-run, self-supporting businesslike enterprises managed by federal employees. Franchise funds provide a variety of common administrative services, such as payroll processing, information technology support, employee assistance programs, public relations, and contracting.³ This review focuses on DOD's use of the franchise funds' contracting services. Franchise funds are required to recover their full costs of doing business and are allowed to retain up to 4 percent of their total annual income. To cover their costs, the franchise funds charge fees for services. The Government Management Reform Act of 1994 authorized the Office of Management and Budget to designate six federal agencies to establish the franchise fund pilot program.⁴ Congress anticipated that the franchise funds would be able to provide common administrative services more efficiently than federal agencies' own

³Franchise fund enterprises are a type of intragovernmental revolving fund, all of which have similar legal authority and operations and are generally created to provide common administrative services. An intragovernmental revolving fund is established to conduct continuing cycles of businesslike activity within and between government agencies. An intergovernmental revolving fund charges for the sale of goods or services and uses the proceeds to finance its spending, usually without the need for annual appropriations.

⁴Between May 1996 and January 1997 pilots were designated to be established at the departments of Commerce, Health and Human Services, the Interior, the Treasury, and Veterans Affairs and at the Environmental Protection Agency. Pub. L. No. 103-356, § 403. The pilots were to expire after 5 years, at the end of fiscal year 1999, but have been extended several times—and as of December 2004—Congress extended the date to October 1, 2005.

personnel. The original operating principles for franchise funds included offering services on a fully competitive basis, using a comprehensive set of performance measures to assess the quality of franchise fund services, and establishing cost and performance benchmarks against their competitors—other government organizations providing the same types of services.⁵ Although there are five franchise funds currently in operation, DOD primarily uses two for contracting services—GovWorks, operated by the Department of the Interior, and FedSource, operated by the Department of the Treasury. Figure 1 shows the revenues for GovWorks and FedSource and the percentage of revenue derived from doing business with DOD in fiscal year 2004.

Figure 1: GovWorks and FedSource Fiscal Year 2004 Revenues



Source: GovWorks and FedSource (data); GAO (analysis and presentation).

Note: Revenues include the cost of the goods and services acquired and the franchise funds' service charges or fees.

Effective contract management requires specialized knowledge and careful attention to a range of regulatory requirements and contracting practices designed to protect the government's interests. In obtaining contracting services through a franchise fund, three main parties share responsibilities for ensuring that proper procedures are followed:

- government customer—the program office or agency in need of a good or service;
- franchise fund—the federal entity that provides contracting services; and

⁵Appendix II lists 12 original operating principles for franchise funds.

- contractor—the vendor that provides the good or service desired by the government customer.

DOD program officials are most familiar with the technical requirements for the goods and services they need. DOD contracting officers can place orders directly through many interagency contracts. Alternatively, DOD pays the franchise fund to assume many of the contracting responsibilities that normally would have been handled by DOD’s contracting officers if the customers had relied on them to purchase the goods or services. Whether DOD makes purchases directly or through another agency, regulatory procedures and requirements are the same, such as ensuring competition, determining fair and reasonable pricing, and monitoring contractor performance. Table 1 shows the basic steps to acquire a good or service through GovWorks or FedSource.

Table 1: Steps to Purchase Good or Service through GovWorks or FedSource

Step	Organization	Actions taken
1	DOD customer	Identifies need for a good or service, sometimes develops government cost estimate, prepares a description of the goods and services needed, and sends it to franchise fund.
2	GovWorks or FedSource	Provides DOD customer an estimated price for acquiring good or service.
3	DOD customer	Commits funds to pay franchise funds for purchase of good or service, plus fee.
4	GovWorks or FedSource	Chooses a contracting vehicle from among several types; develops order for good or service to be provided under an existing contract or develops a new contract, conducts competition. Awards contract to a winning contractor or places order against an existing contract. Designates a contracting officer’s representative or a contracting officer’s technical representative to conduct contractor oversight. GovWorks generally appoints a representative from the customer agency.
5	Contractor	Performs or subcontracts work for DOD according to order.
6	DOD customer	Conducts contractor oversight.
7	Contractor	Submits invoice to franchise fund for work performed.
8	GovWorks or FedSource	Pays contractor for work performed.

Source: GAO analysis of GovWorks’ and FedSource’s procedures.

GovWorks and FedSource can either make use of their own or other agencies’ contracts, or they can develop new, customized contracts to satisfy a DOD customer’s needs. GovWorks generally uses other agencies’ contracts, and FedSource generally uses its own contracts. Table 2 lists the various types of contracting methods the franchise funds use.

Table 2: Contracting Methods Used by GovWorks or FedSource

Contracting method	Description
GSA schedule	Under the General Services Administration (GSA) schedule program, GSA negotiates contracts with vendors for a wide variety of goods and services at varying prices. These contracts permit other agencies to place orders directly with the vendors, providing agencies with a simplified process of acquiring goods and services while obtaining volume discounts.
Indefinite delivery/ indefinite quantity (ID/IQ) Multiple-award and single-award	These contracts can be used to acquire goods or services when the exact date of future deliveries is unknown but a recurring need is likely to arise. One type of indefinite delivery contract is an indefinite quantity contract. Indefinite quantity contracts provide for an indefinite quantity, within stated limits, of supplies or services during a fixed period. The Federal Acquisition Regulation (FAR) states a preference for multiple-awards of indefinite quantity contracts, but award to a single vendor is also permitted. Almost all of the ID/IQ contracts we reviewed were multiple-award.
Requirements	Under a requirements contract, the government designated activity is expected to purchase all of its needs for specific products or services from the holder of the contract.
Blanket purchase agreement	This type of agreement provides a simplified method of filling anticipated repetitive needs for supplies and services, allowing agencies to establish “charge accounts” with qualified vendors.
8(a)	Under the 8(a) program, the Small Business Administration enters into contracts with federal agencies and lets subcontracts for performing those contracts to eligible firms. Small businesses that are owned by socially and economically disadvantaged individuals and certified by the Small Business Administration are eligible for these contracts.

Source: GAO analysis

While use of other agencies’ contracting services may offer convenience and efficiency, our prior work and that of some agency inspectors general have identified problems with the use of other agencies’ contracting services, including lack of compliance with federal requirements for competition and lack of contractor oversight. In prior work, we found that increasing demands on the acquisition workforce and insufficient training and guidance are among the causes for these deficiencies.⁶ Two additional factors are worth noting. First, the fee-for-service arrangement creates an incentive to increase sales volume because revenue growth supports growth of the organization. This incentive can lead to an inordinate focus on meeting customer demands at the expense of complying with contracting policy and required procedures. Second, it is not always clear where the responsibility lies for such critical functions as describing requirements, negotiating terms, and conducting oversight. Several parties—the government customer, the agencies providing the contracting

⁶GAO, *High-Risk Series: An Update*, [GAO-05-207](#) (Washington, D.C.: January 2005) contains a list of related products.

services, and, in some cases, the contractors—are involved with these functions. But, as the number of parties grows, so too does the need to ensure accountability. We have previously reported that ensuring the proper execution of the contracting process is a shared responsibility of all parties involved in the acquisition process and that specific responsibilities need to be more clearly defined.

Franchise Funds Did Not Always Ensure Fair and Reasonable Prices or Competitive Procedures

GovWorks and FedSource did not always obtain the full benefits of competitive procedures, did not otherwise ensure fair and reasonable prices, and may have missed opportunities to achieve savings on behalf of DOD customers for millions of dollars worth of goods and services. With limited evidence that prices were fair and reasonable, GovWorks sometimes added millions of dollars of work to existing orders—as high as 20 times the original order value. In addition, we found limited and inconsistent evidence in the GovWorks and FedSource contract files we reviewed that the franchise funds sought to negotiate prices or conducted price analysis when required. DOD customers told us they were under the impression that franchise funds ensure competition and analyze prices. However, we found numerous cases in which these practices did not occur.

Criteria

The FAR states that contracting officers must purchase goods and services from responsible sources at fair and reasonable prices. Price competition is the preferred method to ensure that prices are fair and reasonable. The FAR also includes special competition procedures for orders placed under the types of contracts the franchise funds use, including GSA schedules and multiple-award contracts. DOD's procurement regulations have additional procedures for ensuring competition when purchasing services from these types of contracts with certain exceptions—such as urgency or logical follow-on. For example, when ordering from GSA schedules, DOD procurement regulations require contracting officers to request proposals from as many contractors as practicable and receive at least three offers. If three offers are not received, a contracting officer must determine in writing that no additional contractors can fulfill the requirement. Alternatively, the contracting officer may provide notice to all schedule

holders that could fulfill the requirement.⁷ When prices for the specific services being ordered are not established in the contract, the FAR and GSA ordering procedures require contracting officers to analyze proposed prices and to document that they are determined to be fair and reasonable. For example, when labor rates are established in the contract, relying on labor rates alone is not a good basis for deciding which contractor is the most competitive. The labor rates do not reflect the full cost of the order or critical aspects of the service being provided, such as the number of hours and mix of labor skill categories needed to perform the work. These procedures are designed to ensure that the government's interests are protected when purchasing goods and services.

GovWorks

We reviewed 10 orders—totaling about \$164 million in fiscal year 2003 funding—in which GovWorks provided contracting services to DOD's customers. With the exception of two orders, which were placed against GovWorks' own contracts, the orders we reviewed were placed against GSA schedules. In 5 of the 10 cases, GovWorks sought, but did not receive, competing proposals as required for the types of contracts used. In 3 of the 10 cases, GovWorks sought and received multiple proposals for the work. In the remaining 2 cases, GovWorks placed orders on a sole-source or single-source basis and provided relevant explanations, such as an urgent need for the work and an award to a small disadvantaged business. Table 3 provides details on these 10 orders, and additional information is available in appendix I.

⁷Section 803 of the National Defense Authorization Act for Fiscal Year 2002, Pub. L. No. 107-107 (2001), requires DOD to develop regulations requiring DOD to solicit offers from all contractors that are offering the required services under a multiple-award contract for orders exceeding \$100,000. For GSA schedule orders, section 803, as implemented, requires that DOD solicit all contractors offering the required services under the applicable schedule or enough contractors to ensure the receipt of three offers. If three offers are not received, a contracting officer must determine in writing that no additional contractors could be identified despite reasonable efforts to do so. Under certain circumstances, section 803 allows waivers of competition for multiple-award contract orders and GSA schedule orders. The implementing regulations in the Defense Federal Acquisition Regulation Supplement became effective in October 2002. Defense Federal Acquisition Regulation Supplement 208.404-70.

Table 3: GovWorks Fiscal Year 2003 Orders

Customer	Type of service	Contracting method	Number of proposals received	Award made to incumbent contractor	Time frame to submit proposals (days)
GovWorks sought but did not receive competing proposals					
Air Force Aging Landing Gear Life Extension Program	Engineering	GSA Schedule	1	Yes	14
Air Force Deputy Chief of Staff Air and Space Operations	Professional	GSA Schedule	1	Yes	4
Air Force Material Command	Network hardware	Interior multiple-award	1	Yes	5
Army National Guard Bureau Chief Information Office	Professional	GSA Schedule	1	No	13
Navy Program Executive Officer Information Technology	Information technology	GSA Schedule	1	Yes	8
GovWorks sought and received competing proposals					
Army Chief Technology Office	Information technology	GSA Schedule	2	Yes	16
Army National Guard Bureau	Information technology	GSA Schedule	3	No	45
Army National Guard Bureau	Telecommunications	GSA Schedule	7	No	28
GovWorks placed sole- or single-source orders					
Army Chief Information Office	Information technology hardware	Interior 8(a)	1	No	Not applicable
Army Program Manager Signals Warfare	Logistics	GSA Schedule	1	No	Not applicable

Source: GovWorks (data); GAO (analysis).

In the five cases for which GovWorks sought competing proposals but received only one proposal for each order, GovWorks allowed 2 weeks or less for proposals to be submitted. In four of these cases, orders were ultimately placed with incumbent contractors to fill requirements for ongoing programs. For example, when the Air Force’s Office of the Deputy Chief of Staff Air and Space Operations sought a contractor to provide analytical services, GovWorks gave potential contractors 4 days—around Christmas—to respond. The one contractor that responded was the incumbent and received the order, which totaled \$63.4 million. When the Air Force’s Aging Landing Gear Life Extension Program needed a contractor to provide services involving landing gear technology, GovWorks invited 17 contractors to submit proposals and posted the solicitation on the Internet allowing 14 days for proposals to be submitted. The incumbent contractor, which had provided services to the program since its inception in 1998, submitted the only proposal and received the

order, which totaled \$19.8 million. Each of these 5 orders was subject to the standards for obtaining competing offers for DOD orders, but in only the case of the Aging Landing Gear Life Extension Program did contract documentation indicate that GovWorks had attempted to meet Defense procurement regulations for ordering from GSA schedules.

Our findings at GovWorks are consistent with our previous work on DOD's use of other agencies' contracts.⁸ In our prior work we found that the reasons only one contractor responded to opportunities to compete for work included a perception among potential contractors that incumbent contractors have an advantage in competing for ongoing work and that very short time frames to prepare proposals discouraged others from competing. In this review, we found GovWorks received multiple proposals for work when there was no incumbent contractor and longer time frames allowed for competition to occur.

In the five cases in which competing proposals were sought but not obtained, we found limited evidence of price analyses in GovWorks' contract files.⁹ In four of these cases, orders were subject to GSA ordering procedures for services requiring a statement of work. In the fifth case, an Interior multiple-award contract, the FAR required price analysis. (See table 3.) Consequently, GovWorks should have determined that the total price was fair and reasonable. GovWorks told us that it had conducted analyses, but we found that the files generally included only brief statements that prices had been determined reasonable, and GovWorks generally could not provide us with documentation showing what data had been gathered or analyses conducted to support the conclusion for the cases we reviewed.

In 6 of the 10 cases we reviewed, GovWorks added substantial work beyond what was originally planned without determining that prices were

⁸GAO, *Contract Management: Few Competing Proposals for Large DOD Information Technology Orders*, [GAO/NSIAD-00-56](#) (Washington, D.C.: March 2000); GAO, *Contract Management: Not Following Procedures Undermines Best Pricing Under GSA's Schedule*, [GAO-01-125](#) (Washington, D.C.: November 2000); and GAO, *Contract Management: Guidance Needed to Promote Competition for Defense Task Orders*, [GAO-04-874](#) (Washington, D.C.: July 2004).

⁹GovWorks primarily used GSA schedule contracts. When ordering services that required a statement of work, GSA's *Multiple-Award Schedules Program Owners Manual* required that offices placing orders consider the level of effort and mix of labor proposed to perform specific tasks and make a determination that task order pricing was fair and reasonable (app. A, 2001).

fair and reasonable. For example, GovWorks increased an original order 20-fold by adding \$45.5 million for management consulting services for the National Guard Bureau Chief Information Office. GovWorks modified another National Guard order on numerous occasions, this time increasing the value of the original order for an automated information system from \$17.6 million to \$44.6 million. An order for reconnaissance and surveillance flight support to Army combatant commands increased in value from \$7.4 million to \$34.9 million. The order was intended to provide support in Bosnia, for a period of 15 months with no option to renew, but was expanded to include operations in Colombia, and the period of performance was extended by more than 2 years. In each of these examples, GovWorks assigned the additional work without conducting price analyses to determine whether the prices charged were fair and reasonable.

FedSource

We reviewed seven FedSource projects—amounting to \$85 million in fiscal year 2003—and found that the franchise fund did not compete orders it placed under multiple-award contracts or perform analyses to ensure fair and reasonable pricing.¹⁰ FedSource commonly used multiple-award contracts to make purchases for DOD. When placing orders against multiple-award contracts, DOD is generally required to ensure that contract holders have a fair opportunity to submit an offer and have that offer fairly considered for each order with certain exceptions—such as urgency or logical follow-on.¹¹ In addition, FedSource used Blanket Purchase Agreements and requirements contracts for some of the projects we reviewed. Table 4 provides detail on the seven projects, and additional information is available in appendix I.

¹⁰We found Treasury competitively awarded the indefinite delivery contracts included in our review.

¹¹Defense Federal Acquisition Regulation Supplement 216.505-70.

Table 4: FedSource Fiscal Year 2003 Projects Reviewed

Customer	Type of service provided	Contracting method used to fill fiscal year 2003 requirements				Blanket purchase agreement	Total number of fiscal year 2003 work assignments	Number of work assignments reviewed
		Indefinite delivery		Requirements	Single award			
		Multiple-award	Indefinite quantity					
Walter Reed Army Medical Center	Staffing	✓				✓	874	66
U.S. Army Fort McCoy	Construction	✓					187	12
Army 88 th Regional Readiness Command at Fort Snelling	Staffing and construction	✓					31	5
The Pentagon	Information technology	✓					5	5
Navy Recruiting Command	Staffing					✓	273	18
Lackland Air Force Base	Staffing	✓	✓	✓			185	14
Brooke Army Medical Center	Staffing	✓	✓	✓			248	25

Source: Department of Treasury (data); GAO (analysis).

The FedSource business model involves a two-step process of placing an order under previously awarded contracts and subsequently developing work assignments to define requirements for that order. In the first step, contracting officers issue orders indicating the type and approximate dollar value of work that FedSource anticipates will be required under each contract. This estimated value is based on historical usage. The second step is executed later when DOD identifies its needs. At this point, FedSource administrative personnel define tasks and outcomes and assign work to a contractor. In our past work, we recommended that the FAR clarify that agencies should not award large, undefined orders against multiple-award contracts and subsequently define specific tasks.¹² The FAR was revised to encourage agencies to define work clearly so that the total price for work could be established at the time orders are issued.¹³

¹²GAO/NSIAD-00-56.

¹³FAR 16.505 (a).

Although this requirement was in effect for the period of our review, we found that FedSource routinely allowed modifications to orders through work assignments that substantially increased the total price of the orders.

FedSource did not provide contractors the opportunity to submit offers for orders under multiple-award contracts and have their offers fairly considered, as required by the FAR. FedSource officials told us that their business model does not provide contractors the opportunity to submit offers on orders. Instead, FedSource officials told us that administrative personnel were responsible for providing contractors a fair opportunity to be considered for work under multiple-award contract orders when assigning specific work to contractors. However, we found this generally did not occur. Of the 120 work assignments we reviewed, 75 were for work under multiple-award contracts. We found that in most of the 75 work assignments, FedSource administrative personnel did not provide contractors this opportunity. For example, FedSource used one of these contracts to fill several individual support staff positions at Brooke Army Medical Center at Fort Sam Houston and generally assigned work to one of the three multiple-award contractors without providing the other two contractors an opportunity to be considered. Justifications accompanying these assignments stated that assigning work to more than one contractor might create conflict among assigned staff over variations in pay and benefits. The Army's Fort McCoy used FedSource to obtain contractor support for a variety of construction projects, and FedSource assigned the work noncompetitively for all 12 work assignments we reviewed to 1 of 3 multiple-award contract holders—totaling \$7.2 million. The contract holder, a firm specializing in staffing, subsequently passed the work through to local construction companies that Fort McCoy officials had identified. Justifications accompanying some of the projects stated that the FedSource contracting officer's representative had determined that it was "in the best interest of the government to award task orders to the vendor that solicited and brought in the business." A FedSource quality review later concluded that these justifications were inadequate. Many months after the assignments were made, a second justification was placed in the contract files citing numerous reasons for selecting the preferred contractor. One of the reasons was that the project required expedited effort to support urgent requirements, which might have been an acceptable reason, except that the justification did not indicate that use of the other two contractors would have resulted in unacceptable delays.

In another example, the Navy needed to fill several administrative positions at its 31 regional recruiting centers around the country. Under another purchasing arrangement,¹⁴ FedSource assigned the work to two contractors, one for recruiting centers east of the Mississippi River and the other for centers to the west of the river. These arrangements did not establish prices for any of the services provided, and FedSource personnel told us that they accepted the prices provided by the contractors. This type of purchasing arrangement does not justify purchasing from only one source—contracting officers are still required to solicit price quotations from other sources. However, there was no evidence FedSource personnel had negotiated or analyzed these prices.

In addition, FedSource did not always demonstrate that prices were reasonable.¹⁵ For example, in two of the customer projects we reviewed, FedSource made work assignments for construction services at the Army's Fort McCoy and Fort Snelling against a contract for operational support. Because the original contract had a very broad and undefined statement of work that did not explicitly include construction, no prices for that type of work had been established in the contract. For the project at Fort McCoy, the contractor that received the assignment solicited prices from potential subcontractors and presented their price, including a markup, to FedSource. We did not find any analysis to determine that the contractor's price was reasonable in FedSource's files. FedSource officials told us that they have since awarded a separate contract for construction services.

In four of the five projects involving staffing support, FedSource paid contractors higher prices for services than were established in the contract. Most of the files we reviewed contained no justifications for the higher prices. For example, in our review of 25 work assignments for staffing support services at an Army medical center, 14 of the work assignments were priced higher than the price established in the contracts. In 9 of these cases, FedSource had agreed to additional sick leave or vacation time as part of the hourly rate, but FedSource's contract file

¹⁴FedSource filled this requirement using two blanket purchase agreements. These blanket purchase agreements must follow section 13.303-5 of the FAR, which requires obtaining quotes from other vendors.

¹⁵The Treasury franchise fund primarily develops multiple-award contracts under section 16.505 of the FAR. When ordering services that are not specifically established in the contract, ordering offices are required to establish prices using the pricing procedures of FAR subpart 15.4. FAR Subpart 15.402 requires that supplies and services are purchased at fair and reasonable prices.

contained no documentation indicating that the contractor employee qualified for the additional benefits.

DOD Focused on Convenience and Did Not Pay Sufficient Attention to Analyzing Contracting Alternatives

DOD did not follow sound management practices designed to ensure value while expeditiously acquiring goods and services. DOD customers chose to use franchise funds based on convenience, rather than as part of an acquisition plan. DOD conducted little analysis, if any, to determine whether using franchise funds' contracting services was the best method for acquiring a particular good or service. For their part, although franchise funds' business operating principles require that they maintain and evaluate cost and performance benchmarks against their competitors, they did not perform analyses that DOD could use to assess whether the franchise funds deliver good value. Their performance measures generally focus on customer satisfaction and generating revenues, rather than proper use of contracts and sound management practices. This focus on customer satisfaction and generating revenues provides an incentive to emphasize customer service rather than ensuring proper use of contracts and good value.

DOD Selected Franchise Funds for Convenience with Limited Analysis of Alternatives

DOD customers told us that they did not formally analyze contracting alternatives but generally chose to pay GovWorks and FedSource to provide contracting services because the franchise funds provided quick and convenient service. Some customers were dissatisfied with the speed and quality of services provided by DOD's in-house contracting offices. For example, two DOD customers told us that their contracting offices required 9 months to respond to their purchasing needs, while the franchise fund required only a few weeks. The franchise fund's ability to place orders quickly was valuable to DOD customers in these situations. DOD customers said that franchise funds' contracting services were less restrictive than other DOD contracting alternatives. Some DOD customers told us that GovWorks and FedSource made it easier to spend funds at the end of a fiscal year unlike DOD's in-house contracting offices. Two DOD customers said that GovWorks made it easier to spend small amounts of funding because GovWorks would place orders incrementally as funding became available. Some DOD customers mentioned that using FedSource meant they did not have to "live with the terms and conditions" of a long term contract or that it was easier to replace problem contractor employees. In one case, we were told that, if the organization had to fill positions with government employees, it would have less flexibility to hire the personnel it needed in a timely manner.

Analysis of contracting alternatives helps to ensure that purchases are made by the most appropriate means and are in DOD's best interest; however, DOD has no clear mechanism for making this determination when using other agencies' contracting services. DOD's guidance on the use of these vehicles has been evolving for several years and has not yet been fully implemented. DOD also lacks a means to gather data on the use of interagency contracts on a recurring basis, although it has been subject over the years to various requirements to monitor interagency purchases. In 2003, in response to a congressional mandate,¹⁶ DOD was unable to compile complete data on spending through interagency contracts. DOD officials told us that their financial systems are not designed to collect this data. Without this type of data, it is difficult to make informed decisions about the use of other agencies' contracting services. DOD issued guidance in October 2004 that requires the military departments and defense agencies to determine whether using interagency contracts—such as those the franchise funds manage—is in DOD's best interest. While this guidance outlines procedures to be developed, and general factors to consider, it does not provide specific criteria for how to make this determination and does not require military departments and agencies to report on the use of interagency contracts. DOD has directed the military departments and defense agencies to develop their own guidance to implement this policy. Congress has also recently taken action to ensure DOD's proper use of interagency contracts.¹⁷ The conference report accompanying this legislation established expectations that DOD's procedures will ensure that any fees paid by DOD to the contracting agency are reasonable in relation to work actually performed.

In 2001, Congress adopted legislation requiring DOD to establish a management structure and establishing savings goals for the procurement of services.¹⁸ The legislation also requires DOD to ensure that contracts for services are entered into or issued and managed in compliance with applicable laws and regulations regardless of whether the services are

¹⁶National Defense Authorization Act for Fiscal Year 2003, Pub. L. No. 107-314 § 824 (2002).

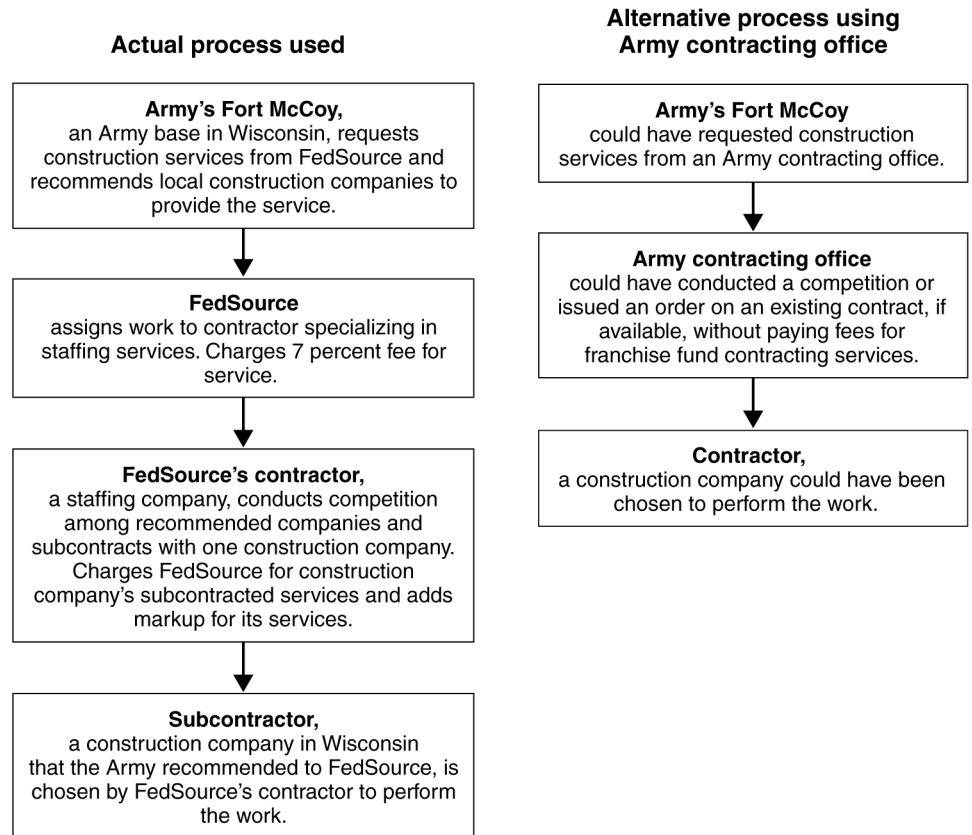
¹⁷National Defense Authorization Act for Fiscal Year 2005, Pub. L. No. 108-375, § 854 (2004). The act prohibits DOD from purchasing goods or services through the use of an interagency contract unless the purchase is made in accordance with procedures for reviewing and approving the use of these contracts. These requirements take effect 180 days after the enactment of the act.

¹⁸10 U.S.C. § 2330 as added by section 801 of the National Defense Authorization Act for Fiscal Year 2002. Section 802 added a note to 10 U.S.C. § 2330 establishing savings goals.

procured by DOD directly or through a non-DOD contract or task order.¹⁹ One of the goals of this legislation was to allow DOD to improve the management of the procurement of services. However, DOD generally chose to use franchise funds for reasons of speed, convenience, and flexibility rather than taking a strategic and coordinated approach to acquiring services. We found that prior to choosing to use a franchise fund, DOD did not analyze costs and benefits or prepare business cases to determine whether the franchise fund provided better value—considering the fees it charges—compared with other alternatives, such as using a DOD contracting office or purchasing goods or services through another federal agency’s existing contract. As a result, DOD customers did not consider opportunities to leverage their buying power when using franchise funds. None of the DOD customers we spoke to analyzed trade-offs between total price, including fees, and the benefits of convenience. For example, on a group of work assignments for construction services valued at \$7.2 million, the Army’s Fort McCoy paid FedSource a total of about \$1 million, or 17 percent above the subcontractor’s proposed price, for the contractor markup and the franchise fund fee. Most of these assignments were placed towards the end of the fiscal year. This may have led to a higher price for the services than DOD would have paid in contracting directly with the subcontractors. Figure 2 shows the general process by which the Army’s Fort McCoy used FedSource to obtain contractor support for construction services.

¹⁹10 U.S.C. § 2330. DOD began implementing these requirements in May of 2002 by requiring the military components to propose their own process and procedures for management and oversight of all acquisition services.

Figure 2: Example of Project for Which Army Paid FedSource 17 Percent In Fees and Markups



Source: FedSource (data); GAO (analysis).

The DOD customer said that FedSource made it easier than his own contracting office to assign work with values greater than \$25,000 late in the fiscal year because FedSource's deadlines were not as strict. He also speculated that the subcontractor probably would have charged more if contracting directly with the government because dealing with the government is cumbersome and costly. He did not have information to indicate what the subcontractor's price might have been, nor did he perform any formal analysis to compare FedSource with other contracting opportunities.

Conducting a thorough analysis also might have given DOD a better understanding of the fees paid to make purchases through the franchise funds. For example, DOD customers sometimes paid a GovWorks fee, or

service charge, on top of a fee to use another agency's contract because GovWorks generally uses other agencies' contracts to make purchases for DOD customers. While some customers were aware of the fees they paid, in two cases, DOD customers selected GovWorks because its fees were lower than fees charged by other agencies; however, the customers did not realize that GovWorks' fees were in addition to the other agencies' fees. GovWorks' fees generally ranged from 2 percent to 4 percent of the price for goods and services purchased, and our analysis showed that FedSource fees ranged from 2 percent to 8 percent for the contracts and orders we reviewed. Congress has mandated that DOD agencies report fees paid for the use of other agencies' contracts in the past and required DOD to do so again for fiscal year 2005.²⁰

Franchise Funds Emphasize Customer Service over Good Value

The franchise funds' business operating principles require that they maintain and evaluate cost and performance benchmarks against their competitors. However, they did not perform analyses that DOD could use to assess whether the franchise funds deliver good value. FedSource claims that it achieves lower prices on goods and services because it aggregates requirements and negotiates price discounts. Further, FedSource claims that competition with other contracting offices provides an incentive to provide better quality at lower cost. However, this incentive may not drive costs down unless customers are sensitive to the cost of doing business with one agency over another and make decisions based on costs. Franchise fund officials told us that demonstrating these advantages was difficult because they lacked insight into the prices customers would have paid when using other contracting alternatives to fill their requirements. FedSource officials also explained that quantifying the value of the other benefits they provide—such as convenience and flexibility—is difficult. Instead, GovWorks and FedSource have used such measures as growth in total contracting activity and revenues as well as customer satisfaction but have little data to demonstrate that they provide better quality and lower price goods and services than other federal contracting alternatives can provide. In fact, GovWorks marketing materials emphasize convenience and value-added service rather than costs. In our prior work, we found that fee-for-service contracting arrangements emphasize the overall sustainability of the contracting

²⁰National Defense Authorization Act for Fiscal Year 2003, Pub. L. No. 107-314 § 824 (2002), and § 854 National Defense Authorization Act for Fiscal Year 2005, Pub. L. No. 108-375 (2004). The fiscal year 2005 requirement applies to all fees imposed on purchases exceeding the simplified acquisition threshold in fiscal years 2005 and 2006.

operation, as the fees collected are used to cover the costs of doing business, which may lead to a focus on customer service at the expense of compliance with contracting policy and procedures.

DOD and Franchise Funds Did Not Pay Sufficient Attention to Defining Outcomes or Overseeing Contractor Performance

DOD, GovWorks, and FedSource did not follow federal contracting procedures designed to ensure value while expeditiously acquiring goods and services. DOD and the franchise funds did not define desired outcomes and the specific criteria against which contractor performance could be measured and paid limited attention to monitoring contractors' work. As we have reported previously, it is not always clear where the responsibility lies for such critical functions as describing requirements, negotiating terms, and conducting oversight. Although the FAR states that contracting officers are responsible for including appropriate quality requirements in solicitations and contracts and for contract surveillance, the franchise funds do not have sufficient knowledge about the DOD customers' needs to fulfill these responsibilities without the assistance of the DOD customer. Recently, the franchise funds contracting operations performed some internal reviews that have findings similar to ours, and the funds are working to address the problems. These shortcomings mirror many of the findings of our previous work and are among the reasons we have designated interagency contracting as a governmentwide high-risk area.

GovWorks and FedSource Did Not Clearly Define Outcomes or Establish Criteria for Quality

In the GovWorks and FedSource cases we reviewed, required outcomes were not well-defined, work was generally described in broad terms, and orders sometimes specifically indicated that work would be defined more fully after the order was placed. GovWorks and FedSource files we reviewed lacked clear descriptions of outcomes to be achieved or requirements that the contractor was supposed to meet.

The FAR states that contracting officers are responsible for including the appropriate quality requirements in solicitations and contracts. Without these criteria, accountability becomes harder to determine and the risk of poor performance is increased. Clear definition of requirements promotes better mutual understanding of the government's needs. In a typical situation, the customer—a DOD program office, for example—is best qualified to know what it needs. However, once a DOD program office chooses to pay a franchise fund to make purchases on its behalf, the office must then rely on the franchise fund to provide the contracting expertise. The two parties have to work together to ensure that requirements for purchases are well-defined with sufficient detail to determine whether the

desired outcomes were met and the goods and services provided meet the government's needs. Critical information must be documented in order to make these determinations. GovWorks and FedSource use different processes, and the tables in appendix III explain some of the pertinent contract documents used to define desired outcomes and criteria.

In 7 of the 10 GovWorks orders we reviewed, statements of work were very broad. For example, six of these orders contained language stating that specific tasks could be added, deleted, or redefined throughout the period of performance. In some cases, DOD program officials told us that the statements of work were broad because they were not aware of all requirements when the order was placed or because they were operating in a constantly changing technological environment. DOD program officials also told us that the broad statements of work gave them flexibility to add requirements to existing orders as additional needs arose.

Orders placed by FedSource against its contracts contained only a very general statement—generally just a few words—describing the work in broad terms and an anticipated dollar value. These orders did not clearly describe all services to be performed or supplies to be delivered so that the full price for the work could be established when the order was placed, as required by the FAR. As noted earlier, FedSource officials explained that in their business model, orders were not intended to describe specific work to be completed. Instead, FedSource administrative personnel issued work assignments that were intended to provide the clear descriptions of desired outcomes that the orders did not. However, we found that these work assignments were often unclear as well. Five of FedSource's largest customer projects for DOD involved use of contracts to provide staff. Work assignments for staffing services often described the position to be filled, including a general outline of duties. However, the assignments did not contain criteria for evaluating the work performed by contract employees.

In addition, when providing staffing support, FedSource uses these contracts to fill positions individually, rather than describing functional needs or desired results. For example, at an Army medical center FedSource filled over 200 positions individually instead of aggregating these positions into fewer functional requirements. This acquisition approach does not provide contractors with the flexibility to determine how best to staff a function and does not lend itself to a performance-

based approach. Under performance-based contracting, the contracting agency specifies the outcome or result it desires and leaves it to the contractor to decide how best to achieve the desired outcome.²¹ FedSource officials said they were moving toward a more performance-based contracting approach.

To determine whether an environment had been created that would allow improper personal services relationships to develop, we interviewed officials at five DOD program offices that used FedSource contracts to staff individual positions. We asked questions about the work performed by the contractor employees and the relationships between the DOD customers and the contractor employees. The DOD officials said that generally: the services provided by the contract employee were integral to agency functions or missions; the contractor employees were providing services comparable to those performed using civil service personnel; and the services were provided on site and with the use of equipment provided by the government. With regard to the work relationships, DOD customers told us that government employees assigned and prioritized daily tasks for the contractor employees. FedSource guidelines also state that the government customer is responsible for verifying contract employee hours worked by signing the contractor's weekly timesheet. Further, a FedSource internal review found that statements of work contained "personal services-type language like 'under the direction of' or 'oversee' or 'duties' or 'job description.'" Our review also found documents that had been edited to revise similar language. FedSource officials were aware of the potential that these contracts might be used for personal services and took various steps to clarify that personal services were not to be provided. For example, FedSource officials provided training for DOD customers on how to avoid creating a situation that had the appearance of personal services. Although this training is a positive step, poorly defined statements of work provided the opportunity for situations to arise in which personal services relationships could develop.

FedSource relied on administrative staff, not contracting officers, to work with the customer to define and assign the specific tasks to be performed or the positions to be filled. A FedSource review found that trained contracting staff was needed for developing task order requirements and

²¹Performance-based services contracting emphasizes that all aspects of an acquisition be structured around the purpose of the work to be performed as opposed to the manner in which the work is to be performed, or broad, imprecise statements of work that preclude an objective assessment of contractor performance.

warranted contracting officers were required for issuing task orders. The FedSource administrative employees do not have the same level of expertise as contracting officers, who have specialized knowledge to ensure compliance with federal regulations and guidelines. Inadequacies we found in FedSource's contracting practices pointed to the challenges of relying on administrative personnel rather than contracting experts to review statements of work, choose appropriate contracting vehicles, ensure adequate competition, and sign off on assignments of specific work.

**DOD Customers,
GovWorks, and FedSource
Did Not Specify Necessary
Criteria for Contract
Oversight**

DOD customers, GovWorks, and FedSource often relied on methods of contract oversight that lacked performance measures to ensure that contractors provided quality goods and services in a timely manner. Typically, the franchise funds failed to include an oversight plan that contained specific quality criteria in their contracts or orders. Without this critical information, neither DOD nor the franchise funds could effectively measure contractor performance.

The FAR and DOD's procurement regulations require contract surveillance and documentation that it occurred.²² Contract surveillance, also referred to as oversight, is a contracting officer's responsibility, and DOD pays the franchise fund to assume the responsibilities of contracting officers. The Office of Management and Budget's Office of Federal Procurement Policy has issued policy stating that contract oversight begins with the assignment of trained personnel who conduct surveillance throughout the performance period of the contract to ensure the government receives the services required by the contract.²³ DOD guidance states that documentation constitutes an official record and the surveillance personnel assessing performance are to use a checklist to record their observations of the contractor's performance. The guidance also states

²²FAR 37.602-2, Quality assurance, FAR 46.104, Contract administration office responsibilities, and Defense Federal Acquisition Regulation Supplement 246.102.

²³Office of Federal Procurement Policy (Policy Letter 93-1). When contracting for services, in particular highly specialized or technical services, agencies should ensure that a sufficient number of trained and experienced officials are available within the agency to manage and oversee the contract administration function.

that all performance should be documented whether it is acceptable or not.²⁴

The GovWorks contract files we reviewed generally did not include contractor monitoring plans, quality assurance surveillance plans, test and acceptance plans, or other evidence of monitoring activities. However, the files did contain evidence that a contracting officer's representative from the DOD program office had been appointed to assist in performing contractor oversight. Although ensuring that contract oversight occurs is a contracting officer responsibility, GovWorks officials told us that surveillance plans were not usually kept in the GovWorks contracting officers' contract files. Instead, these plans were maintained by the contracting officer's representative at the DOD customer agency. When we asked about contract oversight, we found that in the absence of an agreed upon oversight plan, DOD customers generally ensured that there was some process in place for monitoring performance. Some customers described status meetings and regular progress reports, but generally told us that they had no specific criteria for monitoring contractor performance or established measures for determining the quality of services. Although GovWorks officials told us that their contracting officers did assist customers in measuring quality services from the acquisition planning stages through contract completion, we found little evidence that this actually took place.

We found that FedSource generally did not ensure that contractor oversight occurred. As was the case with GovWorks, FedSource officials told us that they encouraged DOD to develop criteria for quality. However, FedSource allowed general information—such as job descriptions—to serve as requirements, even though the job descriptions contained no criteria for measuring quality. These descriptions did not provide sufficient information to establish an oversight plan. FedSource did not appoint trained contracting officers' representatives from DOD to conduct on-site monitoring. Instead, FedSource relied on its own administrative personnel, who had been trained as contracting officers' technical representatives but were not located on-site with the customer, to assess contractor performance. Because they were not on-site, they could not observe the quality of the contractors' work, and FedSource generally took the absence of complaints from DOD customers as an indication that the

²⁴DOD, *Guidebook for Performance-Based Services Acquisition in the Department of Defense* (Washington, D.C.: December 2000).

contractor was performing satisfactorily. A FedSource official explained that FedSource guidelines state that the customer agency's acceptance of the contract employee's time sheet indicates agreement that services have met quality standards and requirements. This policy lacks clear criteria and measures to determine whether the contractor has provided quality services. In place of criteria, we found DOD customers said they generally evaluated performance of contractor staff based on informal observation and customer satisfaction.

The lack of adequate oversight is consistent with what we have reported in our recent work on contractor oversight for DOD service contracts, where we found that almost all of those that had insufficient oversight were interagency contracts. DOD explained that contractor oversight is not as important to contracting officials as awarding contracts and does not receive the priority needed to ensure that oversight occurs. DOD concurred with our recommendations to develop guidance on contractor oversight of services procured from other agencies' contracts, to ensure that proper personnel be assigned to perform contractor oversight in a timely manner no later than the date of contract award, and that DOD's service contract review process and associated data collection requirements provide information that will provide management visibility over contract oversight.²⁵

Oversight of Franchise Funds Has Been Limited

Aside from monitoring the contractors' performance, we also found that the departments of the Interior and the Treasury, which operate GovWorks and FedSource, respectively, and the Office of Management and Budget have conducted infrequent reviews of franchise funds' procurement activities. GovWorks and FedSource have recently conducted internal reviews of their operations that have identified concerns similar to those we found.

A GovWorks' 2004 Management Review identified such issues as lack of acquisition planning for work added to existing awards, unanticipated increases in the amounts of orders, and inadequate documentation of many requirements such as competitive procedures, determinations that changes were within the scope of the contract, the basis of award decisions, and that prices were fair and reasonable. FedSource officials

²⁵GAO, *Contract Management: Opportunities to Improve Surveillance on Department of Defense Service Contracts*, [GAO-05-274](#) (Washington, D.C.: March 2005).

recently started conducting “office assistance reviews.” A June 2004 FedSource review identified lack of documentation, use of purchasing agreements beyond their intended parameters and dollar limits, lack of price analysis, lack of quality assurance plans, and the need for warranted contracting officers rather than administrative personnel to perform much of the work.

While the operating principles for franchise funds require the funds to have comprehensive performance measures, these measures do not emphasize compliance with contracting regulations and generally focus on customer satisfaction, financial performance, and generating revenues to cover operating costs. Several customers we interviewed were unaware of compliance problems and told us that they believed the franchise funds placed orders on a competitive basis, analyzed prices, or otherwise sought to ensure the best deal for the government when the funds, in fact, did not. GovWorks has taken steps that address concerns raised in its own reviews, such as increased training for contracting officers, developing a written acquisition procedures manual, and creating a uniform system of contract file maintenance and sample documents to ensure adequate documentation. GovWorks officials also told us they are trying to improve competitive procedures by requiring all solicitations for DOD work to be posted on e-Buy, an online system to request quotes for products and services.²⁶ FedSource also has taken steps toward addressing concerns raised in this report, such as quality assurance planning, hiring contracting officers, and restructuring its operations. These initiatives are underway, and it is too early to tell whether they will improve contracting operations at the franchise funds.

The Office of Management and Budget’s oversight of franchise funds has been limited. The Office of Management and Budget and the Chief Financial Officers Council established business-operating principles as a foundation for effective franchise fund management and, as required by the Government Management Reform Act, submitted an interim report on the franchise fund pilot program to Congress in 1998. Among other efforts, the report recommended that the franchise funds should continue to seek opportunities to provide services at the least cost to the taxpayer,

²⁶e-Buy is an online Request for Quotations tool that allows federal buyers to send requests and receive quotes for products and services available under the GSA multiple-award schedules program. Implementing regulations for section 803 in the Defense Federal Acquisition Regulation Supplement state that posting of a request for quotations on “e-Buy” is one medium for providing fair notice to all contractors as required by the regulation.

contributing to reducing duplicative administrative functions and consequently to the costs of those functions. The report noted that the franchise funds' performance measures were in varying stages of development. The report recommended that the Office of Management and Budget should report to Congress on franchise fund activity prior to the expiration of the pilot authority and that the office should continue to develop and implement operating guidance for the franchise fund program. Although the Office of Management and Budget's budget examiners conduct some monitoring of franchise funds as part of their general oversight responsibilities, Office of Management and Budget representatives said they have not conducted any comprehensive reviews of franchise funds since they submitted the required report to Congress. Neither have they reviewed the funds' contracting practices.

Conclusions

GovWorks and FedSource, created as a result of governmentwide initiatives to improve efficiency, have streamlined contracting processes to provide customers with greater flexibility and convenience. However, GovWorks and FedSource have not always adhered to competitive procedures and other sound contracting practices. They have paid insufficient attention to basic tenets of the federal procurement system—taxpayers' dollars should be spent wisely, steps should be taken to ensure fair and reasonable prices, and purchases should be made in the best interest of the government. One factor contributing to these deficiencies is that the departments of the Interior and the Treasury have not ensured that the franchise funds' contracting services follow the FAR and other procurement policies. The franchise funds need to develop clear, consistent, and enforceable policies and processes that comply with contracting regulations while maintaining good customer service. Another contributing factor is that the roles and responsibilities of the parties involved in the interagency contracting process are not always clearly defined. GovWorks and FedSource are ultimately accountable for compliance with procurement regulations when they assume the role of the contracting officer. However, they often depend on the customer for detailed information about the customer's needs. To facilitate effective purchasing and to help obtain the best value of goods and services, all parties involved in the use of interagency contracts have a stake in clarifying roles and responsibilities. Additionally, franchise funds sometimes face incentives to provide good customer service at the expense of proper use of contracts and good value. These pressures are inherent in the fee-for-service contracting arrangement.

Because the franchise funds have not always adhered to sound contracting practices, DOD customers must be cautious when deciding whether franchise fund contracting services are the best available alternative. In addition to convenience and flexibility, decisions to use franchise funds should be grounded in analysis of factors such as price and fees. Further, to enhance DOD's ability to develop sound policies related to the use of franchise funds, DOD needs measurable data that would allow it to assess whether franchise funds' contracting services help lower contract prices, reduce administrative costs, and improve the delivery of goods and services. This information would also be useful in leveraging DOD's overall buying power through strategic acquisition planning. No one knows the total cost of using other agencies' contracting services. Without understanding total cost, value is elusive. In addition, DOD customers should ensure that taxpayers' dollars are spent wisely by sharing in the responsibilities for developing clear contract requirements and oversight mechanisms. DOD customers are the best source of information about their specific needs and are also best positioned to oversee the delivery of goods and services.

Given the incentive to focus on sustaining the franchise funds' operations and the many service providers from which customers like DOD may choose, objective oversight would help to ensure that franchise funds adhere to procurement regulations and operate as intended. The Office of Management and Budget, which designated and has previously evaluated the franchise funds, is well positioned to periodically evaluate, monitor, and develop guidance to improve the franchise funds' contracting activities.

Recommendations for Executive Action

While a number of actions to improve DOD's use of other agencies' contracting services are already underway, to enhance these initiatives, we make the following eight recommendations to DOD, the Interior, the Treasury, and the Office of Management and Budget.

To ensure that DOD customers analyze alternatives when choosing franchise funds and to provide DOD with the measurable data it needs to assess the value of the franchise funds' contracting services, we recommend that the Secretary of Defense take the following three actions:

- Develop a methodology to help DOD customers determine whether use of franchise funds' contracting services is in the best interest of the government. The methodology should include analysis of tradeoffs.

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- Reinforce DOD customers' ability to define their needs and desired contract outcomes clearly. This skill includes working with franchise fund contracting officers to translate their needs into contract requirements and to develop oversight plans that ensure adequate contract monitoring.
 - monitor and evaluate DOD customers' use of franchise funds' contracting services, prices paid, and types of goods and services purchased. Prices include franchise fund fees and fees for use of other interagency contracts.

To ensure that GovWorks and FedSource adhere to sound contracting practices, we recommend that the Secretaries of the Interior and the Treasury take the following two actions:

- develop procedures and performance measures for franchise fund contracting operations to demonstrate compliance with federal procurement regulations and policies while maintaining focus on customer service and
- develop procedures for franchise fund contracting officers to work closely with DOD customers to define contract outcomes and effective oversight methods.

To ensure that the FedSource workforce has the skills to carry out contracting responsibilities, we recommend that the Secretary of the Treasury take the following action:

- assign warranted contracting officers to positions responsible for performing contracting officer functions.

In order to provide incentives for the franchise funds to adhere to procurement regulations and to ensure that franchise funds operate as intended, we recommend that the Director of the Office of Management and Budget take the following two actions:

- Expand monitoring to include franchise funds contracting operations' compliance with procurement regulations and policies. These findings should be available to customers to ensure transparency and accountability to customers and the Congress.
- Develop guidance to clarify the roles and responsibilities of the parties involved in interagency contracting through franchise funds.

Agency Comments and Our Evaluation

We provided a draft of this report to DOD, the departments of the Interior and the Treasury, and the Office of Management and Budget for review and comment. We received written comments from DOD and the Department of the Treasury, which are reprinted in appendices IV and V respectively. The Department of the Interior and the Office of Management and Budget provided comments via e-mail.

DOD concurred with our recommendations and identified actions it has taken or plans to take to address them. In response to our recommendation that the Secretary of Defense develop a methodology to help DOD customers determine whether the use of franchise funds' contracting services is in the best interest of the government, DOD indicated that action had been taken through the issuance of a policy memo titled *Proper Use of Non-DOD Contracts* and subsequent policies issued by the military departments. We acknowledge the DOD policy memo in our report and note that this guidance describes general factors to consider but does not provide specific criteria for how to make this determination. The policies issued by the military departments establish procedures for review and approval of the use of non-DOD contract vehicles, but do not address methods of determining whether this is in the best interest of the government. Our recommendation takes these actions into account and encourages DOD to go further by developing a methodology to help customers assess contracting alternatives.

In response to our recommendation that DOD reinforce DOD customers' ability to define their needs and desired contract outcomes clearly, DOD maintained that it is the responsibility of the franchise fund contracting officer to decide whether or not the requirement is described accurately. Nonetheless, DOD committed to issue a memo by August 31, 2005, reinforcing the need for DOD customers to define clearly their requirements and articulate clearly their desired outcomes in the acquisition process. We believe that this memo, coupled with DOD's ongoing efforts to educate DOD customers about the use of interagency acquisitions, are steps in the right direction.

Finally, in response to our recommendation that DOD monitor and evaluate DOD customers' use of franchise funds' contracting services, DOD concurred but explained that the data capture systems that would provide this information are not yet in place. DOD stated that the Federal Procurement Data System-Next Generation would provide this capability in fiscal year 2006. However, data collection is just one step in the evaluation process. In addition to collecting data, DOD will also need to compare alternatives and prices in order to make more informed choices.

Further, the accuracy and reliability of interagency contracting data in the Federal Procurement Data System-Next Generation will depend heavily on accurate reporting by franchise funds.

The Department of the Interior concurred with our recommendations and identified actions it has taken or plans to take to address them. The Interior highlighted 2004 accomplishments and acknowledged a need for better documentation to demonstrate compliance and value provided. The Interior also committed to ensuring an adequate contracting staff and to publishing information to help DOD determine the value of using the franchise fund. In response to our recommendation that the Department of the Interior develop procedures and performance measures for franchise fund contracting operations to demonstrate compliance with federal procurement regulations, the Interior highlighted a number of recent efforts to improve performance, including its 2004 management control review and performance improvement plan that will monitor compliance with federal procurement regulations. This plan establishes a goal of 75 percent reduction in reportable findings. Interior also stated that it had revised its acquisition review process, awarded a contract for a third party acquisition review, and provided additional training to its staff. Interior committed to continue monitoring performance and creating guidance as needed. In response to our recommendation that the Interior develop procedures for franchise fund contracting officers to work more closely with DOD customers, the Interior highlighted efforts to train its contracting officers and develop policies for working with DOD customers.

The Department of the Treasury concurred with our recommendations and identified actions it has taken or plans to take to address them, including centralization of FedSource's acquisition workforce under one line of authority to allow for standardization and consistency. In response to our recommendation that FedSource develop procedures and performance measures for franchise fund contracting operations to demonstrate compliance with federal procurement regulations, the Treasury committed to continue to conduct reviews to measure and evaluate compliance with federal procurement regulations and policies. This is a positive step toward ensuring compliance. The Treasury also said that FedSource had instituted performance-based statements of work for its acquisitions. While this initiative focuses on some aspects of compliance and is important in managing contractor performance, our recommendation addresses the performance of the franchise fund. Developing performance measures related to compliance with procurement regulations would reinforce the agency's commitment to

compliance and provide a means to monitor and demonstrate progress. In response to our recommendation that FedSource develop procedures for franchise fund contracting officers to work more closely with DOD customers, the Treasury indicated that FedSource will also develop procedures to provide its customers with clear guidance for defining contract outcomes. In response to our recommendation that FedSource assign warranted contracting officers to positions responsible for performing contracting officer functions, Treasury stated that FedSource has hired contracting officers to perform all contracting officer functions.

OMB concurred with our recommendations that OMB expand its monitoring to include franchise funds contracting operations' compliance with procurement regulations and policies and develop guidance to clarify the roles and responsibilities of the parties involved in interagency contracting through franchise funds. OMB stated that its Office of Federal Procurement Policy (OFPP) proposed to include the implementation of our recommendations in an undertaking pertaining to governmentwide acquisition contracts and incorporate franchise funds into that project. As part of that project, OMB/OFPP is asking the designated agencies to develop plans to ensure cost-effective and responsible contracting. The plans will address (1) training to contracting staff; (2) customer staff training; (3) management controls to ensure contracts are awarded in accordance with applicable laws, regulations, and policies; (4) contract administration; and (5) periodic management reviews. OMB acknowledged that this was only a part of the solution. We encourage OMB to give additional consideration to providing guidance that would clarify roles and responsibilities of the parties involved in interagency contracting through franchise funds.

We are sending copies of this report to the Secretaries of Defense, the Interior, and the Treasury; the Director of the Office of Management and Budget; and interested congressional committees. We will provide copies to others on request. This report will also be available at no charge on GAO's Web site at <http://www.gao.gov>.

If you have any questions about this report or need additional information, please call me at (202) 512-4841 (cooperd@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on

the last page of this report. Other staff making key contributions to this report were Amelia Shachoy, Assistant Director; Lily Chin; Lara Laufer; Janet McKelvey; Kenneth Patton; Monty Peters; and Ralph Roffo.

In memory of Monty Peters (1948-2005), under whose skilled leadership this review was conducted.

A handwritten signature in black ink that reads "David E. Cooper". The signature is written in a cursive style with a large, sweeping initial "D".

David E. Cooper, Director
Acquisition and Sourcing Management

List of Congressional Committees

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

The Honorable Ted Stevens
Chairman
The Honorable Daniel K. Inouye
Ranking Minority Member
Subcommittee on Defense
Committee on Appropriations
United States Senate

The Honorable Duncan Hunter
Chairman
The Honorable Ike Skelton
Ranking Minority Member
Committee on Armed Services
House of Representatives

The Honorable C. W. Bill Young
Chairman
The Honorable John P. Murtha
Ranking Minority Member
Subcommittee on Defense
Committee on Appropriations
House of Representatives

Appendix I: Scope and Methodology

We reviewed legislation establishing the franchise fund pilot program, governmentwide guidance relating to the program, and reports summarizing program outcomes. We held discussions with Office of Management and Budget representatives responsible for overseeing and providing guidance for the program and with Department of Defense (DOD) officials responsible for oversight of procurement issues. We performed work at the franchise funds managed by the departments of the Interior and the Treasury and interviewed officials and reviewed records relating to Interior's GovWorks and Treasury's FedSource programs. The Interior and Treasury franchise funds accounted for about 76 percent of total revenues for the six franchise funds during fiscal year 2003 (the most recently completed fiscal year at the time we were planning our field work) and about 95 percent of all services the six funds provided DOD. Contracting services the GovWorks and FedSource programs provided accounted for over 95 percent of total revenues at the Interior and Treasury franchise funds. To gain insight into how DOD customers were using franchise funds and into franchise fund contracting processes, we reviewed documentation relating to 17 selected customer projects totaling \$249 million in funding provided and interviewed GovWorks and FedSource contracting personnel responsible for these projects and representatives of the DOD customers.

To determine how DOD customers determined whether franchise funds provided a good value, we interviewed representatives of DOD customers for the selected projects and reviewed available documentation relating to decisions to use franchise fund contracts. We also reviewed information available from the franchise funds that would indicate whether the franchise funds provided a good value, and interviewed franchise fund officials.

To determine how franchise fund contracting officers worked with DOD customers to define measurable quality standards for goods and services and develop effective oversight mechanisms, we reviewed contract documentation for selected customer projects that would establish quality standards, and documentation relating to contract oversight. We also discussed these issues with franchise fund contracting personnel. In addition, we discussed these issues with representatives of DOD customers and reviewed available documentation.

To determine whether franchise funds followed the contracting practices needed to ensure fair and reasonable prices, we reviewed contract documentation for selected customer projects to assess the extent to which contracting personnel sought competition for work and analyzed

proposed prices to determine whether they were fair and reasonable, and discussed these issues with contracting personnel. In addition, we discussed these issues with representatives of DOD customers and reviewed available documentation.

To select customer projects for review, we obtained data files from the Department of the Interior’s GovWorks and the Department of the Treasury’s FedSource contracting programs that reflected customer projects active during fiscal year 2003, and the dollar value of customer funding provided for these projects during the year. We ranked these projects in terms of funding provided and selected projects representing the greatest dollar value of customer funding provided—10 GovWorks projects accounting for \$164 million and 7 FedSource projects accounting for \$85 million. Table 5 summarizes GovWorks projects, and table 6 summarizes FedSource projects.

Table 5: GovWorks Fiscal Year 2003 Projects Reviewed (in Millions of Dollars)

DOD customer	Contractor	Fiscal year 2003 funding provided
Army Chief Technology Office	Cherry Road Technology	\$26.1
Air Force Deputy Chief of Staff Air and Space Operations	SAIC	21.3
Army National Guard Bureau Readiness Center	SRA International Inc,	19.4
Air Force Material Command	Lockheed Martin Inc.	17.4
Army Chief Information Office	TKC Communications Inc.	15.1
Army National Guard Bureau Chief Information Office	Booz Allen Hamilton Inc.	14.4
Army Program Manager for Signals Warfare	Lear Siegler Services Inc.	14.0
Army National Guard Bureau Readiness Center	Sprint Communications Company LP	13.6
Air Force Aging Landing Gear Life Extension Program	General Atomics Inc.	12.6
Navy Program Executive Officer for Information Technology	Bearing Point	10.6
Total		\$164.3

Source: GovWorks data.

Note: Total may not add due to rounding.

Table 6: FedSource Fiscal Year 2003 Projects Reviewed (in Millions of Dollars)

DOD customer	Fiscal year 2003 funding provided	Number of work assignments reviewed	Selection process for work assignments
Walter Reed Army Medical Center	\$27.2	66	Random selection
U.S. Army Fort McCoy	13.2	12	Size
Army 88th Regional Readiness Command at Fort Snelling	10.1	5	Size
The Pentagon	9.7	5	All ^a
Navy Recruiting Command	8.4	18	Random selection
Lackland Air Force Base	8.2	14	Random selection
Brooke Army Medical Center at Fort Sam Houston	8.1	25	Random selection
Total	\$84.9	145^b	

Source: FedSource data.

^aOne project only had five work assignments, and we reviewed all five assignments for that project.

^bWe eliminated 25 of these work assignments from our analyses because they used a contract that expired or that was discontinued by the end of fiscal year 2003.

GovWorks contracting personnel fulfilled the requirements of each project selected by award of a single order, and we reviewed contract documentation related to the relevant order. FedSource contracting personnel, in contrast, fulfilled the requirements of customer projects by award of one or more contracts or orders. Further, FedSource personnel initiated multiple work assignments—in some cases several hundred—to define specific work that would be performed under each of the contracts awarded or orders placed. Accordingly, we reviewed all contracts awarded or orders placed to fulfill the requirements of the selected customer projects and a sample of work assignments initiated under these contracts or orders. To select sample work assignments for review, we first ranked the work assignments in terms of dollar value of the work to be performed. For those projects where a relatively small number of work assignments accounted for a significant share of total project value, we selected the highest dollar value assignments representing at least 50 percent of total project value. For those projects where most individual work assignments represented only a small fraction of total project value, we selected all assignments valued at \$150,000 or more and a sample—selected at random—of the remaining work assignments.

We conducted our review between June 2004 and June 2005 in accordance with generally accepted government auditing standards.

Appendix II: Franchise Fund Operating Principles

Operating principle	Description
Services	The enterprise should only provide common administrative support services.
Organization	The organization would have a clearly defined organizational structure including readily identifiable delineation of responsibilities and functions and separately identifiable units for the purpose of accumulating and reporting revenues and costs. The funds of the organization must be separate and identifiable and not commingled with another organization.
Competition	The provision of services should be on a fully competitive basis. The organization's operation should not be "sheltered" or be a monopoly.
Self-sustaining/ full cost recovery	The operation should be self-sustaining. Fees will be established to recover the "full costs," as defined by standards issued in accordance with the Federal Accounting Standards Advisory Board.
Performance measures	The organization must have a comprehensive set of performance measures to assess each service that is being offered.
Benchmarks	Cost and performance benchmarks against other "competitors" are maintained and evaluated.
Adjustments to business dynamics	The ability to adjust capacity and resources up or down as business rises or falls, or as other conditions dictate, if necessary.
Surge capacity	Resources to provide for "surge" capacity and peak business periods, capital investments, and new starts should be available.
Cessation of activity	The organization should specify that prior to curtailing or eliminating a service, the provider will give notice within a reasonable and mutually agreed time frame so the customer may obtain services elsewhere. Notice will also be given within a reasonable and mutually agreeable time frame to the provider when the customer elects to obtain services elsewhere.
Voluntary exit	Customers should be able to "exit" and go elsewhere for services after appropriate notification to the service provider and be permitted to choose other providers to obtain needed service.
Full-time equivalents accountability	Full-time equivalents would be accounted for in a manner consistent with the Federal Workforce Restructuring Act and Office of Management and Budget requirements, such as Circular A-11.
Initial capitalization	Capitalization of franchises, administrative service, or other cross-servicing operations should include the appropriate full-time equivalents commensurate with the level of effort the operation has committed to perform.

Source: Office of Management and Budget and the Chief Financial Officers Council.

Note: These principles were developed by the Office of Management and Budget and the U.S. Chief Financial Officers Council. The U.S. Chief Financial Officers Council is an organization of the chief financial officers and deputy chief financial officers of the largest federal agencies and senior officials of the Office of Management and Budget and the Department of the Treasury who work collaboratively to improve financial management in the U.S. government.

Appendix III: Overview of Contract Documents Used at GovWorks and FedSource

Table 7: GovWorks Contract Documents Used to Define Desired Outcomes and Performance Criteria

Master contract or another agency's contract	Master contract contains information about the general scope of work; however, the exact dates and quantities of future deliveries are not known. The contract also includes additional details, such as maximum or minimum quantities that can be ordered under each individual order and the maximum that it may order during a specified period of time, and the time frame that contract remains valid. Under the GSA schedules (also referred to as multiple-award schedules and Federal Supply Schedules) Program, GSA establishes long-term governmentwide contracts with commercial firms to provide access to commercial supplies and services. Schedule contracts contain much of the same information as other master contracts.
Purchase request	DOD customer describes the needs for goods or services and describes desired outcomes and quality standards that contractors are expected to meet.
Task or delivery orders	Multiple orders can be written off of a master contract. Orders define work to be performed; location of work; period of performance; deliverable schedule; applicable performance standards; and any special requirements. Individual orders shall clearly describe all services to be performed or supplies to be delivered so the full cost or price for the performance of the work can be established when the order is placed.

Source: GAO analysis of GovWorks documents and interviews with GovWorks officials.

Table 8: FedSource Contract Documents Used to Define Desired Outcomes and Performance Criteria

Master contract	Contracting officers develop master contract based on anticipated needs. Master contract contains information about the general scope of work; however, the exact dates and quantities of future deliveries are not known. Also includes additional details, such as maximum or minimum quantities that the government may order under each individual order and the maximum that it may order during a specified period of time, and the time frame that contract remains valid.
Order	Multiple orders can be written off of master contract. FedSource contracting officers issue orders to each contractor based on anticipated business for the year. FedSource briefly describes types of services and obligates funds to cover anticipated work. At this point, FedSource does not know exact quantities or dates of future deliveries.
Purchase request	DOD customer describes needs for goods or services. Program office describes desired outcomes and quality standards that contractors are expected to meet.
Work assignment	FedSource uses work assignment to define work to be performed, location of work, period of performance, deliverable schedule; applicable performance standards, and any special requirements.

Source: GAO analysis of FedSource documents and interviews with FedSource officials.

Appendix IV: Comments from the Department of Defense



ACQUISITION,
TECHNOLOGY
AND LOGISTICS

OFFICE OF THE UNDER SECRETARY OF DEFENSE
3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000

JUL 2 2 2005

Mr. David E. Cooper
Director, Acquisition and Sourcing
Management
U.S. Government Accountability Office
441 G. Street, NW
Washington, DC 20548

Dear Mr. Cooper:

This is the Department of Defense (DoD) response to the GAO draft report, "INTERAGENCY CONTRACTING: Franchise Funds Provide Convenience, but Value to DoD is not Demonstrated," dated June 30, 2005, (GAO Code 120357/GAO-05-456).

The report recommends that the Secretary of Defense develop a methodology to help DoD customers determine whether use of franchise funds' contracting services is in the best interest of the government, that the Secretary of Defense reinforce DoD customers ability to define their needs and desired contract outcomes early and that the Secretary of Defense monitor and evaluate DoD customers' use of franchise funds' contracting services, prices paid and types of goods and services purchased.

The Department concurs with the recommendations. Our comments on the report are enclosed. Thank you for the opportunity to review and comment on the subject draft report. For any questions concerning this response, please contact Mike Canales, on 703-695-8571 or via e-mail at Michael.Canales@osd.mil.

Sincerely,

Deidre A. Lee
Director, Defense Procurement
and Acquisition Policy

Enclosure:
As stated



**DoD COMMENTS ON
GAO DRAFT REPORT - DATED JUNE 30, 2005
GAO CODE 120357/GAO-05-456**

**“INTERAGENCY CONTRACTING: FRANCHISE FUNDS PROVIDE
CONVENIENCE, BUT VALUE TO DOD IS NOT DEMONSTRATED”**

**DEPARTMENT OF DEFENSE COMMENTS TO THE
RECOMMENDATIONS**

RECOMMENDATION 1: The GAO recommended that the Secretary of Defense develop a methodology to help DoD customers determine whether use of franchise funds’ contracting services is in the best interest of the government—the methodology should include analysis of tradeoffs. (p. 29/GAO Draft Report)

DoD Response: Concur. Actions have already been taken at both DoD and Military Department (MILDEP) levels that address this recommendation. The OSD policy memo of October 29, 2004, entitled, “Proper Use of Non-DoD Contracts,” and companion policy memos from the MILDEPS including Air Force policy memo dated December 6, 2004, the Navy policy memo dated December 20, 2004, and the Army policy memo dated July 12, 2005 (interim policy memo previously issued) were issued to provide direction to program managers, requirements personnel, financial management personnel and contracting personnel. The OSD memo places primary responsibility for compliance on acquisition Program Managers/Requirements personnel. It also identifies that a team approach, involving Contracting and Financial Management personnel, is best to ensure that acquisition strategies comply with policy and that the use of a non-DoD contract is in the best interest of the government. The DoD policy was jointly signed by the Acting Under Secretary of Defense for Acquisition, Technology, and Logistics and the Principal Deputy Under Secretary of Defense (Comptroller). All MILDEP policy memos implement the policy and provide a framework of the key aspects needed for compliance.

RECOMMENDATION 2: The GAO recommended that the Secretary of Defense reinforce DoD customers’ ability to define their needs and desired contract outcomes clearly. This skill includes working with franchise fund contracting officers to translate their needs into contract requirements and to develop oversight plans that ensure adequate contract monitoring. (p. 29/GAO Draft Report)

Enclosure

DoD Response: Concur. DoD will issue a memo to reinforce the need for DoD “customers” to clearly define their requirements and clearly articulate their desired outcomes in the acquisition process. The expected date for issuance of the memo is August 31, 2005. If the decision has been made to use a franchise fund activity, it is the responsibility of the franchise fund contracting officer to ensure the DOD customers’ needs and desired outcomes are defined in a way that allows for proper solicitation, evaluation, award, performance and post award administration. Ultimately the franchise fund Contracting Officer must make a decision on whether or not the requirement is described adequately. In the same vein, the franchise fund and requiring activity must work together to perform appropriate contract monitoring.

RECOMMENDATION 3: The GAO recommended that the Secretary of Defense monitor and evaluate DoD customers’ use of franchise funds’ contracting services, prices paid, and types of goods and services purchased. Prices include franchise fund fees and fees for use of other interagency contracts. (p. 29/GAO Draft Report)

DoD Response: Concur. However, current data capture systems are not in place that will provide this information easily and consistent with policy requirements. The functionality to support this reporting will be established in the Federal Procurement Data System-Next Generation (FPDS-NG). The target date for implementation is Fiscal Year 2006. DoD is working with the MILDEPS to satisfy the requirements of Section 854 of the FY05 National Defense Authorization Act, which may provide some of this information sooner.

Enclosure

Appendix V: Comments from the Department of the Treasury



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

JUL 25 2005

Mr. David E. Cooper
Director, Acquisition and Sourcing Management
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Mr. Cooper:

I am writing to provide the Treasury Department's comments on the Government Accountability Office's draft report, entitled *Interagency Contracting: Franchise Funds Provide Convenience, but Value to DOD is Not Demonstrated*.

I would like to state that prior to your GAO audit, the FedSource centralized their acquisition workforce into a new Acquisition Center. This action was taken to address weaknesses identified through internal compliance evaluations and validated during this audit. Placing the FedSource contracting officers and other related acquisition personnel under one line of authority will allow for standardization and consistency.

The following comments below address your recommendations in the report.

Recommendation: The FedSource should develop procedures and performance measures for franchise fund contracting operations to demonstrate compliance with federal procurement regulations and policies while maintaining focus on customer service

I agree and the FedSource and their contracting office are conducting joint compliance reviews to measure and evaluate compliance with federal procurement regulations and policies. On all recent work, FedSource has instituted performance-based statements of work and quality assurance surveillance plans to ensure proper solicitation, evaluation, award, performance and post award administration.

Recommendation: The FedSource should develop procedures for franchise fund contracting officers to work closely with DOD customers to define contract outcomes and effective oversight methods.

I agree and the FedSource will be putting procedures in place to provide customers with clear guidance to define contract outcomes. FedSource has instituted performance-based statements of work and quality assurance surveillance plans to ensure proper solicitation, evaluation, award, performance and post award administration.

Recommendation: The GAO recommends FedSource assign warranted contracting officers to positions responsible for performing contracting officer functions.

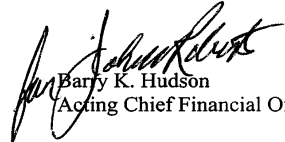
**Appendix V: Comments from the Department
of the Treasury**

-2-

I agree and the FedSource has hired Contracting Officers to perform all contracting officer functions. FedSource is conducting joint compliance reviews with their contracting office to measure and evaluate compliance with federal procurement regulations and policies.

Thank you for the opportunity to respond to this draft GAO report. If you have any questions or wish to discuss these comments further, please contact me at (202) 622-0750.

Sincerely,



Barry K. Hudson
Acting Chief Financial Officer

cc: Martin Davis, Managing Director,
Treasury Franchise Fund

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