




U.S. GENERAL SERVICES ADMINISTRATION  
Office of Inspector General

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MEMORANDUM FOR: Steven J. Kempf  
Commissioner, Federal Acquisition Service (Q)

FROM:   
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SUBJECT: Major Issues from Fiscal Year 2010  
Multiple Award Schedule Preaward Audits

To assist GSA in managing its Schedules Program, we are providing this rollup memorandum on three recurring issues we identified while conducting our fiscal year (FY) 2010 preaward contract audits.

- The majority of vendors we reviewed provided information that was not current, accurate, and/or complete to support their proposed prices.
- Nearly half of the vendors we reviewed had minimal or no non-federal commercial customers, making it impossible to use non-governmental commercial sales as a basis for determining price reasonableness under the GSA Schedules Program.<sup>1</sup>
- Over a quarter of the vendors we reviewed supplied labor that did not meet the minimum educational or experience qualifications required by the contracts.

While we audited a limited number of the contracts in GSA's Schedules Program, the high rates at which these three issues recur suggest that similar concerns would be uncovered in a comprehensive, program-wide audit. Therefore, we are providing you this information so that GSA can decide how to best address them. Below we discuss each of these issues in more detail.

### **Background**

Under GSA's Schedules Program, the Federal Acquisition Service (FAS) establishes long-term government-wide contracts with commercial vendors. Through these contracts, over 11 million commercial products and services are made available to customer agencies at volume discount pricing. In FY 2010, GSA Schedules Program sales exceeded \$38 billion.

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<sup>1</sup> The terms "commercial sales" and "commercial marketplace" as used throughout this memorandum refer to non-governmental sales and customers.



Per Federal Acquisition Regulation 8.404, the prices of products and services available for purchase from the Schedules Program are considered to be fair and reasonable. Thus, GSA contracting officers (COs) are tasked with evaluating price reasonableness by performing steps such as the following:

- Ensuring that the proposed prices are comparable to prices offered to commercial customers;
- Conducting other analyses, such as evaluating cost build-up<sup>2</sup> in the absence of comparable commercial sales; and
- Requiring that the vendor reduce the prices offered to the Government if the prices granted to the basis of award customer<sup>3</sup> are reduced during the contract period.

The GSA Office of Inspector General (OIG) conducts preaward audits to assist COs in negotiating MAS contracts. These audits provide COs with information regarding whether vendor-supplied commercial sales practices (CSP) information is current, accurate, and complete prior to awarding the contract or exercising an option to extend the contract.

During FY 2010, the OIG performed 49 Multiple Award Schedule (MAS) preaward contract audits. The subject contracts had estimated sales of over \$8 billion for their pending 5-year option periods. As a result of these audits, we informed GSA COs of numerous contract deficiencies. We also recommended price and discount adjustments that, if realized, would allow for over \$423 million in cost avoidances for customer agencies and, ultimately, the taxpayer. Additionally, we recommended over \$3 million in recoverable overcharges related to misclassified labor.

### **Commercial Sales Practices Disclosures Are Not Current, Accurate, and/or Complete**

The majority of vendors we reviewed provided COs with flawed CSP information. This adversely affects both (1) the initial price reasonableness determination for the proposed contract prices and (2) the Government's discount structure/pricing relationship with the basis of award customer over the life of the contract.

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<sup>2</sup> Conducting a cost build-up analysis of a service contract generally involves verifying the accuracy of proposed labor rates by obtaining additional information such as payroll stubs, financial statements, and expense reports. A multi-tiered process is used to compute a fully-loaded labor rate for each labor category, which includes verifying base labor rates and determining the allocability of other direct and indirect costs.

<sup>3</sup> Under the Price Reductions clause, the vendor's discount relationship with the basis of award customer or category of customers is generally used as the basis for the discounts given to the Government. If the discounts given to these customers increase, the discounts given to the Government also increase.

The preferred method COs use to determine price reasonableness is to compare proposed prices to those the vendors charge in the commercial marketplace. The commercial marketplace should compel vendors to offer reasonable prices in order to remain competitive. Accordingly, the General Services Administration Acquisition Manual Part 515.408(2) requires vendors to submit their CSP as part of their offer. The CSP should contain information demonstrating that the proposed discount structure or pricing is reasonable in relation to the vendor's commercial discounts/pricing. As part of the CSP, the vendor must provide detailed information on those customers or categories of customers that receive pricing equal to or better than that offered to the Government.

We audited 24 option proposals that were based on commercial pricing (i.e., cost buildup information was not analyzed). In 20 cases (83 percent), the CSPs reflected non-current, inaccurate, and/or incomplete pricing information. We found that some vendors granted other customers more favorable discounts or terms than were disclosed on their CSPs. In one instance, a vendor disclosed a standard discount of 0 percent; however, we determined that the vendor routinely granted "non-standard" discounts. In fact, we sampled \$59.5 million of transactions and 99 percent of the time, customers received a discount greater than 0 percent. Situations similar to this adversely affect MAS contract pricing.

If the greater discounts and terms identified through our preaward audits in these 20 contracts could be negotiated, the Government would realize overall cost avoidances of \$116.5 million during the contracts' 5-year option periods. These savings represent the difference between the offered discounts and those we calculated using current, accurate, and complete CSP information.

We believe FAS should take action to ensure that GSA COs appropriately and consistently evaluate discount information. This evaluation should include consideration of the difference between "standard" and "non-standard" discounts, the frequency and range of discounts, and the impact of rebates.

### **No Commercial Sales**

Our preaward audits also disclosed that many MAS vendors have minimal or no commercial sales to non-federal customers. For 21 of the 49 vendors audited (43 percent), commercial customers accounted for 5 percent or less of the vendor's total sales. In 12 instances, the vendor had no commercial sales. This includes both vendors who sell items with no commercial application and vendors who sell commercial items solely to the Government. For example, in one FY 2010 audit, a vendor disclosed that its Schedule offerings "do not by definition have a commercial application" and its proposed rates "were developed solely for the use on task orders under our Schedule." In another instance, a large professional services vendor with more than \$1 billion in estimated contract period sales had no commercial sales for any of the labor categories offered on its GSA Schedule.

GSA's stated goal is "to obtain the offeror's best price (the best price given to the most favored customer)." If there are no commercial sales to non-federal customers or federal agencies under a non-MAS contract, this goal cannot be met. Although the FAR provides for other methods of price analysis (e.g., comparison to prices offered by others, market analysis, vendor cost buildup data) these approaches will not achieve GSA's stated goal of obtaining the best price given to the most favored customer.

In addition, if there are no rate comparisons with commercial sales, it may not be possible to identify a basis of award customer; therefore, the Government has no foundation for implementing price reductions. Without a basis of award customer, GSA Schedule customers cannot be assured that they will be aware of and benefit from pricing changes in the marketplace. This is particularly true in the information technology market, where costs tend to decrease dramatically as technology ages. As a vendor's costs decline over the contract period, its profit margin will increase, but without price reductions, the Government will be unable to share in these savings. Allowing vendors to remain on GSA Schedule with minimal or no commercial sales to non-MAS customers creates the potential for Schedules Program users to pay significantly higher prices than warranted.

If FAS continues to allow vendors such as these to be on Schedule, FAS should take appropriate steps to ensure that GSA Schedule prices meet the stated goal of being the vendor's best price and that there is an effective mechanism for price reductions.

### **Unqualified Labor**

Finally, our preaward audits disclosed that GSA customers were overcharged approximately \$3 million for professional services which did not meet the minimum educational and/or experience qualifications proposed by the vendor and required in their contracts.

MAS vendors that provide services must submit labor category descriptions and their associated wage rates as part of their offers. These descriptions include the minimum qualifications (e.g., level of education and experience) for each proposed labor category. This ensures that customer agencies are provided individuals who have the skill sets required to meet the agencies' needs. The billable rates for each category are based on these qualifications.

As part of our audits of service contracts, we evaluate employee resumes to determine whether the employees possess the requisite qualifications for their billable labor categories. In the 37 services contracts we audited, we found 10 instances in which vendors charged customer agencies for labor that did not meet the minimum labor category qualifications called for by the contract. In one audit, 75 percent of the employees in our sample did not fully meet the qualifications for the labor category under which the employee was billed. In another case, approximately 24 percent of the personnel assigned to GSA task orders did not meet the standards stipulated by the contract. In fact, this same vendor was cited in a FY 2009 GSA OIG audit as providing

unqualified labor on a different MAS contract and the Defense Contract Audit Agency reported similar findings in a FY 2007 review. In these situations, we are not challenging the labor rates themselves; however, we are questioning whether customer agencies paid for higher levels of service than they received.

We believe that COs may not realize the extent or potential ramifications of this problem. We suggest that FAS take appropriate action to ensure that vendors are providing GSA and ordering agencies with individuals who have the labor qualifications for which the agencies are paying.

### **Conclusion**

The Schedules Program, with over \$38 billion in FY 2010 sales, is the largest interagency contracting vehicle. The goal of the Schedules Program is to use commercial terms and conditions and leverage the Government's volume buying to obtain the best possible prices and terms for customers and taxpayers, which is consistent with the goal of reduced federal spending. We believe that addressing the issues raised in this memorandum will help improve the effectiveness of the Schedules Program.