



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

AUDIT REPORT

Battelle's Pacific Northwest National
Laboratory Procurement Activities

OAI-M-16-14

July 2016



Department of Energy
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July 27, 2016

MEMORANDUM FOR THE MANAGER, PACIFIC NORTHWEST SITE OFFICE

Michelle Anderson

FROM: Michelle Anderson
Assistant Inspector General
for Audits and Inspections
Office of Inspector General

SUBJECT: INFORMATION: Audit Report on "Battelle's Pacific Northwest National Laboratory Procurement Activities"

BACKGROUND

Since 1965, Battelle Memorial Institute (Battelle) has operated the Pacific Northwest National Laboratory, which performs research in the areas of environmental protection and cleanup, energy resources, and national security. The Department's Pacific Northwest Site Office (PNSO) manages Battelle under a performance-based management and operating contract. To achieve the Department's mission, Battelle procures services and equipment through subcontracts. For fiscal year 2015, Battelle had over \$318 million (33 percent of laboratory funding) in subcontracts.

The Department of Energy Acquisition Regulation specifies that purchasing systems and methods must be well-defined, consistently applied, and follow the appropriate purchasing practices. Furthermore, Federal regulations require that management and operating contractors maintain effective systems of management controls for both administrative and programmatic functions, such as procurements. Some of these controls are outlined in Battelle's acquisition guidelines and in Federal regulations. The controls include contract thresholds relating to various contract requirements, such as records retention, Department notification, and management review. These controls are in place to ensure that costs incurred are in compliance with regulations and are for the intended purposes of the contract, and that resources are safeguarded against waste, loss, mismanagement, or misappropriation. Battelle documents all procurement activities in either official hard copy or paperless files. We initiated this audit to determine whether Battelle effectively managed its procurement activities. This audit is part of a planned series of audits focusing on management and operating contractor subcontract administration.

RESULTS OF AUDIT

Our audit identified instances in which Battelle did not effectively manage its procurement activities. In particular, we found the following:

- Paperless procurement files were not always reliable in that the paperless system did not record the origination, approvals, changes, and review of changes to documents. In 29 of 47 paperless procurements randomly sampled, documentation included editable Microsoft Office Word or Excel files, which could be easily modified after management review. Additionally, in 22 of the 47 procurements, documents contained “image” signatures that could easily be copied or fabricated.
- Paperless procurement files did not always contain the necessary documentation to support contracting decisions. In 28 of 47 procurements, required documents, such as the Memorandum of Procurement and Representations and Certifications, were added to the paperless file after Battelle was notified of our sample selection. We also noted that the required documents in the paperless file were not always for the specific procurement and did not always include descriptors, such as dates, Purchase Requisition or Purchase Order number, and signatures by appropriate individuals. The Memorandum of Procurement provides key details of the acquisition and could serve as the approval of steps taken during the contracting process. Additionally, lack of specific detail calls into question the integrity of the documents.
- Battelle split procurements into multiple awards, which appeared to allow Contracts Specialists to award procurements that exceeded their authority. We judgmentally selected four subcontractors that received multiple awards on the same day, and found that in all four cases, the procurement requirement was split into multiple awards. Combined, these awards exceeded threshold values for management review and approval. There was no indication that upper management was aware of the aggregate value of these task orders, which could give the appearance that thresholds were being circumvented. For example, Battelle awarded 30 Purchase Orders on September 20 and September 23, 2013, with an aggregate value of \$1.9 million. This amount was more than the Contracts Specialist’s delegation of authority of \$1.5 million. When we discussed this with management, they performed an analysis of procurements for facility security upgrades in one major program and found that procurements were split 96 percent of the time.
- Contracts did not always receive the appropriate level of review and approval when they were modified. We performed tests to identify subcontracts with multiple modifications and identified two individual contract actions, where initial award and modifications were under key approval amounts; however, these contracts were then modified to values that exceeded approval thresholds. For example, Battelle awarded a 1-year, \$100,000 contract, which was then modified 20 times over a 6-year period to over \$3 million without requiring any increase in scrutiny over a now significantly larger dollar subcontract.

The issues we identified were due to weaknesses in Battelle’s policies and procedures as well as inconsistent implementation of the policies and procedures by Battelle procurement officials. Policies and procedures did not provide guidance for maintaining required documents in the official procurement file or sufficient management review of accuracy and completeness in the files. They also proved insufficient in preventing or detecting split purchases under Purchase

Orders. Additionally, in recent reviews conducted over Battelle's procurement activities, PNSO noted an inconsistency in the application of Battelle's acquisition guidelines. Contributing to these weaknesses, PNSO expressed concerns that the primary method used for performing independent verifications of contractors' purchasing systems did not go to the same depth as a full purchasing system review. Also, Battelle did not conduct adequate reviews of individual contract files.

Based on our findings, Department management expressed concern that inattention to requirements and details could lead to issues with the validity of contracting actions and whether they were in the Government's best interests. The paperless system's inadequate capabilities in ensuring integrity in the approval and signature process and support for contracting decisions hinders Battelle, the Department, and other reviewers' ability to identify whether questionable procurement practices have occurred or potentially to question unallowable subcontract costs. Finally, because Contracts Specialists exceeded their Delegation of Authority and threshold values, there is increased risk that Battelle procurements are being managed by individuals who do not have the skills and experience commensurate with the value and complexity of the procurement.

MANAGEMENT RESPONSE

Management generally concurred with the report's findings and recommendations. However, management did not agree with our conclusion that Department management did not provide adequate oversight, and in commenting to this report, it identified several oversight actions taken. Management comments were generally responsive to the findings and recommendations. However, although we acknowledge the oversight steps taken by Department management, we remain concerned that these steps were not fully adequate. Management's comments can be found in Appendix 4.

cc: Deputy Secretary
Director, Office of Science
Chief of Staff

BATTELLE’S PACIFIC NORTHWEST NATIONAL LABORATORY PROCUREMENT ACTIVITIES

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. Sampling Methodology for Split Purchases and Modifications	13
3. Prior Report	15
4. Management Comments	16

BATTELLE'S PACIFIC NORTHWEST NATIONAL LABORATORY PROCUREMENT ACTIVITIES

DETAILS OF FINDING

Battelle Memorial Institute (Battelle) did not effectively manage its procurement activities. In particular, Battelle's paperless procurement files were inadequate in that they were unreliable and were incomplete. In addition, subcontracts appeared to exceed procurement personnel's authority and did not receive the appropriate level of review when large dollar value procurements were split into multiple separate contract actions at the time of award and when contracts were modified.

Inadequate Paperless Procurement Records

Battelle's paperless procurement files were inadequate to support individual procurements. Department of Energy Acquisition Regulation 970.5244-1, *Contractor's Purchasing System*, requires adequate documentation in contract files to establish the propriety of the transaction and the price paid. However, we reviewed a random sample of 47 paperless procurements and found several issues with contract file documentation. Specifically, the paperless procurement files were not reliable in that the system did not record the origination, approvals, changes, and review of changes to documents. Furthermore, the paperless files did not contain all of the required documents. Additionally, in several instances, included documents were either not for, or could not be readily attributed to, the specific procurement. Battelle started using the paperless procurement system in 2011 and now uses it for virtually all of its procurements.

File Reliability

The paperless procurement files were not reliable in that the system did not document the origination, approvals, changes, and review of changes to documents. We found the following:

- 29 of 47 files (62 percent) contained Microsoft Office Word or Excel files, such as the statement of work, sole source justification, subcontractor proposal, and technical evaluation, which made the documents vulnerable to editing after management review.
- 22 of 47 procurements (47 percent) had required documents with signatures that could not be validated. Instead, these documents used "image" signatures that could easily be copied or signatures typed in a handwriting-like font. Therefore, we could not determine whether the named individual actually signed the document.

Additionally, we noted that the paperless system did not document who accessed and used the system or the procurement files prior to closeout. Therefore, any changes that occurred could not be tracked or authenticated. Also, the paperless system did not have a system sign-off on documents. This made it difficult to authenticate the signer and maintain the integrity of the signed record. For example, we found three procurements where the sole source justification did not include validated signatures. In these instances, the paperless system did not document the user who uploaded the sole source justification into the contract file or whether the document had been reviewed by the appropriate individual(s).

Incomplete Documentation

Battelle paperless procurement files did not contain the necessary documentation to support contracting decisions. We found instances in which paperless files did not contain all the required documents. In 28 of 47 procurements (60 percent), required documents were added to the paperless file after we submitted our sample selection to Battelle. For example, we observed multiple instances where the Memorandum of Procurement was added after we requested procurement file documentation. The Memorandum of Procurement is required under Battelle's acquisition guidelines (AGs) for all acquisitions exceeding either \$25,000 or \$100,000, depending on the pricing technique utilized. The Memorandum of Procurement documents various key details of the acquisition and could serve as the approval of steps taken during the contracting process. However, in two instances, where the Memorandum of Procurement was the primary support for the subcontract, it did not fully describe the contract action. During our audit, the Pacific Northwest Site Office (PNSO) conducted a *Survey of Battelle Memorial Institute's Procurement System at Pacific Northwest National Laboratory*. PNSO identified similar issues in its report, dated November 4, 2015, in which Contracts Specialists did not fully document actions in the Memorandum of Procurement, which should be a stand-alone document that addresses all aspects of the procurement.

Additionally, in five of these procurements, required subcontractor Representation and Certification documents were missing from the paperless file. The Representation and Certification identifies conflicts of interest, foreign control, small business status, and debarment. We provided Battelle a list of the missing documents, and it was able to locate the documents for four of the five procurements. Battelle was unable to obtain the final missing Representation and Certifications because the main point of contact on the procurement was on long-term disability. This stresses the importance of including all necessary documentation in the official contract file because a knowledgeable party may not always be available.

Similarly, required documents included in the contract files were either not associated with, or could not be attributed to, the specific procurement. For example, documents:

- Did not contain dates that would give context for when they were completed in 8 of 47 procurements (17 percent).
- Did not have the Purchase Requisition or Purchase Order number that would attribute the documents to the specific procurement in 8 of 47 procurements (17 percent).
- Were signed by someone who was no longer a Contracts Specialist and no longer had signature authority at the time of award in 1 of the 47 procurements (2 percent).

Furthermore, in one procurement the sole source justification title listed only a Blanket Ordering Agreement (BOA) number, even though the Purchase Order was not under a BOA. The document also was not dated, and the dates referenced in the document as "deadlines" were 6 months before the Purchase Order was issued. Moreover, the Contracts Specialist who "signed"

the document did not work for the Procurement Department at the inception of the Purchase Order. Not only was this document not attributable to the procurement, but it was also an easily editable Word document, calling into question the integrity of the document.

Exceeding Procurement Authority and Threshold Values

Subcontracts appeared to exceed procurement personnel authority and did not receive the appropriate level of review when large dollar value procurements were split into multiple separate contract actions at the time of award and when contracts were modified.

Split Purchases

Battelle contracted for services and goods that appeared to split procurements into multiple awards, which allowed Contracts Specialists to award procurements that exceeded their authority. We judgmentally selected four subcontractors that received multiple awards on the same day and found that in all four cases, the procurement requirement was split into multiple awards. The aggregate value of these procurements also exceeded threshold values for the review and approval of Battelle's Acquisition Review Board and Contracting Officer Notification. There was no indication that upper management was aware of the aggregate value of these task orders, which could give the appearance that thresholds were being circumvented. Both the Federal Acquisition Regulation (FAR) and Battelle's AGs prohibit splitting acquisitions into multiple awards to avoid any requirements that applied to these purchases. Battelle's AGs also prohibit individuals from exceeding the amount authorized under the Contracts Specialist's delegation of authority. However, we found instances in which numerous awards were made to the same subcontractor, for the same type of items and services, and were often awarded on the same day. Battelle accomplished this by issuing task orders under a single BOA or as multiple separate awards. A BOA only contained the terms and conditions of a contract, and individual task orders that outline specific scope, timing, and cost were issued at a later time against the BOA. For example, Battelle did the following:

- Awarded 30 Purchase Orders with an aggregate value of \$1.9 million, which was more than the Contracts Specialist's delegation of authority of \$1.5 million. We noted that the procurement actions were competed at the higher \$1.9 million value and were later broken into the 30 separate Purchase Orders. Twenty-eight of the awards were processed on September 20, 2013, and two on September 23, 2013, to one subcontractor to perform work at various sites within Poland. Battelle used a BOA, processed on August 22, 2013, and issued each task order as a separate Purchase Order.
- Awarded 27 Purchase Orders with a value over \$3.1 million, which was more than double the Contracts Specialist's delegation of authority of \$1.5 million. This action was split into 27 Purchase Orders to one subcontractor, among various sites in Ukraine. These Purchase Orders were processed on September 25, 2014, under a single BOA. The BOA was processed on June 20, 2013. Furthermore, the same sole source justification

was copied and used for several of the Purchase Orders, including the solicitation amount, even though the amount varied among the separate Purchase Orders indicating that this was, in substance, a single procurement action.

- Awarded 69 separate Purchase Orders with a combined value over \$2.1 million, which was over the Contracts Specialist's delegation of authority of \$500,000. These awards were processed between September 23 and September 25, 2014, to the same subcontractor for work throughout Mexico and Colombia. Several of the sites were included under one proposal, and the costs were divided equally among the separate Purchase Orders. For example, costs were proposed as one amount for travel among four sites and then the amount appeared to be split evenly among the corresponding four Purchase Orders.
- Awarded three procurements with a combined value of approximately \$1.9 million, processed on September 26, 2014, to the same subcontractor. The procurements were for help desk support, preventative maintenance labor, and preventative maintenance travel to various countries. The preventative maintenance travel costs were incurred in direct support of the preventative maintenance labor, even though they were issued under separate Purchase Orders.

Battelle management asserted that they split these awards for contract administration convenience and based on the funding client's needs and to provide ease in reporting metrics, paying invoices, and timely closeout. If this was indeed the case, then this practice was inconsistently applied. We noted that in other instances, Battelle awarded similar procurement actions in a manner that was within the Contracts Specialist's authority, without splitting the procurements. When we discussed this with Pacific Northwest National Laboratory management, they performed an analysis of procurements in one major program for facility security upgrades and found that procurements were split 96 percent of the time. In 62 of 1,639 Purchase Orders (4 percent) for one program from 2013 through 2015, Battelle combined sites, buildings within a site, or scope of work. In another example, in July 2010, Battelle awarded a contract for the preventative maintenance and repair of equipment at various locations in Spain. The work conducted at these sites was combined into one contract. The total value of the work at both sites was approximately \$180,000, and the Contracts Specialist's authority was \$1 million, which was not split into multiple Purchase Orders and was within the Contracts Specialist's authority.

When we discussed these concerns with management, Battelle officials told us they consider individual task orders under BOAs as stand-alone actions for purposes of management review. However, PNSO expressed concern over Battelle treating individual task orders as distinct contracts and not aggregating the amounts to show the true value of an acquisition. In a letter to Battelle dated November 19, 2015, PNSO stated that this practice led to specialists exceeding their delegated authorities, avoidance of independent reviews by other acquisition professionals, and avoidance of providing adequate notification to the PNSO Contracting Officer.

Contract Modifications

Contracts did not always receive the appropriate level of review and approval when they were modified. We performed tests to identify subcontracts with multiple modifications and identified two individual contract actions that did not receive the appropriate level of review and approval when modified. Specifically, individual contract actions, such as initial award and modifications, were under key approval amounts, but these contracts were then modified to values that exceeded approval thresholds. For example, without requiring any increase in scrutiny over a larger dollar subcontract, Battelle:

- Awarded a 1-year, \$100,000 contract for the installation of radiation portal monitor hardware and software, which was then modified 20 times over a 6-year period to over \$3 million; and
- Awarded a \$980,000 contract for the purchase of portable radiation detection devices, which was modified within 1 month to over \$1.2 million.

Again when we discussed these concerns with management, Battelle officials told us that they consider original awards and modifications as stand-alone actions. However, PNSO expressed concern over Battelle treating modifications as distinct contracts, and in its November 19, 2015, letter, PNSO outlined its reservations in treating task orders under BOAs as stand-alone actions.

Contributing Factors

The issues we identified were due to weaknesses in Battelle's policies and procedures, as well as inconsistent implementation of policies and procedures. Additionally, the Department relied on reviews that did not fully assess Battelle's procurement system, and Battelle management did not provide adequate oversight of Battelle's procurement activities.

Battelle Policies

Battelle's policies and procedures were not adequate to identify or prevent questionable procurement practices. For example, policies and procedures:

- Did not provide guidance for maintaining required documents in the official procurement file or sufficient management review of accuracy and completeness in the paperless files. All procurements, including those completed within the paperless system, were subject to the requirements under Battelle's AGs. The AGs address maintenance of the procurement file and required documentation. However, the AGs did not discuss the appropriate location for documentation or for referencing where documentation under a specific procurement is stored. PNSO's November 4, 2015, report also noted that documentation was not always in the official file and the actual location of documentation was not clearly outlined in the procurement file.
- Provided little guidance on preventing and detecting split purchases under Purchase Orders. The only guidance for procurement personnel concerning split purchases is in

AG-01, *Procurement Policies Manual*, which states that purchases were not to be split for the purpose of employing simplified acquisition procedures. However, there were no controls outlined in the policies and procedures to prevent and detect splitting purchases so that procurements were under a Contracts Specialist's delegation of authority. In comparison, Battelle's Purchase Card policies and procedures contained guidance to prevent and detect split purchases, including monthly reviews that target possible split transactions, and provided references to the definition of a split purchase.

Furthermore, Battelle's policies and procedures over acquisitions were not always implemented consistently and effectively. In recent reviews of Battelle's procurement activities, PNSO noted a pattern of inconsistency in the application and utilization of the AGs. For example, AG-23, *Types of Contracts*, provided personnel with an explanation of the different types of contracts utilized at the laboratory and criteria to consider when selecting the contract type for a procurement. However, PNSO noted in its November 19, 2015, letter that Contracts Specialists did not always clearly understand the type of contract utilized in procurements. This included considering a Time and Material contract as a Fixed-price contract and subject to Fixed-price terms. Additionally, specialists used Indefinite Delivery, Indefinite Quantity contracts when there was a known delivery date and a definite quantity to be ordered. Per Battelle's AG-28, *Indefinite Quantity Contracts and Basic Ordering Agreements*, this type of contract is normally utilized when the exact times and/or quantities of future deliveries are not known at the time of contract award. PNSO further stated in its letter that it believed training was necessary for Contract's staff to understand the requirements of the different types of contracts, along with expanding AG-23 to include more detail of the types of contract and their appropriate uses.

We also noted the inconsistency in the application of policies and procedures. Specifically, Battelle's management and AG-28 indicated that BOAs were utilized to expedite contracting for uncertain requirements for services/supplies when specific items, quantities, and prices were not known at the time the agreement was executed. However, we found that BOAs were frequently used for other program procurements when scope and price were well known.

Department and Contractor Oversight

Contributing to the weaknesses we identified, the Department relied on reviews that did not fully assess Battelle's procurement system. Additionally, Battelle management did not provide adequate review and oversight to ensure that specialists were following policies and procedures.

Battelle's Procurement Department was reviewed by the Procurement Evaluation and Re-engineering Team (PERT), a collection of contractor and DOE procurement professionals. However, PNSO expressed concerns that, even though the PERT was used as the primary method for performing independent verifications of contractors' purchasing systems, it did not go to the same depth as a full purchasing system review. The PERT assessment over a contractor's purchasing system is required to be performed at least every 5 years and is conducted by an independent team of Federal and contractor personnel. This review is a peer review that aids Contracting Officers in their responsibility for approval and oversight of contractors' purchasing system reviews, as outlined in FAR 44.202, *Contracting Officer's Evaluation* and FAR 44.3, *Contractors Purchasing Systems Reviews*. It also was intended to be

a comprehensive review of a contractor's purchasing system using standardized criteria as a guideline. However, the standardized criteria for this assessment did not address the adequacy of the contractor's policies and procedures and only considered whether the procurement staff complied with the written purchasing policies and procedures. Additionally, PNSO further indicated that it planned to conduct more ad hoc reviews of Battelle's procurement activities.

For example, the 2013 PERT assessment over Battelle's procurement system had no significant observations. However, PNSO's 2015 survey team found that contract files were inadequate to support procurements. The team found that Contracts Specialists did not fully document contracting actions in the Memorandum of Procurement, the Procurement Department did not maintain a complete contract file, several files contained mistakes in documentation, and Representations and Certifications were not completed correctly. Additionally, some of the concerns we identified in this report occurred during the scope of the 2013 PERT assessment and may have been identified had PNSO performed a more detailed review beyond the 2013 PERT assessment.

Additionally, Battelle's Procurement Department did not provide adequate reviews of individual contract actions. Several policies existed to ensure that procurement actions received the appropriate level of review. These included Division Contracts Manager review of actions over either \$25,000 or \$100,000, depending on the type of action. However, during our audit we noted several inadequate contract files that were signed by the Division Contracts Manager. For example, we found inconsistencies in the Memorandum of Procurement for a Labor Hour type contract that were not identified during the management review of the action. Even though the contract was a Labor Hour contract, the Memorandum of Procurement stated that an Accounting System Adequacy Summary was not applicable because the contract was Firm Fixed-price. Additionally, the contract amount on the signature page was \$990,000, even though the actual contract amount was \$360,000. We also noted an instance where a Representation and Certification document was added after a contract file was closed, even though the Contracts Specialist and Closeout Specialists confirmed, in a closeout checklist, that file documentation was complete.

In its letter to Battelle dated November 19, 2015, the PNSO Contracting Officer adjusted Battelle's consent thresholds and provided several recommendations to Battelle based on the Office of Inspector General's concerns that were communicated to the Contracting Officer and the outcome of PNSO's survey. PNSO's survey was conducted concurrently with our audit. Overall, PNSO's survey found gaps in the content of the AGs, a pattern of inconsistency in following the AGs, improper documentation of transactions, and lack of adequate review and oversight by contracts managers. The survey team recommended the PNSO Contracting Officer reduce Battelle's Purchasing Consent Threshold and conduct regular random file reviews. In response to the weaknesses we identified, the Contracting Officer's recommendations to Battelle included:

- Addressing the cultural issue of treating modifications or individual task orders as distinct contracts;

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- Training staff on the requirements of the different types of contracts and expand the AGs to provide more detail on the different contract types; and
 - Conducting more file reviews to ensure all the appropriate information is contained within the contracting file.

Battelle provided a plan to address these concerns to PNSO on January 27, 2016. Planned actions included implementing process changes for the review and approval of modifications, developing a training plan covering contract types and their appropriate use, revising its AGs, and enhancing contract file reviews. All actions are set to be completed by September 2016.

Subcontract Validity

Problems at the subcontract level can have a significant impact on the prime contractor's ability to meet its contractual obligations. Based upon our findings, Department management expressed concern that Battelle's procurement controls were not working as designed. In particular, inattention to requirements and details can lead to issues with the validity of contracting actions and whether they were in the Government's best interests. Further, Department management was concerned about the lack of integrity and inadequate support for contracting decisions in the paperless system. We noted that the paperless system's lack of integrity and inadequate support for contracting decisions hinders Battelle, the Department, and other reviewers' ability to identify whether questionable procurement practices have occurred or potentially question unallowable subcontract costs. Furthermore, by allowing Contracts Specialists to exceed their Delegation of Authority, Battelle risks procurements being managed by individuals who do not have the skills and experience commensurate with the value and complexity of the procurement.

RECOMMENDATIONS

Improvements within applications, systems, and procurement file reviews will help ensure that Battelle's procurements are appropriately managed and that Battelle acts in the Government's best interest. To address its concerns, PNSO plans to request an additional review of Battelle's procurement system by no later than September 30, 2017. In addition to the Contracting Officer's recommendations to Battelle, we further recommend the Manager, Pacific Northwest Site Office to:

1. Ensure Battelle's policies and procedures are revised to address maintaining adequate official procurement files that support individual procurement actions and are consistently followed;
2. Ensure Battelle's training on contract types and their appropriate use is adequate to provide Procurement Department personnel the skills necessary for effectively administering assigned contract actions;
3. Develop a plan for completing more frequent ad hoc reviews of Battelle's procurement activities in areas not covered under other assessments; and
4. Ensure that Battelle's changes to contract file reviews adequately identify issues with file documentation and Procurement Department personnel following policies and procedures.

MANAGEMENT RESPONSE

Management generally concurred with the report's findings and recommendations. However, management did not agree with our conclusion that Department management did not provide adequate oversight. PNSO noted that it identified Battelle's inconsistencies in its procurement activities prior to the Office of Inspector General performing its review. Also, it noted that acquisition thresholds were lowered in response to PNSO's findings and a corrective action plan was in place addressing many of the concerns found by the Office of Inspector General. PNSO provided corrective actions to address the issues and recommendations identified in the report. PNSO will direct Battelle to perform an effectiveness review of Battelle's corrective actions taken to address the following: inadequate policies and procedures, contract file reviews; and training on contract types and their appropriate use. PNSO will also develop and implement a plan to perform more frequent ad hoc reviews of Battelle procurement activities not covered under other assessments.

AUDITOR COMMENTS

Management comments were generally responsive to the findings and recommendations. However, although we acknowledge the oversight steps taken by Department management, we remain concerned that these steps were not fully adequate. We made changes to this report to reflect the actions taken by Department management.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

The objective of this audit was to determine whether Battelle Memorial Institute (Battelle) effectively managed its procurement activities.

Scope

The audit was performed from June 2015 to July 2016, at the Department of Energy's Pacific Northwest Site Office and the Pacific Northwest National Laboratory (PNNL) in Richland, Washington. The scope of the audit was limited to a review of the Department and Battelle management of procurement activities from fiscal years (FYs) 2005 through 2015. The audit was conducted under the Office of Inspector General project number A15RL044.

Methodology

To accomplish the audit objective, we:

- Reviewed laws, regulations, and program guidance and requirements under Battelle's contract applicable to procurement and subcontracting activities.
- Interviewed key Department and Battelle officials to discuss the processes and procedures used to issue procurement actions and provide oversight over PNNL's Procurement Department.
- Obtained and reviewed Battelle policies and procedures over procurement activities.
- Randomly selected a sample of 47 of 12,500 Purchase Orders from all of Battelle's paperless subcontract files (which started August 17, 2011) up to a process date of August 8, 2015. We reviewed the documents in these files for file reliability and completeness.
- Judgmentally selected 21 of 10,328 Purchase Orders from 4 subcontractors that had multiple Purchase Orders processed on the same day from FY 2010 to FY 2014. We reviewed the subcontract documents to determine similarities in scope of work and key information available at subcontract solicitation and award.
- Judgmentally selected 29 of 14,002 Purchase Orders based on the number of actions processed under individual Purchase Orders and across 6 categories related to the risk of PNNL not applying key threshold requirements.
- Obtained and analyzed selected procurement actions against Battelle's policies and procedures, Battelle's contract requirements, and laws and regulations.

- Obtained and reviewed procurement system oversight activities and the adequacy and completeness of assessments that were relied upon for determining system verification.
- Held discussions with officials from the Department of Energy's Pacific Northwest Site Office and Battelle.

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 objective. We believe the evidence obtained provides a reasonable basis for our conclusions based on our audit objective. Accordingly, we assessed significant internal controls and compliance with laws and regulations necessary to satisfy the audit objective. In particular, we assessed the Department's implementation of the *GPR Modernization Act of 2010* as it relates to our audit objective and found that performance measures had been established for procurement activities reviewed.

Because our review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit. We utilized computer-processed data to identify the population and samples of procurements to achieve our audit objective. Based on our comparison of computer-processed data to supporting documentation, we determined that the data was not reliable for the purposes of selecting items under the split purchases and modifications samples. We took further actions, such as utilizing judgmental samples where pertinent information was obtained from supporting documentation and reported findings were not dependent on the reliability of computer-processed data. However, we determined that data was sufficiently reliable for the purposes of the remaining areas of our report, including paperless file designation and aggregate values of split purchases.

Management waived an exit conference on July 12, 2016.

SAMPLING METHODOLOGY FOR SPLIT PURCHASES AND MODIFICATIONS

We reviewed Purchase Orders from Pacific Northwest National Laboratory's PeopleSoft Acquisition System. Each Purchase Order represented either one subcontract or a portion of a subcontract. We selected Purchase Orders to test Battelle's paperless system by selecting a random sample of 47 of 12,500 Purchase Orders from all of Battelle's paperless subcontract files (which started August 17, 2011) up to a process date of August 8, 2015. Prior to selecting our sample items, we narrowed the universe to 1,860 Purchase Orders, which represent those procurements from the paperless subcontract files with a funding amount as of August 8, 2015, over \$25,000. Additionally, we selected Purchase Orders for review under two judgmental samples from this system to identify split purchases and subcontract modifications. Because selection was based on a judgmental or nonstatistical sample, results and overall conclusions were limited to the items tested and were not projected to the entire population or universe.

Split Purchases

We created a table of 3,420 instances where multiple Purchase Orders were processed under the same subcontractor on the same date from fiscal years (FYs) 2010 through 2014. We judgmentally selected 21 of 10,328 Purchase Orders within these instances. We selected 18 Purchase Orders among the 3 subcontractors with the highest number of Purchase Orders processed on the same day. We also selected three Purchase Orders processed on the same day to one subcontractor where it appeared that Battelle may have split a subcontract into multiple contract types. We reviewed the subcontract files to determine similarities in scope of work and what key information was known by Battelle Contracting personnel at the time of subcontract solicitation and award.

Modifications

We grouped Battelle's Purchase Orders from FY 2010 to August 8, 2015, into 3 categories: (1) Purchase Orders with 10 or more actions; (2) Purchase Orders with more than 1 action but less than 10; and (3) Purchase Orders with 1 action. For the purposes of our judgmental selection, we only considered procurement actions that included either an increase or decrease in funding (see Table 1). We judgmentally selected a total of 29 of 14,002 Purchase Orders (see Tables 1, 2, and 3) from the first 2 categories for our modifications testing based on 6 types of criteria:

1. Purchase Orders that were initially \$650,000 and under, but were modified to over \$1 million. Purchase Orders over \$650,000 would have been subject to key thresholds, such as competition requirements, sole source justifications, divisional management review, and small business requirements.
2. Purchase Orders that were over \$650,000, but were modified to over \$1 million, and therefore, may not have been subject to the approval of the Acquisition Review Board or required Contracting Officer Notification.

3. Purchase Orders that were initially under \$25,000, but were modified to over \$100,000, the threshold for completing a formal Memorandum of Procurement, but not over \$1 million.
4. Purchase Orders that were modified to over the maximum dollar amount listed in the description of the Purchase Order action.
5. Purchase Orders where the number was included the description of other Purchase Order actions, suggesting that the subcontract was managed using multiple Purchase Orders.
6. Purchase Orders that had multiple actions processed across a period greater than 5 years.

We selected 17 of 151 Purchase Orders with 10 or more actions from 5 of the criteria (see Table 2). We also judgmentally selected 12 of 13,851 Purchase Orders with more than 1 action but less than 10 from of the selection criteria (see Table 3). We reviewed the subcontract files to determine whether the selected subcontracts received the appropriate level of review and approval when they were modified.

**Table 1:
Combined Summary Data for Purchase Orders with Multiple Actions
October 1, 2009, Through August 8, 2015**

	Purchase Orders
10 or more actions	151
2 to 10 actions	13,851
1 action	21,333
Total Purchase Orders	35,335

**Table 2:
Purchase Orders with 10 or More Actions**

Selection Criteria	Purchase Orders
Initial action under \$650,000	9
Initial action over \$650,000	2
Total amount under \$1 million	2
Modified to over subcontract maximum	2
Subcontract under multiple Purchase Orders	2
Total Purchase Orders	17

**Table 3:
Purchase Orders with 2 to 10 Actions**

Selection Group	Purchase Orders
Initial action under \$650,000	4
Initial action over \$650,000	3
Total amount under \$1 million	1
Subcontract under multiple Purchase Orders	1
Actions over more than a 5-year period	3
Total Purchase Orders	12

PRIOR REPORT

Audit Report on [Subcontract Administration at Selected Department of Energy Management and Operating Contractors](#) (OAS-M-15-07, July 2015). The audit noted that nothing indicated that Kansas City and Jefferson Lab had not administered the subcontracts substantially in accordance with established policies and procedures and contract terms. However, the audit found a certain class of subcontracts had been noncompetitively awarded. Specifically, Kansas City awarded 8 of the 47 subcontracts we reviewed, or \$10.2 million of \$33.7 million in subcontracts, on a sole-source basis without specific justification. The majority of the subcontract administration issues at Kansas City occurred due to a policy providing an exception from competition in instances when a Work for Others customer required the use of a specific subcontractor. Kansas City officials stated the use of a customer-directed subcontractor without competition was permissible because Kansas City's Procurement Work Instructions (Work Instructions) allowed such action. Specifically, the Work Instructions stated that an exception to subcontract competition is allowed when a customer directed, in writing, the use of a specific subcontractor. However, the Work Instructions appear to be inconsistent with (1) Department of Energy Acquisition Regulation (DEAR) requirements in the contract, DEAR 970.5217-1, *Work for Others Program (Non-DOE Funded Work)*, which require management and operating contractors to select the subcontractor and the work to be subcontracted for Work for Others customers, and (2) Federal Acquisition Regulation 52.244 5, *Competition in Subcontracting*, and DEAR 970.5244-1, *Contractor Purchasing System*, which require the use of competition.

MANAGEMENT COMMENTS




Department of Energy
Pacific Northwest Site Office
P.O. Box 350, K9-42
Richland, Washington 99352

JUN 27 2016

16-PNSO-0288

MEMORANDUM FOR MICHELLE L. ANDERSON
ASSISTANT INSPECTOR GENERAL FOR AUDITS AND
INSPECTIONS
OFFICE OF INSPECTOR GENERAL
IG-30, HQ

FROM: ROGER E. SNYDER
MANAGER 

SUBJECT: DRAFT REPORT ON BATTELLE'S PROCUREMENT
ACTIVITIES

Thank you for the opportunity to review and comment on the subject draft report. In addition to our responses to the recommendations below, the Pacific Northwest Site Office (PNSO) disagrees that it failed to provide adequate oversight. PNSO identified Battelle's inconsistencies in its procurement activities prior to the IG performing its review and acquisition thresholds were lowered in response to PNSO's findings.

In addition, PNSO also takes exception to the sentence identified in the memorandum (Page 3, Paragraph 1, Sentence 2), in the report (Page 6, Section "Department and Contractor Oversight", Paragraph 1, Sentence 1), and in the monetary impact statement (Page 2, Paragraph 1, Sentence 5). As an alternative, the Department offers the following sentence for use: "Contributing to the weaknesses identified, Battelle management did not provide adequate oversight of its procurement activities."

Recommendation 1: In addition to the Contracting Officer's recommendations to Battelle, we further recommend the Manager, PNSO to ensure Battelle's policies and procedures are revised to address maintaining adequate official procurement files that support individual procurement actions and are consistently followed.

Management Response: Concur.

Action Plan: PNSO will direct Battelle to perform an effectiveness review of the corrective action taken to address whether or not Battelle's policies and procedures address maintaining adequate official procurement files that support individual procurement actions and are consistently followed.

Ms. M. L. Anderson
16-PNSO-0288

JUN 27 2016

2

Estimated Completion Date: July 30, 2017

Recommendation 2: We further recommend the Manager, PNSO to ensure Battelle's training on contract types and their appropriate use is adequate to provide Procurement Department personnel the skills necessary for effectively administering assigned contract actions.

Management Response: Concur.

Action Plan: PNSO will direct Battelle to perform an effectiveness review of the corrective action taken to address whether or not Battelle's training on contract types and their appropriate use is adequate to provide the Procurement Department personnel the skills necessary for effectively administering assigned contract actions.

Estimated Completion Date: July 30, 2017

Recommendation 3: We further recommend the Manager develop a plan for completing more frequent ad hoc reviews of Battelle's procurement activities in areas not covered under other assessments.

Management Response: Concur.

Action Plan: PNSO will develop and implement a plan to perform more frequent ad hoc reviews of Battelle procurement activities not covered under other assessments.

Estimated Completion Date: July 30, 2017

Recommendation 4: We further recommend the Manager, PNSO to ensure that Battelle's changes to contract file reviews adequately identify issues with file documentation and Procurement Department personnel following policies and procedures.

Management Response: Concur.

Action Plan: PNSO will direct Battelle to perform an effectiveness review of the corrective action taken to address whether or not Battelle's contract file reviews are adequately identifying issues with file documentation and Procurement Department personnel are following policies and procedures.

Estimated Completion Date: July 30, 2017

Ms. M. L. Anderson
16-PNSO-0288

JUN 27 2016

3

If you or your staff have any questions, please contact Ryan Kilbury, Contracting Officer, with Office of the Manager, at (509) 372-4030.

Attachment

cc w/attach:
T. D. Fuller, CF-12
G. Gozum, CF-12
M. W. Hayes, ORO
T. J. Pooler, ORO
J. B. Venneri, SC-41.1

FEEDBACK

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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.