



U.S. Department of Energy
Office of Inspector General
Office of Audits and Inspections

AUDIT REPORT

Management and Oversight of Information
Technology Contracts at the Department of
Energy's Hanford Site

DOE-OIG-16-10

April 2016



Department of Energy
Washington, DC 20585

April 1, 2016

MEMORANDUM FOR THE SECRETARY

FROM:

A handwritten signature in blue ink, appearing to read "Rickey R. Hass".

Rickey R. Hass
Acting Inspector General

SUBJECT:

INFORMATION: Audit Report on the “Management and Oversight of Information Technology Contracts at the Department of Energy’s Hanford Site”

BACKGROUND

The Department of Energy’s Hanford Site (Hanford) supported the Manhattan Project and Cold War through the production of plutonium. The weapons production processes resulted in the creation of solid and liquid wastes that posed a risk to the local environment. To help remediate the environmental risks, the Richland Operations Office and the Office of River Protection oversee the cleanup work completed by seven prime contractors. The Richland Operations Office designed Hanford’s Mission Support Contract to provide integrated infrastructure services to the prime contractors performing the cleanup mission. A portion of the contract’s scope included information technology (IT) support services related to application hosting services, support for hardware and software, network management, and desktop/user services. In 2009, the Richland Operations Office awarded the \$3 billion Mission Support Contract to Mission Support Alliance, LLC (MSA), a joint venture that included Lockheed Martin as the principal partner. MSA noncompetitively awarded a subcontract for IT support services to its affiliate, Lockheed Martin Services, Inc. (LMSI), valued at an estimated \$232 million over approximately 5 years starting in January 2010.

The Office of Inspector General received a complaint expressing concerns with the Department’s oversight of IT functions at Hanford. The complaint alleged, among other things, that MSA’s request to subcontract to LMSI had not been formally approved and that LMSI had refused to provide a breakdown of costs. The complainant further alleged that LMSI was likely receiving unallowable affiliate profit. Shortly after the audit began, Richland Operations Office officials stated that they had similar concerns regarding unallowable fee or profit and had made attempts to resolve the issue. The complaint also alleged a potential conflict of interest between MSA and LMSI. To that end, we initiated this audit to determine whether IT contracts and activities at Hanford were effectively managed.

RESULTS OF AUDIT

Our review largely substantiated that there were a number of problems related to the management and oversight of the IT contracts at Hanford. While we did not substantiate the

allegation regarding a conflict of interest, we determined that several MSA executives also held senior executive positions within Lockheed Martin Corporation and, as such, had inappropriately taken actions on excluded activities that resulted in the appearance of a conflict of interest. We identified weaknesses related to contract awards and work scope, time and material task orders, and affiliate fee or profit. In particular, we found that:

- Although the Richland Operations Office intended the Mission Support Contract to consolidate all infrastructure services for Hanford's cleanup mission under one prime contract, some of the site's major prime contractors entered into separate agreements with LMSI to perform services that had been included in the scope of the original MSA contract. For instance, contrary to the defined scope of work in the Mission Support Contract, MSA entered into a separate subcontract with LMSI to provide services to CH2M Hill Plateau Remediation Company. Similarly, Washington River Protection Solutions entered into two separate subcontracts to obtain services directly from LMSI. Although required to do so, MSA and Washington River Protection Solutions did not request consent from Federal officials on these subcontracts, an action that would have given the Department visibility into the additional cost of providing IT support services at the Hanford Site. Ultimately, MSA's actions in this case adversely affected the Department's ability to oversee services included under these subcontracts, activities that cost the Government more than \$114 million.
- Time and materials task orders significantly exceeded the amount proposed in the support contract with LMSI. When requesting consent from the Richland Operations Office on the LMSI subcontract, MSA indicated that time and materials task orders would only cover services not expected to be performed regularly, if at all, and estimated that such task orders would account for less than 12 percent of the total work for fiscal year 2011 and beyond. However, we found that the actual value of time and materials task orders exceeded \$120 million and accounted for nearly 50 percent of the cost of work performed as of October 2014. Federal regulations generally discourage overuse of time and materials contracts because such arrangements provide little incentive to control costs.
- The Department may have paid unnecessary fee or profit when acquiring IT support services. Specifically, we identified potential unallowable profit of more than \$63.5 million. We determined this amount by comparing the costs incurred by LMSI from January 2010 through December 2014 to the actual amounts reimbursed to LMSI by various Hanford site prime contractors. Even though Federal Acquisition Regulation required that all noncommercial goods and services sold or transferred between affiliates were not subject to additional fee or profit, our analysis identified that profit appeared to have been included in rates charged by LMSI. Prior to contract award, the Department's contracting officer determined that the IT services provided through the Mission Support Contract were not commercial. According to Richland Operations Office officials, paying fee or profit for subcontracted work performed by LMSI amounted to both Lockheed Martin controlled organizations (MSA and LMSI) receiving fee or profit for the same work. Federal officials also told us that paying LMSI fee or profit for such work resulted in payments that amounted to total markups on LMSI's subcontracts in

excess of its costs ranging from 1 to almost 7,000 percent. MSA disagreed with the Department's findings on the LMSI subcontract. At the time this report was issued, the Department and MSA were engaged in the resolution process to address the issue.

The identified weaknesses occurred, at least in part, because MSA had not fully executed the Mission Support Contract in accordance with its terms. Richland Operations Office officials told us that excessive costs occurred because MSA ignored Federal direction that LMSI services should be treated as not commercial in nature and, as such, were to be provided at cost. While we did not find that the Richland Operations Office had wavered in its determination regarding the LMSI subcontract's commerciality, we noted that it had not conducted all contract management activities that were required for this type of contract to ensure that costs incurred were appropriate and transparent to the Department. In addition, the Richland Operations Office had not promptly acted to compel involved contractors to comply with requirements. We also observed that Richland Operations Office and MSA officials had not ensured that incurred cost audits were conducted in accordance with Federal requirements, a key component of an effective monitoring and oversight program.

In light of the issues identified, the Department may have awarded a contract that was not in the best interest of the Government. Specifically, the Department may have inappropriately paid up to \$63.5 million in affiliate fee or profit. In addition, we questioned \$120 million in time and materials costs pending resolution through incurred cost audits. As a result, we made several recommendations that, if fully implemented, should improve the management and oversight of IT contracts at Hanford and ensure activities are carried out in accordance with Federal regulations.

MANAGEMENT RESPONSE

Management concurred with the recommendations and indicated that corrective actions had been initiated or were planned to address the issues identified in the report. For example, the contracting officer has issued a decision disallowing more than \$63 million of affiliate fees or profits paid to MSA. At the time of this report, the Department and MSA were in the resolution process for the disallowed costs. Management's comments and our responses are summarized in the body of the report. Management's formal comments are included in their entirety in Appendix 3.

Attachments

cc: Deputy Secretary
Deputy Under Secretary for Management and Performance
Assistant Secretary for Environmental Management
Chief of Staff
Chief Financial Officer

MANAGEMENT AND OVERSIGHT OF INFORMATION TECHNOLOGY CONTRACTS AT THE DEPARTMENT OF ENERGY'S HANFORD SITE

TABLE OF CONTENTS

Audit Report

Details of Finding	1
Recommendations.....	9
Management Response and Auditor Comments.....	10

Appendices

1. Objective, Scope, and Methodology	11
2. Prior Reports	13
3. Management Comments	14

MANAGEMENT AND OVERSIGHT OF INFORMATION TECHNOLOGY CONTRACTS AT THE DEPARTMENT OF ENERGY'S HANFORD SITE

DETAILS OF FINDING

In 2009, the Richland Operations Office awarded Mission Support Alliance, LLC (MSA), the Hanford Mission Support Contract to provide support services to the Department of Energy (Department) and its contractors. As part of this contract, MSA subcontracted the information technology (IT) support services work to its affiliate, Lockheed Martin Services, Inc. (LMSI). The subcontract was valued at \$232 million over approximately 5 years. The Office of Inspector General received a complaint related to the performance and management of the subcontract awarded to LMSI. The complaint alleged that MSA's consent to subcontract with LMSI had not been formally approved and that LMSI had refused to provide a breakdown of costs. The complainant further alleged that LMSI was likely receiving inappropriate affiliate profit. The complaint also alleged a potential conflict of interest between MSA and LMSI.

We substantiated the allegations related to the LMSI subcontract's lack of approval and the Department's lack of visibility into the costs associated with IT support services. We also substantiated the allegation that LMSI may have inappropriately received affiliate profit. We found that the Richland Operations Office had only provided conditional consent for the LMSI subcontract. The officials that granted the conditional consent informed us that MSA had not met all of the conditions for it to be considered effective, including enforcing audit requirements and providing sufficient visibility to determine that affiliate fees were not paid. However, MSA officials told us that the question of whether it met all the conditions for the consent to be effective is before the Civilian Board of Contract Appeals. In addition, although the Richland Operations Office intended the Mission Support Contract to consolidate all infrastructure support services, several additional subcontracts valued at more than \$114 million were awarded to perform previously contracted work without required approval from the Department. Furthermore, despite MSA's original assertion that time and materials (T&M) task orders would only account for a small portion of the work, they significantly exceeded the amount proposed in MSA's contract with LMSI even though they provide no incentive for the contractor to control costs or labor efficiency. The Department also may have paid unnecessary fee or profit of at least \$63.5 million when acquiring Hanford's IT support services.

We did not substantiate the allegation regarding a conflict of interest between MSA and LMSI. However, we did determine that several executives within MSA also held senior executive positions within Lockheed Martin Corporation and, as such, had inappropriately taken actions on excluded activities.

Contract Awards and Work Scope

Although the Mission Support Contract was intended to consolidate all infrastructure support services needed to support Hanford's cleanup mission under one prime contract, including those related to IT, we found that additional subcontracts had been awarded for services required to be provided through the Mission Support Contract. As a result, the cost to provide IT support services to Hanford's contractors was significantly more than envisioned when the contract was awarded. Specifically, we found that:

-
- MSA awarded a separate subcontract to LMSI to provide IT support services to CH2M Hill Plateau Remediation Company (CHPRC). The subcontract had an estimated value of \$70 million, \$50 million of which had been invoiced as of October 2014. Upon issuance of this subcontract, MSA did not adjust the amount of its existing subcontract with LMSI to ensure that costs did not exceed the \$232 million estimate. This action effectively added to the value of the Mission Support Contract.
 - Although included in the scope of the original Mission Support Contract, Washington River Protection Solutions (WRPS) paid LMSI \$65 million under four separate subcontracts for IT support services. Specifically, WRPS awarded LMSI two subcontracts in August 2012. As of November 2014, expenditures on these two subcontracts totaled approximately \$24 million. Furthermore, WRPS also continued to obtain services directly from LMSI under two other subcontracts that were issued in September 2002 by its predecessor. LMSI was paid approximately \$41 million on these two subcontracts after the Mission Support Contract was effective.

Although required to do so, MSA and WRPS did not request consent from Federal officials on these subcontracts, an action that would have given the Department visibility into the additional cost of providing IT support services at the Hanford Site. Ultimately, MSA's actions in this case reduced Federal officials' awareness of additional IT support service contracts and adversely affected the Department's ability to oversee services included under these subcontracts, activities that cost the Government more than \$114 million.

Time and Materials Task Orders

Even though T&M contracts provide no incentive for the contractor to control costs or labor efficiency and are prohibited by Federal regulations except in specific circumstances, MSA's use of such task orders significantly exceeded the amount proposed in its contract with LMSI for routine support services. T&M contracts allow the contractor to be reimbursed based on direct labor hours at specified fixed hourly rates and actual costs for materials. The Federal Acquisition Regulation (FAR) directed that T&M contracts only be used when it is not possible to accurately estimate the extent or duration of work or to anticipate costs with any reasonable degree of confidence. Although MSA believed that this did not put any restrictions on its use of T&M purchases, its proposal stated that T&M task orders would cover services not expected to be performed regularly, if at all. It estimated that T&M would total about \$46 million throughout the initial period of performance and would account for less than 12 percent of the total work performed in fiscal year 2011 and beyond. Despite these estimates, we determined that the value of T&M task orders exceeded \$120 million as of October 2014, nearly 50 percent of the costs of the work performed to date.

Although MSA officials told us that the increase was likely due to funding received from the *American Recovery and Reinvestment Act of 2009* (Recovery Act), we noted that LMSI's contract had already considered the increase in demand from the Recovery Act. In addition, T&M task orders continued to exceed anticipated levels for more than 2 years after Hanford's Recovery Act funding ended. For example, during fiscal years 2013 and 2014, T&M task orders accounted for approximately 40 percent of the overall costs incurred on the subcontract.

In addition to the significant growth in T&M costs, we identified numerous instances of potentially unallowable costs claimed by LMSI in its T&M task order invoices. For instance, a review of a limited subset of invoices for various task orders covering several years found that:

- Several invoices did not contain adequate support for the materials being reimbursed. One invoice in the amount of \$31,097 for network equipment did not include any supporting documentation from the vendor indicating what was purchased and received. Additional invoices for equipment rentals totaling \$9,605 were only supported by an internally generated spreadsheet and did not include vendor support. In one case, the charges submitted on the file from one month to the next were identical, with no date or identifying information to confirm that these were new charges.
- In certain instances, work invoiced was outside the scope of a particular task order. The work scope for one task order was limited to ad-hoc media services (such as photography services for recognition events or organization photos, general video production and streaming media support, presentation development, and event planning and coordination). However, the supporting documentation submitted with the invoice was for conference room and audio/visual room modifications totaling approximately \$11,000.
- Numerous invoices contained questionable costs, totaling approximately \$1,400, related to MSA's family picnic expenses. When we inquired whether these expenses were included in the statement of work, MSA officials responded that they were unallowable and would be credited to the Department.

Finally, task orders to provide software to Hanford contractors were not appropriately implemented. Although the task orders were written as firm fixed unit rate tasks, the rates were frequently adjusted to reflect LMSI's actual costs. The FAR encouraged using fixed rate contracting because it places responsibility on the contractor to control its costs. If the contractor can perform for less than the contracted rate, it realizes profit from its efficiencies; if not, it must absorb the loss. However, by frequently adjusting its software licensing rates to account for higher costs, MSA subverted the purpose of fixed rate contracting and effectively treated the task orders as cost reimbursable. Because of the inappropriate management of the task orders, we question approximately \$313,000 incurred in fiscal years 2013 and 2014.

Affiliate Fee or Profit

The Department may have paid unnecessary fee or profit for Hanford's IT support services. Prior to award, the contracting officer determined that the IT services provided through the Mission Support Contract were not commercial. Based on our reading of the FAR, the contracting officer is ultimately responsible for such determinations. Therefore, we did not specifically evaluate the services provided by LMSI to determine the subcontract's commerciality. However, we compared January 2010 through December 2014 costs incurred by

and reimbursed to LMSI through various contracts for IT support services. Contrary to FAR requirements related to affiliate arrangements,¹ we identified potentially unallowable profit of more than \$63.5 million, as detailed in the following chart.

CALENDAR YEAR	AMOUNT INVOICED	COSTS INCURRED	CALCULATED PROFIT
2010	\$62,489,586	\$58,744,285	\$3,745,301
2011	78,844,916	54,152,264	24,692,652
2012	59,278,770	42,045,310	17,233,460
2013	56,923,107	47,792,011	9,131,096
2014	56,703,072	48,003,925	8,699,147
TOTALS	\$314,239,451	\$250,737,795	\$63,501,656

Despite our requests, LMSI was unable to provide evidence that fixed unit and labor rates did not include unallowable fee or profit. In preliminary comments on our draft report, management was concerned that we had not included costs charged by LMSI to MSA's predecessor in our analysis. We determined, however, that the predecessor's subcontract with LMSI was not an affiliate contract and, based on the FAR, was entitled to earn fee or profit. Therefore, it would not have been appropriate to include these amounts in our analysis.

According to Richland Operations Office officials, paying fee or profit for subcontracted work performed by LMSI amounted to MSA and LMSI receiving fee or profit for the same work. Federal officials also told us that MSA and WRPS paying LMSI fee or profit for such work resulted in total markups on LMSI's subcontracts in excess of its costs ranging from 1 to almost 7,000 percent. We are concerned that the Department may have reimbursed LMSI significant amounts of fee or profit for work that was required to be performed through the Mission Support Contract even though pre-award documentation indicated that it was not allowable. In response to a draft copy of this report, the Richland Operations Office informed MSA that it intended to disallow payments made to LMSI in excess of its incurred costs. MSA disagreed with the Department's findings on the LMSI subcontract and, at the time this report was issued, was engaged in the resolution process before the Civilian Board of Contract Appeals regarding those findings.

Contract Execution, Management, and Monitoring and Oversight

The issues identified occurred because MSA and WRPS had not fully executed the terms of their respective contracts, which required that several of the Hanford prime contractors receive IT support services through the Mission Support Contract. In addition, issues related to due diligence and an ongoing dispute over the commerciality of the LMSI subcontract affected the Department's ability to manage its IT support service contracts at the Hanford site. Furthermore, Richland Operations Office and MSA officials did not provide effective monitoring and oversight to ensure that costs incurred by LMSI were appropriate and transparent to the Department.

¹ FAR 31.205-26(e) requires that all goods and services sold or transferred between affiliates under a common control on a noncommercial basis not be subject to additional fee or profit.

Contract Execution

MSA and WRPS did not fully execute the terms of their prime contracts. Specifically, MSA was required to provide IT support services to many of Hanford's prime contractors through the Mission Support Contract. This requirement was incorporated into all of the site's prime contracts. Despite this, MSA issued an additional subcontract to LMSI for services provided to CHPRC, claiming the need to segregate costs. Likewise, WRPS acted against the requirements of its contract by issuing separate subcontracts for work covered by the Mission Support Contract. Overall, these actions resulted in additional subcontracts for work that had already been awarded to LMSI through the Mission Support Contract. While WRPS officials believed that MSA authorized WRPS to directly enter into the subcontracts with LMSI, we noted that the contract between WRPS and the Department required WRPS to obtain IT services from MSA, not LMSI. Therefore, we concluded that the WRPS scope of work should have been performed by MSA and was subject to the same terms as the rest of the Mission Support Contract, including the prohibition to earn profit or fee.

In addition, based on discussions with the cognizant Federal contracting officers, we determined that MSA had not requested the Department's approval of the \$70 million subcontract to support CHPRC even though the FAR required Federal consent on certain procurement actions. The Department also required approval on any agreements between MSA and its affiliate that were valued at over \$1 million. Similarly, WRPS had not requested consent from the Office of River Protection—the Federal office responsible for overseeing its contract with the Department—for any of its four subcontracts with LMSI.

Contract Management

While we did not find that the Richland Operations Office had wavered in its determination regarding the LMSI subcontract's commerciality, we noted that it had not conducted all the contract management activities necessary to ensure that costs incurred were appropriate and transparent to the Department. The FAR required that the contracting officer give "particularly careful and thorough consideration" to contracts issued by affiliated parties. The contracting officer was required to obtain certified cost and pricing data for noncommercial items to determine fair and reasonable pricing before the contract was awarded. Despite this requirement and the relationship between MSA and LMSI, the Richland Operations Office did not require MSA to submit certified cost and pricing data prior to award of the LMSI subcontract. Such action would have given the Richland Operations Office visibility into the subcontract to identify any unallowable fee or profit. Richland Operations Office contracting officials stated that they believed the conditions for consent would provide enough insight into LMSI's costs to determine whether the Department was receiving services at cost. However, because of the ongoing disagreement over commerciality, the Richland Operations Office did not achieve the anticipated level of visibility for LMSI activities. In addition, Richland Operations Office officials stated that a sole source justification was not necessary because LMSI was a preselected subcontractor in MSA's teaming arrangement. However, the FAR stated that such arrangements did not limit the Government's right to pursue its policies on competitive contracting. Because of the affiliate

relationship between MSA and LMSI, we concluded that the Richland Operations Office's actions did not constitute careful and thorough consideration of the subcontract as required by FAR.

We also found that an ongoing dispute over the LMSI subcontract's commerciality affected the Department's ability to successfully manage IT contracts. Early in the contracting process, the Richland Operations Office determined that the services provided by MSA's affiliate were noncommercial in nature. Even though MSA's consent request for the primary LMSI subcontract included terms stating the contract was commercial, Richland Operations Office officials stated that they believed MSA would provide the information needed to ensure that unallowable fee or profit was not incurred when the conditions of consent were fully met. Richland Operations Office management responded to our preliminary report that it had no legal duty to continue communicating its commerciality determination and, ultimately, the dispute remained unresolved throughout the contract's period of performance.

Monitoring and Oversight

Despite the significant increase in costs, Federal officials did not provide adequate oversight related to T&M costs. The FAR notes that appropriate Federal oversight of contractor performance is necessary to reasonably assure that contractors use efficient methods and effective cost controls when using T&M contracts. However, Richland Operations Office contracting officials stated that they did not have contracting purview over MSA's subcontractors and had not been provided access to the data and records that would be needed to conduct effective monitoring activities. Although the Richland Operations Office had options available to encourage MSA to properly monitor the LMSI subcontract, such as deducting or reducing fee, we found that it had not attempted to exercise these options to require incurred cost audits until December 2013. If applied earlier, such actions could have helped ensure that costs to the Department were reasonable.

In addition, MSA did not implement required subcontract monitoring activities. LMSI's subcontract required incurred cost audits; however, MSA did not perform the audits, or arrange for them to be performed, despite multiple requests from Richland Operations Office officials that the audits be conducted. As noted in our special report on *Incurred Cost Audit Coverage of Non-Management and Operating Contractors* (DOE/IG-0934, February 2015), timely contract audits are an essential management tool. Because MSA did not ensure incurred cost audits were performed in a timely manner, the Department's ability to question the growth in T&M costs was severely restricted. In addition, because of statute of limitations requirements,² significant delays in performing incurred cost audits could affect the Richland Operations Office's ability to recover unallowable contractor incurred costs.

According to MSA officials, LMSI refused to provide access to its records, preventing them from performing required subcontract audits. MSA officials informed us that, although they could not gain access to perform cost incurred audits of LMSI, they did conduct invoice reviews. We acknowledge that such reviews are an important component of a strong internal control

² The *Federal Acquisition Streamlining Act of 1994* established a 6-year statute of limitations for claims filed under the *Contracts Dispute Act of 1978*.

system, but they do not supersede the need for required incurred cost audits, as evidenced by the anomalies we identified during our limited invoice review. Furthermore, MSA asserted that because LMSI would not provide access to its records, the responsibility for performing cost incurred audits was elevated to the Department. However, we did not find this argument to be persuasive because *Department of Energy Acquisition Regulations* required that the prime contractor either conduct the audit or arrange for one to be performed.

Another factor that likely affected the monitoring and oversight of the contract was a dispute regarding the commerciality of the LMSI subcontract. The commerciality of the subcontract had been disputed by MSA since it was issued in February 2011. Richland Operations Office officials made clear that the subcontract was not commercial when they awarded the prime contract. However, MSA, through its actions during the course of the subcontract, continued to operate as though the subcontract was commercial in nature. As such, LMSI continued declining the Richland Operations Office and MSA any visibility into the firm fixed price and fixed unit rate portions of its subcontract. Even though MSA acknowledged that the audit requirement was applicable to a portion of the subcontract, it failed to conduct the necessary audits. At the time of our review, the dispute between MSA and the Department remained unresolved.

Increased Risk

Our review found that contracts may have been awarded that were not in the best interest of the Government and that the Department may have paid higher costs than were necessary and allowable. In particular, LMSI was awarded a \$232 million subcontract to provide IT support services to a defined population at the Hanford site. It was then awarded almost \$115 million in additional subcontracts to perform work that was within the scope of the original subcontract without an accompanying downward adjustment to the value of the initial subcontract. As of the end of fiscal year 2014, LMSI had been paid nearly \$312 million for IT support services rendered, an increase of approximately \$80 million over its estimate. We are concerned by the Department's lack of consent to, visibility into, and incurred cost audits on these subcontracts.

The Department also may be paying unallowable costs related to inappropriate profit in an affiliate arrangement. Contrary to Federal requirements, our analysis of LMSI's incurred costs and invoices from January 2010 through December 2014 indicated that the Department paid more than \$63.5 million in excess of costs incurred.

Without effective monitoring and oversight by the Department and MSA, the escalation of T&M costs could continue throughout the remainder of the LMSI subcontract, limiting assurance that LMSI was using efficient methods and effective cost controls. In addition, the lack of timely subcontract cost audits increases the risk that the necessary records will not be available for review and the Department may be unable to fully recover unallowable costs. Because of the significant growth in T&M costs and the discrepancies identified during our test work on a limited sample of invoices, we question the full \$120 million incurred on T&M task orders until an allowability determination can be made through appropriate cost incurred audits.

Other Matters

The complaint received by the Office of Inspector General also alleged a conflict of interest between MSA and LMSI. Based on our review, we could not substantiate that there had been a conflict of interest in this situation. However, a similar incident that gave the appearance of a conflict of interest came to our attention during our review. In particular, we found that several executives within MSA also held senior executive positions within Lockheed Martin Corporation. As a result, six MSA employees were specifically excluded from making strategic and tactical decisions on the management of its contract with the Department. However, we determined that some of these excluded employees were directly involved in discussions or negotiations with Department officials on a proposed settlement agreement for \$2.2 million related to profits paid on the LMSI subcontract. The proposed agreement, which the Richland Operations Office did not accept, would have required Federal officials to relinquish any future claims or other contract actions related to consent of the LMSI subcontract, including reimbursement of unallowable costs. In addition, the agreement would have extended the subcontract's period of performance. Based on our review of the personnel involved in decision making at MSA, we concluded that these individuals had inappropriately participated in excluded activities.

Inappropriate actions on excluded activities occurred because MSA had circumvented the internal controls established in its *Organizational Conflict of Interest Mitigation Plan for Information Management Activities Associated with the Department of Energy Mission Support Contract*, which restricted these individuals from taking part in strategic or tactical decision-making. Therefore, we have recommended actions that, if implemented, should prevent any future conflicts of interest, either in appearance or fact.

RECOMMENDATIONS

To help ensure that IT contracts are effectively managed at the Hanford Site, we recommend that the Deputy Under Secretary for Management and Performance direct the Richland Operations Office and the Office of River Protection to:

1. Resolve the questioned costs and issues related to affiliate profit described in this report and ensure that appropriate incurred cost audits are performed in an expeditious manner;
2. Direct the Hanford Site's prime contractors to fully comply with contract requirements for obtaining IT services; and
3. Ensure full compliance with the FAR, including areas related to affiliate contracts, subcontract consent, and subcontract audits.

To ensure that organizational conflicts of interest do not occur, we recommend that the Assistant Secretary for Environmental Management, in conjunction with the Richland Operations Office:

4. Review MSA's Mitigation Plan to ensure that it includes specifically prohibited activities and enforceable consequences for undertaking such activities; and
5. Ensure that MSA's Mitigation Plan is fully enforced.

MANAGEMENT RESPONSE

Management concurred with the report's recommendations and indicated that corrective actions had been initiated or were planned to address the issues identified in the report. For example, management noted that the Department issued a final Contracting Officer's decision disallowing more than \$63 million of affiliate fee or profit paid to MSA's affiliate Lockheed Martin Services, Inc., for calendar years 2010 through 2014. Moreover, management indicated that the Richland Operations Office was working with MSA to ensure all prime and subcontract incurred costs audits were completed expeditiously. In addition, Richland Operations Office and Office of River Protection officials plan to perform a review of the contract mechanisms and processes that Hanford Site prime contractors use to obtain IT services provided through the MSA contract to determine whether the contract's intent for providing those services was met.

Management noted that it was through its oversight that the issue of affiliate fee or profit was initially identified. However, it intends to revise existing oversight mechanisms related to affiliate subcontract, subcontract consent, and subcontract audits to ensure similar issues are identified and addressed going forward. The Richland Operations Office and Office of River Protection also plan to continue providing oversight through reviews and audits by independent entities to ensure contractor compliance with the FAR, subcontract consent requirements, and subcontractor audits.

To ensure that organizational conflicts of interest do not occur, management responded that it had identified the affiliate fee or profit during the pre-award phase of the Mission Support Contract and concluded that its review of MSA's mitigation plan in the specific instance was effective. Management commented that the subsequent breach of the plan and applicable contract clause related to organizational conflict of interest and resulting disallowance of affiliate fee was the consequence of undertaking such activities under this contract. As such, management indicated that it would continue to use the applicable tools and clauses to ensure compliance with contract terms and conditions. Management also noted that it had taken action against the prohibited organizational activities identified in the report by disallowing more than \$63 million of affiliate fee or profit for calendar years 2010 through 2014.

AUDITOR COMMENTS

Management's comments and planned corrective actions were generally responsive to our recommendations. However, management's stated corrective actions did not fully address recommendations 4 and 5. While we appreciate management's concurrence with all recommendations and applaud management's efforts to disallow affiliate fee or profit, this action was unrelated to the enforcement of the Mitigation Plan related to organizational conflicts. As noted in the report, these recommendations were made because of prohibited actions taken by MSA officials in contravention of its Mitigation Plan when attempting to resolve the affiliate fee or profit issue with the Department. As such, we continue to recommend that management review MSA's Mitigation Plan to ensure that it includes enforceable consequences for undertaking prohibited activities and fully enforce it in the event such activities occur. Management's comments are included in Appendix 3.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

To determine whether information technology (IT) contracts and activities at the Department of Energy's Hanford Site were effectively managed.

Scope

The audit was performed between August 2014 and April 2016 at the Department's Hanford Site in Richland, Washington. The audit was conducted under Office of Inspector General project number A14TG052.

Methodology

To accomplish our objective, we:

- Reviewed applicable laws and regulations pertaining to contract oversight and management;
- Reviewed applicable standards and guidance issued by the Department;
- Reviewed prior reports issued by the Office of Inspector General;
- Held discussions with Office of River Protection, Richland Operations Office, and contractor personnel;
- Reviewed the selection and implementation processes associated with IT contracts at the Hanford Site;
- Reviewed pertinent official correspondence between Federal and contractor personnel as it related to the audit scope; and
- Obtained a list of all known task orders associated with IT services since the inception of the Mission Support Contract and judgmentally selected a sample of Lockheed Martin Services, Inc. (LMSI) task orders to determine whether the Statements of Work were detailed and that work being performed was within the scope of the Statements of Work. We also judgmentally selected and reviewed a sample of LMSI invoices and supporting documents to determine appropriateness to support payment. Because we did not use a statistical sample, we were unable to project the results of our analysis to the entire population.

We conducted this performance audit in accordance with generally accepted Government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis

for our findings and conclusions based on our audit objectives. Accordingly, we assessed significant internal controls and the Department's implementation of the *GPRRA Modernization Act of 2010* and determined that it had established performance measures for managing contracts and contractor performance. Because our review was limited, it would not have necessarily disclosed all internal control deficiencies that may have existed at the time of our audit. We did not rely on computer-processed data to satisfy our audit objective.

An exit conference was held with Department officials on March 22, 2016.

PRIOR REPORTS

- Special Report on *Incurred Cost Audit Coverage of Non-Management and Operating Contractors* (DOE/IG-0934, February 2015). Historically, the Department of Energy has met its non-management and operating (M&O) contract cost audit requirements through an agreement with the Defense Contract Audit Agency (DCAA). However, over the past several years, DCAA has been unable to perform many of its audits on a timely basis. In fact, DCAA itself reported delays from 1 year to more than 8 years for audits of the Department's non-M&O contracts and related Department-funded subcontracts due to a lack of resources to meet all Department of Defense and civilian agency audit requests. These delays resulted in a backlog of audits of contracts and subcontracts with incurred costs valued at billions of dollars per year. This situation was exacerbated by the fact that the Department lacked a comprehensive strategy to ensure that non-M&O contractor costs were subjected to necessary audits. Timely incurred cost audits of non-M&O contractors and subcontractors are an essential part of the system of safeguards to identify internal control weaknesses and detect and prevent Department reimbursement of contractor-claimed unallowable costs.
- Audit Report on the *Lawrence Livermore National Laboratory's Use of Time and Materials Subcontracts* (OAS-M-13-06, August 2013). Lawrence Livermore National Laboratory (LLNL) had not always procured services through time and materials subcontracts in the most effective and efficient manner. Testing revealed that some sole source justifications were not fully supported as required by Federal regulations and internal policies and procedures. Specifically, LLNL had not fully justified sole source selection on six of seven subcontracts. Furthermore, in two of the sole source subcontracts, LLNL did not perform an adequate price analysis. As a consequence, LLNL did not demonstrate, so the audit was unable to determine, that the decision to award those particular time and materials subcontracts was in the best interest of the National Nuclear Security Administration.
- Special Report on *Management and Operating Contractors' Subcontract Audit Coverage* (DOE/IG-0885, April 2013). Between fiscal years 2010 and 2012, the Office of Inspector General reported subcontract audit weaknesses with nine M&O contractors. Subcontracts valued in excess of \$906 million had not been audited or were reviewed in a manner that did not meet audit standards. The subcontract costs were not audited because the Department did not ensure that its M&O contractors developed and implemented procedures to meet their contractual requirements. The failure to ensure that effective subcontract audit policies were developed and implemented substantially increased the risk that the Department would incur undetected unallowable costs. Furthermore, the lack of timely audits increased the risk that required records would not be available or that the statute of limitations would prevent M&O contractors from recovering unallowable costs.

MANAGEMENT COMMENTS



Department of Energy
Washington, DC 20585
February 10, 2016

MEMORANDUM FOR RICKEY R. HASS
DEPUTY INSPECTOR GENERAL
FOR AUDITS AND INSPECTIONS
OFFICE OF INSPECTOR GENERAL

FROM: MONICA C. REGALBUTO *Monica C. Regalbuto*
ASSISTANT SECRETARY
FOR ENVIRONMENTAL MANAGEMENT

SUBJECT: Management Response to the Office of Inspector General
Draft Audit Report on "The Department of Energy's
Management and Oversight of Information Technology
Contracts at the Hanford Site"

Thank you for the opportunity to review the Office of Inspector General (OIG) subject draft report. After completing our review, we agree with the recommendations contained in the draft report.

The following clarifications are requested:

1. Regarding the portions of the draft report related to findings that "the Department of Energy (DOE) did not question the substantial growth in T&M costs." (Draft at page 3 of the "Details of Finding" section) -- DOE's lack of questioning these costs was due to Mission Support Alliance (MSA), Limited Liability Company consistently neglecting to obtain detailed cost information regarding the Time & Materials (T&M) tasks, despite contract requirements and specific direction from the DOE contracting officer to provide such information. DOE requested information about the Lockheed Martin Services, Incorporated (LMSI) incurred costs through at least two formal letters and other informal requests. Accordingly, this finding should be clarified by stating that "MSA's lack of oversight and failure to provide visibility of the costs incurred on the T&M tasks resulted in DOE's restricted ability to question the substantial growth in T&M costs."
2. Regarding the portions of the Draft related to findings that "some of the site's prime contractors entered into separate agreements with LMSI to perform services that had been included in the scope of the original MSA Contract." (Draft at page 2 of the "Results of Audit" section, first bullet). The Draft consistently states that "MSA" entered into a separate agreement with LMSI to provide services to CH2M Hill Plateau Remediation Company (CHPRC), and that "Washington River Protection Solutions" (WRPS) entered into separate



agreements with LMSI to provide services to WRPS. The Richland Operations Office (RL) review has indicated that CHPRC and WRPS each entered into an agreement with LMSI to receive Information Technology (IT) services, so it is not clear whether the Draft intended to indicate that "CHPRC" rather than "MSA" entered into a separate agreement to provide services to CHPRC. Moreover, clarification is requested regarding what is meant in the Draft by referring to these agreements as "separate." MSA's subcontract with LMSI (Subcontract No. 39568) included a provision whereby LMSI could perform the MSA IT scope of work through agreements directly with other Hanford contractors. Such agreements would appear to be extensions of Subcontract No. 39568, and therefore not separate in that sense. To the extent the LMSI/CHPRC and LMSI/WRPS agreements are in fact "separate" from Subcontract No. 39568, then RL agrees that MSA's failure to request or receive consent from the DOE contracting officer is a clear non-compliance with the terms of the MSA Contract. Similarly, to the extent the LMSI/CHPRC and LMSI/WRPS agreements are truly "separate" from Subcontract No. 39568, then RL agrees that CHPRC's and WRPS's failure to request or receive consent from the DOE contracting officer is a clear non-compliance with the terms of the CHPRC and WRPS Contracts. However, to the extent the LMSI/CHPRC and LMSI/WRPS agreements are not separate from Subcontract No. 39568, then the terms of CHPRC and WRPS prime contracts do not appear to require CHPRC and WRPS to obtain consent from the DOE contracting officer. The finalized version of the Draft should make this clarification.

The draft OIG report identifies five recommendations, which Environmental Management accepts and will implement actions to address. A summary of the actions planned to address each of the recommendations is delineated in the attachment.

If you have any questions, please contact me or Mr. J. E. Surash, Deputy Assistant Secretary for Acquisition and Project Management, at (202) 586-6382.

Attachment

cc: Mark Whitney, EM-2
Frank Marcinowski, EM-2.1 (Acting)
Mark Gilbertson, EM-10
J. E. Surash, EM-50
Melody Bell, EM-70
Jeanne Beard, EM-72

**Attachment – Department Response to the Recommendation of the
Office of Inspector General Draft Report DOE/IG-A14TG052 on
“The Department of Energy’s Management and Oversight
of Information Technology at the Hanford Site”**

Recommendations:

To help ensure that IT contracts are effectively managed at the Hanford Site, we recommend that the Deputy Under Secretary for Management and Performance direct the Richland Operations Office and the Office of River Protection to:

- 1. Resolve the questioned costs and issues related to affiliate profit described in this report and ensure that appropriate incurred cost audits are performed in an expeditious manner;**

The Richland Operations Office (RL) has attempted to resolve the affiliate profit/fee issues through mediation with Mission Support Alliance, LLC (MSA), but this process has not resulted in an acceptable resolution. Accordingly, RL formally issued a final Contracting Officer’s decision (Letter No. 16-PRO-0036, dated November 10, 2015) disallowing \$63,501,654.96 of affiliate fee/profit paid to MSA’s affiliate, Lockheed Martin Services, Inc. (LMSI) for calendar years 2010 through 2014. Moreover, RL is actively working with MSA to ensure all prime and subcontract incurred cost audits are completed expeditiously.

- 2. Direct the Hanford Site’s prime contractors to fully comply with contract requirements for obtaining IT services;**

RL and the Office of River Protection (ORP) will work with the Hanford Site’s prime contractors to ensure they fully comply with contract requirements for obtaining IT services. This action will be accomplished by performing a review of the contract mechanisms and processes Hanford site prime contractors are using to obtain IT services provided through the MSA contract and determining whether those mechanisms and processes are meeting the MSA contract’s intent for providing those services.

- 3. Ensure full compliance with the FAR, including areas related to affiliate contracts, subcontract consent, and subcontract audits;**

RL and ORP will continue to provide oversight thru reviews, and audits by independent audit entities, to ensure contractor compliance with FAR, subcontract consent and subcontractor audits. It was through RL’s oversight that the issue of affiliate fee/profit was identified, and RL will continue to oversee our contractors to ensure issues relative to affiliate contracts are adequately addressed/reviewed. To the extent necessary to provide sufficient oversight of IT services, RL and ORP will revise the existing mechanisms and processes related to affiliate subcontracts, subcontract consent and subcontract audits.

To ensure that organizational conflicts of interest do not occur, we recommend that the Assistant Secretary for Environmental Management, in conjunction with the Richland Operations Office:

4. Review MSA's Mitigation Plan to ensure that it includes specifically prohibited activities and enforceable consequences for undertaking such activities;

The affiliate fee/profit issue was identified during the pre-award phase of the Mission Support Contract, therefore it can be concluded that RL's review of MSA's mitigation plan in the specific instance was effective. The subsequent breach of the plan and applicable contract clause related to organizational conflict of interest and resulting disallowance of affiliate fee is the consequence of undertaking such activities under this contract. RL will continue to use applicable tools and clauses to ensure compliance with contract terms and conditions.

5. Ensure that MSA's Mitigation Plan is fully enforced.

RL took enforcement action by issuing Letter No. 16-PRO-0036, dated November 10, 2015, subject: Final Contracting Officer's (CO) Decision Regarding Unallowable Affiliate Profit/Fee Paid to Lockheed Martin Services, Inc. (LMSI) disallowing \$63,501,654.96 of affiliate fee/profit for calendar years 2010 through 2014.

FEEDBACK

The Office of Inspector General has a continuing interest in improving the usefulness of its products. We aim to make our reports as responsive as possible and ask you to consider sharing your thoughts with us.

Please send your comments, suggestions, and feedback to OIG.Reports@hq.doe.gov and include your name, contact information, and the report number. You may also mail comments to:

Office of Inspector General (IG-12)
Department of Energy
Washington, DC 20585

If you want to discuss this report or your comments with a member of the Office of Inspector General staff, please contact our office at (202) 253-2162.