

~~11952~~

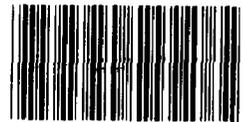
115083

UNITED STATES GENERAL ACCOUNTING OFFICE
Washington, D.C.

FOR RELEASE ON DELIVERY
EXPECTED AT 10:00 a.m.
THURSDAY, APRIL 29, 1981

[DOD Use of Consultant Service Contracts]

Statement of
Walton H. Sheley, Jr., *Director*,
MISSION ANALYSIS AND SYSTEMS ACQUISITION DIVISION
before the
Subcommittee on Human Resources
House Committee on Post Office and Civil Service
and the
Subcommittee on Civil Service, Post Office
and General Services
Senate Committee on Governmental Affairs



115083

016721

At the request of the former Chairmen of the Senate Subcommittee on Civil Service and General Services and House Subcommittee on Human Resources, we undertook an examination of DOD's use of consultant service contracts. It is our pleasure to appear before you today to discuss our recent report resulting from this request: "Controls Over DOD's Management Support Service Contracts Need Strengthening."

As agreed with the respective Chairmen, we reviewed a broader spectrum of contract support services than consulting services as defined by the Office of Management and Budget. We did so because on the basis of prior work we believe consulting services may be significantly understated in DOD, and past experience has shown that other types of management support services are subject to similar problems and abuses as consulting service contracts.

In fiscal year 1979, the latest year for which complete data was available at the time of our review, DOD spent about \$2.6 billion for all types of management support service contracts. These services ranged from relatively simple studies to aid in management decisions to contracts involving complex engineering support for major weapon systems.

In our recent review, we selected the following types of contracts for review:

- consulting services
- management and professional services and special studies and analysis

--research, development, test and evaluation--management
and support.

From computer listings detailing fiscal year 1979 actions within categories of contracts, we selected 14 purchasing offices with large dollar volumes of transactions for review. Each of the services and the Office of the Secretary of Defense were included among the offices selected. The total dollar value of fiscal year 1979 actions for these offices was about \$347.1 million, or 13.3 percent of the total fiscal year 1979 actions.

For each purchasing office, we randomly selected contract actions on fiscal year 1979 contracts. A total of 256 contract awards valued at about \$175.4 million were reviewed. We believe our findings are representative of the total universe of management support contracts.

[We found serious problems relating to DOD's use of contractor management support services. These problems range from the lack of in-house capability, frequency of unsolicited proposals, the heavy involvement of former DOD employees in contracts, the continuous nature of the support services, questionable need for some of the services, and poor contracting practices highlighted by the almost exclusive use of sole-source contracts. I will briefly discuss each of those problems.

In-House Capability

Our review has shown that DOD, at one time, had the in-house capability for much of the work currently being contracted out. This is apparent from the extensive involvement of former

DOD officials and employees in contracts included in our review. DOD is not adequately considering the in-house capability that it already has. In several instances where inhouse capability was available, we were told such capability was not relied on because of the need for (1) a timely study or (2) an "independent" or "objective" study. In other instances where in-house capability was available, contracting out was justified on the basis that in-house personnel were required for other work.

In 183 of the 256 contracts reviewed, or about 71 percent, we believe that the task contracted out raises the issue of the availability of in-house capability. The criteria we used to make this judgement was whether (1) the nature of the tasks performed under the contract suggested that it may have been governmental in nature, (2) in the past the work had been performed by DOD's in-house staff, and/or (3) work of a similar nature was currently being done by DOD staff. To illustrate:

--An \$82,138 sole-source contract was awarded on behalf of OSD to review Army support unit requirements for the first 30 days of a North Atlantic Treaty Organization war. We believe DOD should have performed this task since it deals with critical defense requirements. The contractor received the sole-source contract because of time constraints and his extensive experience. The contractor's experience base consisted of former DOD employees and military officers including a retired Lt. General and Lt. Colonel. Furthermore, DOD officials told us that a month

after the study was completed, in-house personnel were used to prepare another study similar in nature to the one contracted for.

--A sole-source contract totaling \$304,018 was awarded for services to assist in the development of a DOD Mobilization Plan. Some of the specific tasks given the contractor included: (1) development of improvements in the DOD management of the manpower mobilization system; (2) development of the framework for a Mobilization Plan; and (3) assistance in planning and preparing for a specific mobilization exercise. The justification for the contract was that in-house expertise was not available. In our opinion, DOD should possess the in-house expertise in such vital areas. It should be noted that the contractor used former DOD personnel. Consultants to the contractor included a former Vice Chief of the Army, a former Air Force General, and a former Deputy Assistant Secretary of the Army.

Unsolicited Proposals

Of the 256 contracts reviewed, 102, or approximately 40 percent, resulted from unsolicited proposals. In many cases, the proposal was the result of the contractors' unique knowledge of and/or experience with DOD. Once a contractor performs work in one area, he continues to receive contracts which build upon the experience in the particular area. While unsolicited proposals should not be prohibited, we believe that all too often, they are being used to (1) subvert the competitive process, (2) encourage work that may not be important relative to DOD's mission needs and priorities, (3) abrogate DOD's responsibilities over the scope and

direction of work related to defense management, and (4) are not truly unique or innovative. Some examples follow:

--The Air Force issued a task under a Basic Ordering Agreement for \$98,000, for a feasibility study on developing a model to be used by program managers to assess and measure the impact of the Integrated Computer Aided Manufacturing Program on the aircraft industry. This contract resulted from an unsolicited proposal by a firm whose Vice President was a former Deputy Assistant Secretary of Defense who had published several articles and papers relating to this subject matter. In April 1980, the contractor submitted another unsolicited proposal to perform a continuation effort which included the basic task of developing the model and two options at a total additional cost of \$400,000. An order for the development of the model was awarded to the contractor on a sole-source basis in August 1980 for \$178,655.

--The Army awarded a contract for \$199,505 based on an unsolicited proposal to study the readiness and sustainability of selected combat and artillery units. The contractor's capability to perform as outlined in the proposal was based on using former DOD employees, some of whom retired from the program office making the subject award.

Former DOD Employees

The involvement of former DOD military and civilian employees in contracts with DOD is extensive. Of the 256 contracts reviewed, 131, or 51 percent, involved former employees in capacities of top management as well as various technical levels. While the

use of former DOD employees does not necessarily constitute a conflict of interest, we believe the extensive involvement of former employees raise questions as to (1) the extent DOD uses the skills of former employees to perform functions similar to those performed while employed by DOD, (2) the objectiveness of work performed by former employees in areas where they were formerly involved, and (3) the degree of influence used by former top level DOD officials in securing contracts with DOD.

Some examples follow, which in our opinion, raised the foregoing questions.

--A contract was awarded on behalf of OSD for \$294,597 to survey drug and alcohol use and abuse within the military services. Due to misunderstandings between DOD and the contractor, the contract was modified, expanding the scope of work and increasing the cost by \$175,872. DOD officials acknowledged that in-house capability existed to perform the study, but because of past congressional criticisms, the decision was made to obtain an objective assessment from a contractor. The contract was awarded to a firm whose Vice President was a former Director of Research and Evaluation in the Office of Drug and Alcohol Abuse Prevention within the Office of the Assistant Secretary of Defense.

--The Army awarded a contract for \$29,995 to a retired DOD employee to prepare an annual report on DOD research facilities. This is the fourth in a series of contracts, which aggregate \$120,345 awarded to this individual. The annual report is the same report that the contractor assisted in or prepared from

1966 to 1973 as a DOD employee. Program officials told us they are aware of the fact that the report should be prepared by in-house staff, but they continue to contract out for it.

Continuous Contracts

As a result of "unique in-depth knowledge," "qualifications," or "unique expertise obtained during performance of previous work," we found contractors essentially being assured of continuous contracts resulting in virtually perpetual sole-source positions.

We found that 146 contracts, or approximately 57 percent of the contracts reviewed, were repeatedly renewed--ranging in periods from 2 to 28 years.

In addition, we found few cost studies that justified contracting out as the least costly alternative. In many cases, contracts have been renewed annually without an evaluation of the relative costs of in-house versus contract performance. The failure to consider the in-house costs of performing work of a continuous nature may result in DOD paying significantly more for services which are essential to accomplishing DOD's mission.

Consideration of the least costly form of work force is only applicable to those functions which are not governmental in nature. For activities which can be considered governmental functions, such as management of programs requiring value judgments in directing national defense--cost is not relevant. OMB Circular A-76 specifically provides that a governmental

function is a function which must be performed in-house due to the special relationship which exists in executing governmental responsibility. To illustrate:

--The Air Force awarded a sole-source contract for \$1,624,037 to (1) provide support to a program office's data base and (2) provide in-depth studies of Soviet and People's Republic of China research and development facilities and resources. The contractor has had a sole-source contract to perform this type of work since 1951--a period of 28 years. Program officials told us that there have been no studies performed of the relative costs involved in contracting out versus performing the work in-house. All indications are that this work will continue to be contracted out on a sole-source basis in the future. The contract was modified three times expanding the work scope, extending the period of performance 4 months, and increasing costs by \$1,298,000 to \$2,922,037. It should also be noted that three of the contractor's employees involved with the work are former DOD employees/service members, and a consultant to the contractor was formerly assigned to the program office.

--The Navy awarded a \$190,000 contract to continue for the 7th year studies of economic and cost factors of strategic weapons systems in connection with the systems' vulnerability and effectiveness. The total contract amount was subsequently increased by \$65,000. Program office officials advised

us that the Navy's decision to use the contractor to develop the in-house DOD capability to do missile cost analyses was the basis for the contractor's initial effort. The contractor was then able to receive follow-on sole-source contracts on the basis of the initial and ever increasing experience. We were further advised that the Navy planned to extend the contract another year, through fiscal year 1981, at an additional cost of \$50,000.

Need For Services

The contracting methods and procedures used by DOD do not assure that the services are needed. Of the 256 contracts reviewed, we found 44, or about 17 percent, to be of questionable value in terms of DOD's priorities and mission. The criteria we used to make this judgment were basically (1) the subject matter of the contract indicated that the information should already be available in the Federal Government, (2) the questions raised which justified the study could or should have been answered by the service itself and/or other DOD activities, or (3) the contract results appeared to be of questionable use to DOD. For example:

--A Navy contract was awarded for \$43,000, of which \$23,000 was for data on the technical aspects of a Naval test range. The data was to be used in making a decision on the relocation of the test range. Program officials told us that the technical data was available and could have been obtained

directly from the Naval activity operating the range. This activity, however, was not contacted because its objectivity was considered questionable. Instead, a contractor was paid to obtain the data from Navy sources.

--The Navy awarded a \$124,529 contract to provide engineering and management support of a development surface effect ship. Shortly after this contract was awarded, and before the first task was issued, DOD terminated the prime ship development contract. At that time the engineering and management support contract could have been terminated for the convenience of the Government. However, program officials advised us that at the direction of higher officials, they were urged to continue this effort. The Navy, in an effort to obligate, rather than lose any portion of the program's remaining \$4.1 million fiscal year 1980 budget, programmed an additional \$96,000 to continue engineering efforts on a cancelled program by the Congress.

Sole-Source Awards

We found sole-source contracting to be the rule rather than the exception at DOD. Of the total 256 contracts reviewed valued at about \$175.4 million, 211 (82 percent) were sole source.

The justifications for sole-source contract awards were essentially based on the contractor's previous and/or continuous contractual relationship with DOD. The justifications cited either "unique experience," "in-depth knowledge of operations," or the need for timely completion. Contributing factors involved in sole-source awards are unsolicited proposals and the involvement of former DOD employees in contract performance. Some examples which

cast doubt on the original sole-source justification follow.

--A \$30,000 sole-source contract was awarded on behalf of OSD to assist in developing and supporting a new NATO Logistics Directorate. The sole-source award was justified on the basis of immediate time requirements. As a result of modifications, the due date of the final product was extended 7 months. The final report was completed and delivered 6 months beyond the extended due date. Program officials stated that two of five options considered at the time of award identified the use of in-house personnel to accomplish this work.

--An OSD contract valued at \$192,696 was issued to develop a standard method of forecasting personnel requirements for the Foreign Military Sales Program. The contract was the result of an unsolicited proposal by a contractor who had formerly developed a personnel accounting system for the program. The sole-source justification cited urgency, because the results were needed for the budget submission. The final product, however, was not due until November 15, 1980--too late for the budget submission.

Summary

Our current report, as well as our previous report of consulting services at civilian agencies, have clearly shown that the foregoing problems exist for the entire universe of support service contracts. These problems are not unique to consulting service contracts as defined by OMB.

Consulting services are a small part of the overall universe of management support services at Federal agencies. In our opinion, it makes little sense to focus attention and establish special controls over only consulting services. This is

particularly true in view of our finding that essentially the same types of problems exist in all types of contract management support services.

RECOMMENDATIONS

GAO has issued over 30 reports during the past 20 years identifying deficiencies related to the use of consulting services. One of the major issues identified was the failure to obtain adequate competition in awarding procurement contracts for these services. Normally, we are opposed to legislative remedies for problems that should be resolved administratively. However, we believe this problem is serious enough in DOD to warrant legislative action.

Accordingly, we have recommended that the Congress, as an interim measure, consider legislation which would minimize the funding of sole-source contracts for management support services and the funding of such contracts resulting from unsolicited proposals. One way to accomplish this might be to establish quotas for a period of 2 to 4 years. For example, the Congress might require that not more than 50 percent of the total dollars spent by an agency for management support service contracts may be used to fund sole-source contracts. This figure could be adjusted in future years until a more acceptable balance is achieved.

We also believe action by OMB is necessary. The Director of OMB should:

- Extend the management controls outlined in OMB Circular A-120 to other categories of management support services.

--Assure that agencies identify all requested funds to be used for management support services and provide this information to the Congress.] Such identification would provide the basis for the Congress to review agencies' use of such services as well as provide a base from which to control funds available for such services.] We believe that OMB could satisfy this recommendation by extending the requirements of OMB Bulletin No. 80-13 for the types of management support services identified in this report.

Further, we believe [the Secretary of Defense should take the following actions:

- Require DOD activities to establish an independent review board to assure the highest level review of proposed contract awards and modifications over \$100,000 for management support services. This independent assessment is particularly critical for those contracts to be performed by former DOD employees.
- Identify functions being performed by contractors which are governmental in nature, and determine personnel needs and develop ways to meet those needs.
- Identify management support services which are not governmental in nature and which are required on a continuing basis. For each service, an assessment should be made of current in-house capability, the possibility of acquiring such capability, and the relative costs involved in performing the work in-house versus contractor support.

Agency Comments

OMB agreed that our report makes a strong case for more stringent controls to eliminate weaknesses in and curtail abuses of DOD's procurement of management support services. However, OMB does not totally agree with our recommendations. OMB believes that legislation is not necessary to solve the problems with contracting for management support services. It is currently considering issuing an OMB bulletin and a revision to an existing circular which it believes will correct the problems illustrated in our report.

We believe OMB's planned actions, if carried out, are commendable, but several of its suggested actions will not result in meaningful improvements in contracting for management support services.

OMB intends to eliminate the majority of improper sole-source awards by removing the incentives to use unsolicited proposals for management support service contracts. In our opinion, this proposed action will result in fewer unsolicited proposals but will not by itself have a major impact on the number of sole-source awards. We continue to believe legislation is necessary to correct this longstanding problem.

OMB does not believe that a specific entry (budget line item) for consulting services within the object classification schedules for each agency account in the budget is necessary, appropriate, or practicable. Our recommendation for budgetary identification does not require a specific entry for management support services.

Our report clearly demonstrates that the problems identified are not restricted to consulting service contracts alone but instead, are prevalent throughout the entire universe of management support service contracts. With the implementation of OMB Bulletin No. 80-13, budgetary identification of consulting services is already required. We believe that OMB could satisfy this recommendation by extending the existing requirement to include the types of management support services identified in this report and providing the information to the Congress.

Finally, OMB believes that review and approval of management support service contracts by a level above the sponsoring activity will provide sufficient control. We continue to believe that review and approval by an independent board is a more desirable approach. Such a board or boards would have no direct benefit from the outcome of their decision and would bring management support services under a proper degree of independent and objective scrutiny.

Although this report was furnished to DOD for comment, its written comments are not included in our report because they were received after the report was signed. Attached for inclusion in the record is a copy of their comments and our analysis of them. In summary, DOD stated it agreed with the thrust of our report but disagreed with several of the findings and with our recommendations.

First, DOD did not agree that it was relying on contractors to perform defense management functions of a governmental nature.

It argues that it has policies and directives which prohibit using contractors to perform governmental functions. It also admits that it has lost certain kinds of in-house capability, which it formerly possessed, because of salary considerations, because A-76 encourages contracting out, and because of federal hiring policies. We agree that there are policies and directives which prohibit contracting for governmental functions. However, we found many cases where there was at least an appearance of contracting for governmental functions. DOD has not dissuaded us from our conclusion that it has a serious problem in this area.

Second, DOD believes that we unjustly implied there was something wrong in contracting with former DOD employees. We agree that proper use of former employees can be advantageous to the Government. However, we became concerned about former DOD employees when their use is coupled with the high rate of unsolicited proposals and sole-source contracts. The extensive involvement of former employees raises questions about the degree of influence used by these former employees in securing contracts with DOD as well as lost in-house capabilities.

Third, DOD believes our findings are less valid now because of actions taken since the period covered by our review. At the time we selected contracts for review, which was in April 1980, the most recent and complete data available to us was for contracts awarded during fiscal year 1979. In that regard, we did examine modifications entered into as recent as early fiscal year 1981 for the contracts we selected. We admit there has been a strong

drive, starting with the issuance of our March 1980 report on contracting for consulting services, to control the use of consultants throughout the Federal Government. Your Subcommittees, in particular, have been in the forefront of this drive. There is no doubt that Federal managers are now more aware of significant problems in contracting for such services and are working toward correcting those problems. However, our report illustrates the problems in contracting for consultants services are not limited to consultants as defined by OMB, but are applicable to the much broader universe of management support services. Little action has been put into effect to correct the problems in this larger universe.

Finally, DOD disagrees with our recommendations. In essence, it believes actions already underway will correct the problems. We disagree. We believe the problems are bigger and more pervasive than DOD is willing to admit, and the strong actions recommended in our report are necessary to correct them.

Despite DOD's disagreements with our report, on Wednesday, March 4, 1981, the Secretary of Defense issued a news release announcing a reduction in the use of consultants and contract management services for fiscal years 1981-1986 which is expected to result in a \$550 million savings.

This concludes my prepared testimony. I would be pleased to respond to any questions you may have.

Attachments - 2



RESEARCH AND
ENGINEERING

THE UNDER SECRETARY OF DEFENSE
WASHINGTON, D.C. 20301

25 March 1981

Mr. W. H. Sheley, Jr.
Director, Procurement and Systems
Acquisition Division
U.S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Sheley:

This is in reply to your letter of January 14, 1981, to the Secretary of Defense regarding your report, The Department of Defense's Use of Management Support Services Needs Attention and Scrutiny, dated January 1981, OSD Case #5592, GAO Code 950601.

While we are in general agreement with the thrust of the Report's findings, having previously recognized the need to improve management controls and practices for management support services, we do not agree with several of the findings. These disagreements are discussed below. We are not in agreement with two of the recommendations. These are discussed starting on page 3 of this letter.

First, we do not agree that DoD is relying upon contractors to perform defense management functions of a government nature. We do contract for certain management support services, but, as your report states, the proper use of service contracts can be a normal, legitimate, and economical way to satisfy mission requirements. At the same time, it is our policy to ensure that service contracts will not be used in performing work of a policy/decision making or managerial nature, which is the direct responsibility of DoD officials. DoD Directive 4100.15, Commercial and Industrial Type Activities, and DoD Instruction 4100.33, Operation and Commercial and Industrial Type Activities, which are the implementing instructions for OMB Circular A-76, "Policies for Acquiring Commercial or Industrial Products and Services Needed by the Government," direct that governmental functions be performed by government personnel. We will watch this area to avoid abuses. However, we believe it is necessary to point out that the federal work force has changed in composition, technical skill, and characteristics over the last decade. As a result, we have lost certain kinds of in-house capability which we formerly

possessed. These losses are due in large measure to salary considerations, the fact that OMB Circular A-76 encourages contracting out and federal personnel hiring policies.

Second, there is a statement on page i of the GAO Report which says, referring to this contracting out of services by DoD, that "Much of the work is currently being performed by former DoD employees." This suggests by implication that something is wrong with this procedure. DoD Directive 5500.7, Standards of Conduct, in addition to citing the various statutory prohibitions that apply to DoD personnel conduct, states, among other things, that DoD personnel shall avoid any action that might result in or reasonably be expected to create the appearance of giving preferential treatment to any person or entity. It goes on to state that DoD personnel shall not knowingly deal on behalf of the government with present or former military or civilian government personnel whose participation in the transaction would be in violation of a statute, regulation, or policy set forth in the Directive. The Directive also includes a requirement that all DoD personnel shall be reminded, at least semi-annually, of their duty to comply with required standards of conduct. It should be noted, however, that former government personnel provide a source of expertise that should not be overlooked. These personnel often seek employment with firms to utilize their experience. It would be to the government's benefit to take advantage of their expertise as long as contracts are properly awarded and their responsibilities and conduct conform to statutory provisions and implementing regulations.

Third, the data contained and cited in the report is based on contracts awarded in FY 1979 (October 1978 through September 1979). Starting in early 1980, the Defense Department undertook, as described below, a series of actions to control these services and to assure that sound acquisition procedures and practices are followed. Thus the report's findings are less valid today as a result of our initiatives than they would have been had the report been published within a reasonable time after fiscal year 1979 when the data was collected. In September 1980, the Military Departments and Defense Agencies were directed to establish improved management controls over the acquisition process for consultant services, studies and analyses, and professional and management support. This direction resulted from OMB Circular A-120, Guidelines for the Use of Consulting Services, and a July 2, 1980, OMB letter governing Management Control of Consulting Service Contracts and Improvement of Agency Procurement Practices. We have expanded upon these OMB directives in our Departmental guidance of September 1980, a copy of which has been given to your staff previously, because we perceive that the

President and Congress are concerned not only about consulting services, but about studies and management support service contracts as well. In addition, the Defense Audit Service and the Army, Navy, and Air Force audit agencies have been instructed to evaluate the progress DoD components make in implementing effective controls over such contracts.

In addition, we are currently preparing a new DoD Directive on the Management of Studies to replace the currently existing one. A key feature of this new Directive is the establishment of a coordinator of DoD studies, whose primary function will be to serve as a focal point for studies in the Department, a source for the issuance of guidance concerning the management and control of studies, and a coordinator of activities related to studies use and management throughout the Defense Department.

Collectively, we believe these actions along with the development, starting in FY 1979, by the OSD (Comptroller) of the Special Exhibit (PB-21) entitled Special Analyses Consultants, Studies and Analysis, and Management Support Contracts, will further improve our management and control of studies and consulting service contracts. This document is used to support annual Defense budget submittals. It now breaks down costs among categories (which are defined) of Experts and Consultants; Studies and Analyses; Professional, Management and Services by Contract; and Contract Engineering Technical Services. Within each of the aforementioned categories, the format requires separate identification of "Consulting Services." Thus, this special analysis clearly portrays for management and Congress the budget costs for consulting and other services for the various Defense appropriations.

It has been this Department's contention that these categories constitute separate and distinct definable types of services and should not be grouped together as "Consulting Services" as is done by OMB, Congress, and on occasion by the GAO. We believe these categories must be clearly defined and their differences recognized by all interested parties. Without such agreement, the ability to account for, manage, control, count and be credible regarding the use and reporting of these services to everyone's satisfaction will be impossible.

In addition to our disagreement about several of the Report's findings, we disagree with two of the Report's recommendations. With respect to the two recommendations that Congress consider legislation (1) to minimize the funding of sole source contracts for management support services, and (2) extend the management controls outlined in

OMB Circular A-120 to other categories of management support services, we believe such legislation would be counterproductive and not cost effective. The improvement of controls over management support service contracts is the responsibility of the Executive Branch. It should have freedom to select the most promising approaches, and to make subsequent changes as may be found necessary, rather than be statutorily limited to specific approaches that in the long run might not prove to be in the government's best interest.

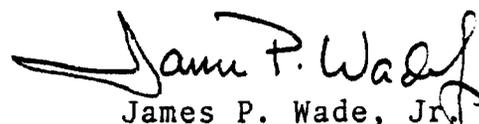
We are particularly opposed to that portion of the first recommendation addressed to Congress that suggests statutory imposition of competitive quotas for contract awards for services. The number of contracts and the number of purchasing offices would make such an approach impractical. Aside from the impracticality of the measure, it would reduce the present flexibility in Defense contracting and would interfere with the carrying out of Defense responsibilities. Despite tremendous effort, competitive quotas might not be reached resulting in postponement of necessary Defense contracts until the next year, adversely affecting our Defense posture and increasing costs.

The second recommendation addressed to Congress is unnecessary as we have already taken action to extend the management controls outlined in OMB Circular A-120 to other categories, i.e., studies and analyses and professional and management support. We have developed the PB-21 Special Exhibit discussed above to provide Congress the basis for exercising oversight of the funds involved for these services by appropriation account.

There are three recommendations addressed to the Secretary of Defense: (1) establish an independent review board; (2) evaluate all management support services in terms of future need and in-house capability; and, (3) identify functions currently being performed by contractors which are governmental in nature. We believe our direction to the Military Departments and Defense Agencies previously noted covers the thrust and intent of these recommendations.

The opportunity to comment on your report is appreciated.

Sincerely,


James P. Wade, Jr.
Acting

GAO COMMENTS ON DOD RESPONSE TO GAO REPORT TITLED
CONTROLS OVER DOD'S MANAGEMENT SUPPORT SERVICE CONTRACTS
NEEDS STRENGTHENING (MASAD-81-19 dated 3/31/81)

GAO was unable to include DOD written comments in our report because they were received 42 days after our comment period closed. By the time they were received, the report was signed and printing had started. In general, DOD agrees with the thrust of our report. However, DOD disagrees with several findings and with our recommendations.

DOD does not agree with our finding that DOD is relying upon contractors to perform defense management functions of a governmental nature. DOD argues that it is their policy not to rely on contractors for such services. In support of this position, DOD identified two policy pronouncements which direct that governmental functions be performed by government personnel. However, DOD goes on to acknowledge that they have lost certain in-house capabilities which they formerly possessed. DOD cites three reasons for this loss, all apparently outside of DOD's control: salary considerations, contracting out encouraged by A-76, and federal hiring policies. We recognize that contracting for services of a defense management function is contrary to DOD policy. Our report, however, has demonstrated that the existence of these policy pronouncements did not preclude contracting for such services.

Secondly, DOD takes exception to our highlighting that much of the work contracted for was performed by former DOD employees. Again, DOD cites policy directives which are intended to ensure

compliance with the statutory prohibitions that apply to DOD personnel in the avoidance of preferential treatment to any person or entity. DOD feels that expertise held by former DOD employees should not be overlooked. We agree that the proper use of this expertise can be advantageous to the Government. However, we are concerned about the extensive reliance on former DOD employees when their use is coupled with the high rate of unsolicited proposals and sole-source contracts. The extensive involvement of former DOD employees raises questions about the degree of influence used by former employees in securing contracts within DOD as well as DOD's lost in-house capability.

The third point raised by DOD deals with the validity of our findings. DOD feels that, because of their corrective actions during 1980, the report findings are less valid. In April 1980, when we selected contracts for review, the most recent and reliable data available to us was for fiscal year 1979. However, in addition to the period covered by our review, our coverage included some 735 modifications to these contracts extending through early fiscal year 1981. Thus, some effect of these corrective actions was evident to us and did not convince us that the use of fiscal year 1979 data was inappropriate.

Regarding DOD's corrective actions, DOD cites a September 1980 direction to Military Departments and Defense agencies to establish improved management controls over consulting and management support services. DOD admits that this direction is the result of OMB actions, and Presidential and Congressional concerns about management support services. The timing of DOD's action to establish improved

management and controls prevented us from evaluating the impact of any improvements in DOD's use of management support services. Considering DOD's past slow responsiveness to Congressional and OMB direction on consulting services, we have serious doubts about when any actual improvement in management and controls over management support services will be realized.

DOD further disagrees with any effort to group the three distinct definable types of services in our universe, consulting services, management and professional services by contract, and management and support services under Research, Development Test and Evaluation. We have not attempted to remove the distinctions which exist among these types of services. However, our review clearly indicates that the same abuses associated with consulting services exist in the broader universe of management support services. We believe that any effort to control the abuses of and exercise oversight over consulting services should be applied to management support services as well.

In general, DOD takes exception with most of our recommendations. Concerning our legislative recommendation to restrict the funding of sole-source procurements for management support services, DOD states that it is impractical and inflexible and that it will interfere with carrying out their Defense related responsibilities. We believe DOD's flexibility argument misses the point. It is DOD's inability to administratively correct the longstanding problem with sole-source procurements that has prompted our recommendation to restrict funding for sole-source

procurements. Secondly, the GAO recommendation fully recognizes that provision must be made for those cases where a sole-source procurement is necessary to the national defense.

DOD, also, did not agree with the legislative proposal in our draft report to extend the management controls of A-120 to all management support services. Their basis for this is their belief that it is the Executive Branch's responsibility to improve the controls over management support services. We believe that the planned OMB action, if carried out as intended, to extend the management controls of A-120 to all management support services, will accomplish the same thing as our draft proposal to Congress. Accordingly, we have readdressed this proposal as a recommendation to OMB in our final report.

DOD feels that our recommendation calling for budgetary identification for funds used for management support services is unnecessary because it provides the desired information in an existing exhibit. We feel that this exhibit is a good first step that does not go far enough because it only provides planned expenditures by appropriation account. More information is needed in order to provide the Congress with sufficient information to enable them to exercise effective oversight and control. However, two recent OMB actions, if combined and properly implemented, can accomplish the intent of our recommendation relating to budgetary identification. In January 1981, in its Bulletin 81-8 OMB acknowledged in effect, that the problems which exist in consulting services also

exists in the broader universe of management support services. If the basic thrust of Bulletin 81-8 is combined with OMB Bulletin 80-13, which directs Executive departments and agencies to submit budgetary estimates and related information on planned consulting services, then OMB would have the information we believe should be provided to Congress.

In our draft report, we addressed three proposals to the Secretary of Defense. They called for (1) the establishment of an independent review board to assure the highest level review of proposed contracts for management support services, (2) identify functions being performed by contractors which are governmental in nature and be prepared to bring them in-house, and (3) identify management support services which are not governmental in nature and required on a continuing basis and assess these services in terms of long term need and least costly alternative.

DOD feels that the direction provided to the Military Departments and Defense Agencies to establish improved management and controls over consulting and management support services, covers the thrust and intent of these proposals. We disagree. We believe the problems identified in our report are more severe than DOD is willing to admit. The DOD directions, in our opinion, lack the specificity to resolve the cited problems and require the type of attention addressed in our proposals. We therefore made firm recommendations in our final report.