Audit Report

OFFICE OF THE INSPECTOR GENERAL

SUSPENSION AND DEBARMENT REPORTING PROCEDURES FOR SUBCONTRACTORS

Report No. 93-098 May 21, 1993

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The following acronyms are used in this report.

FAR.....Federal Acquisition Regulation
GAO.....General Accounting Office

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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ARLINGTON, VIRGINIA 22202

REPORT
NO. 93-098

May 21, 1993

MEMORANDUM FOR DIRECTOR OF DEFENSE PROCUREMENT
ASSISTANT SECRETARY OF DEFENSE (PRODUCTION AND LOGISTICS)
ASSISTANT SECRETARY OF THE NAVY (FINANCIAL MANAGEMENT)
ASSISTANT SECRETARY OF THE AIR FORCE (FINANCIAL MANAGEMENT AND COMPTROLLER)
INSPECTOR GENERAL, DEPARTMENT OF THE ARMY
DIRECTOR, DEFENSE CONTRACT AUDIT AGENCY
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Audit Report on Suspension and Debarment Reporting Procedures for Subcontractors (Project No. 3CA-0003)

Introduction

We are providing this report for your information and use. The audit objectives were to determine whether the subcontractor disclosure requirement prescribed in United States Code, title 10, section 2393, as amended by section 813 of the FY 1991 National Defense Authorization Act, was effectively implemented throughout DoD and to evaluate whether related internal controls were effective. As of June 25, 1991, DoD prime contractors had to require their subcontractors (for subcontracts exceeding $25,000) to disclose, in writing, whether the subcontractors were debarred or suspended by the Federal Government from Government contracting or subcontracting.

Discussion

The audit showed that DoD was adequately implementing the requirements under U.S.C., title 10, section 2393. DoD contractors have generally established adequate internal controls that either preclude subcontract awards to debarred or suspended subcontractors or provide appropriate notification to the cognizant contracting officer. In addition, the Defense Logistics Agency periodically reviews contractor purchasing systems at major DoD contractors. The Defense Logistics Agency reviews contractor internal controls for identifying debarred and suspended subcontractors and complying with the subcontractor disclosure requirement in accordance with U.S.C., title 10, section 2393.

The audit identified one occurrence in which a contractor did not obtain the required subcontractor certifications, but we did not consider the single instance to be significant. We attribute the occurrence to the relatively short time between the effective date of the revised disclosure requirement and the award date of the pricing action.

The audit found no examples of subcontract awards to debarred or suspended contractors among the 211 subcontracts reviewed under the 20 sampled pricing actions. In general, DoD prime contractors avoided awarding subcontracts to debarred or suspended companies because such awards were considered imprudent and potentially unprofitable. In addition to requiring subcontractor written disclosure according to U.S.C., title 10, section 2393, three contractors incorporated the *Lists of Parties Excluded from Federal Procurement or Nonprocurement Programs*, published monthly by the General Services Administration into their automated purchasing systems.

Scope of Audit

Audit methodology. Our stratified sample consisted of 20 pricing actions that we selected from a universe of 8,076 actions in the DD Form 350, "Individual Contracting Action Report," database. The DD Form 350 database contained pricing actions valued at $25,000 or greater that occurred between July 1, 1991, and August 31, 1992. We included in our audit universe only those pricing actions in the DD Form 350 database that exceeded $1 million. The 20 sampled pricing actions were awarded to 17 contractors. Each contractor provided a list of subcontracts exceeding $25,000 from which we selected a second-tier judgmental sample totaling 211 subcontracts. The subcontract lists and the DD Form 350 report were the only computer-generated data on which we relied. Nothing came to our attention as a result of audit procedures that caused us to doubt the reliability of the computer-generated data. The sample of prime contracts and contract modifications was valued at $3.8 billion (6 percent) of the $62.6 billion universe.

The audit included an examination and analysis of subcontract documentation for each judgmentally selected second-tier sample item at each prime contractor. The audit also included interviews with cognizant contractor personnel, contracting officers, and other contract administration personnel; a review of contractors' written policies and procedures for internal controls; and a comparison between

subcontractors reviewed and the General Services Administration *Lists of Parties Excluded from Federal Procurement or Nonprocurement Programs*. The contractor documentation we examined was dated from October 1990 through December 1992. The activities and contractors we visited or contacted during the audit are listed in Enclosure 1.

Audit period and standards. This program audit was performed from October 1992 to March 1993, in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD. Accordingly, we included such tests of internal controls as were considered necessary.

Internal Controls

We assessed the effectiveness of the DoD internal controls related to the subcontractor disclosure requirement of U.S.C., title 10, section 2393, as implemented by Federal Acquisition Regulation (FAR) 52.209-6, "Protecting the Government's Interest when Subcontracting with Contractors Debarred, Suspended, or Proposed for Debarment." Specifically, we reviewed contractor internal controls for identifying debarred and suspended subcontractors and for ensuring compliance with the subcontractor disclosure requirement.

The internal controls applicable to identifying debarred and suspended subcontractors were effective. No material deficiencies, as defined by Public Law 97-255, Office of Management and Budget Circular A-123, and DoD Directive 5010.38, were disclosed by the audit.

Background

Section 813 of the FY 1991 National Defense Authorization Act (Public Law 101-510) directs that all DoD prime contractors require each subcontractor whose subcontract exceeds $25,000 to disclose, as of the subcontract award date, whether the subcontractor is suspended or debarred by the Federal Government from Government contracting or subcontracting. DoD implemented this requirement through a revision to FAR 52.209-6. Before the FAR revision, the prime contractor was required to certify to the Government that at the time of contract award the subcontractor was not debarred or suspended.

In cases where the Government does not have the right to approve or disapprove the contractor's selection of a subcontractor (for example, fixed-price contracts), the prime contractor is required to notify the contracting officer in writing if the contractor intends to enter into a contract with a debarred or suspended company. The notice must state the compelling reason for doing business with the subcontractor and explain the systems and procedures the contractor has established to ensure that the Government's interests will be fully protected when dealing with the debarred or suspended subcontractor.

Congress intended for Public Law 101-510, section 813, to act as a mechanism to trigger the prime contractor's requirement to notify the Government. The FY 1991 National Defense Authorization Act Conference Report required the Inspector General, DoD, to monitor the effectiveness of the revised regulation.

Prior Audit Coverage

General Accounting Office (GAO) Report No. NSIAD-87-37BR (OSD Case No. 7239), "Procurement - Suspension and Debarment Procedures," February 13, 1987, stated that "None of the agencies we reviewed have completely implemented fully effective procurement fraud coordination and oversight systems to ensure . . . ineligible contractors are not inadvertently awarded new contracts."

The GAO recommended changes to the FAR that would make debarments effective Government-wide, require all prospective contractors to certify whether they are affiliated with a suspended or debarred contractor, and extend the coverage of the regulations to include all subcontractors. The Defense Acquisition Regulations Council concurred with the recommendations and established a joint high-level working group to revise the FAR. In June 1991, the FAR was amended to incorporate GAO's recommended changes.

GAO also recommended that the FAR be amended to require that each Government contract contain a clause that states that the Government may terminate the contract for default if the contractor is debarred during the course of the contract because of criminal conviction or civil judgment for fraud in connection with any Government contract. The Defense Acquisition Regulations Council nonconcurred, stating that a clause allowing

default of existing contracts when a contractor is debarred will provide no additional protection to the Government.

Management Comments

We provided a draft of this report to the addressees on April 14, 1993. Because there were no recommendations, no comments were required of management, and none were received. Any comments on this final report should be provided by June 21, 1993.

We appreciate the courtesies extended to the audit staff. The distribution of this report is listed in Enclosure 2. If you have any questions regarding this audit, please contact Mr. Richard B. Jolliffe, Program Director, (703) 692-2999 (DSN 222-2999), or Ms. Bobbie Sau Wan, Project Manager, (703) 692-3013 (DSN 222-3013).

Edward R. Jones
Deputy Assistant Inspector General
for Auditing

Enclosures

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ACTIVITIES VISITED OR CONTACTED

Office of the Secretary of Defense

Contract Policy and Administration Directorate, Director of Defense Procurement, Washington, DC

Department of the Army

Procurement Fraud Division, Office of the Judge Advocate General, Washington, DC

Department of the Navy

Office of the Assistant Secretary of the Navy (Research, Development and Acquisition), Washington, DC
Resident Supervisor of Shipbuilding, Conversion and Repair, Intermarine USA, Savannah, GA
Supervisor of Shipbuilding, Conversion and Repair, Pascagoula, MS

Department of the Air Force

Office of the Assistant Secretary of the Air Force (Acquisition), Washington, DC

Defense Agencies

Headquarters, Defense Contract Audit Agency, Alexandria, VA
Headquarters, Defense Logistics Agency, Alexandria, VA
- Defense Contract Management Area Operations Birmingham, AL
- Defense Contract Management Area Operations Detroit, Williams International Corporation Resident Office, Walled Lake, MI
- Defense Contract Management Area Operations Orlando, FL
- Defense Contract Management Area Operations San Diego, CA
- Defense Contract Management Area Operations Seattle, WA
- Defense Plant Representative Office, General Dynamics Corporation, San Diego, CA
- Defense Plant Representative Office, General Electric Ordnance Systems Division, Pittsfield, MA
- Defense Plant Representative Office, Hughes Aircraft Company, Fullerton, CA
- Defense Plant Representative Office, Lockheed Aeronautical Systems Company, Marietta, GA
- Defense Plant Representative Office, Lockheed Missiles and Space Company, Sunnyvale, CA

ACTIVITIES VISITED OR CONTACTED (cont'd)

Defense Agencies (cont'd)

Defense Plant Representative Office, Magnavox Electronics Systems Company, Fort Wayne, IN
Defense Plant Representative Office, Stewart and Stevenson Services, Incorporated, Sealy, TX
Defense Plant Representative Office, Texas Instruments, Incorporated, Lewisville, TX

Non-Government Activities

Convair Division, General Dynamics Corporation, San Diego, CA
Data Systems Division, Litton Industries, Incorporated, Woodland Hills, CA
El Paso Refining Company, Limited, El Paso, TX
Electronics Division, Sparton Corporation, DeLeon Springs, FL
Hughes Aircraft Company, Fullerton, CA
Hughes Missile Systems Company, Incorporated, San Diego, CA
Hyster Company, Portland, OR
Ingalls Shipbuilding Company, Incorporated, Pascagoula, MS
Intermarine USA, Savannah, GA
International Technology Corporation, Slidell, LA
Lockheed Aeronautical Systems Company, Marietta, GA
Lockheed Missiles and Space Company, Sunnyvale, CA
Pentastar Electronics, Incorporated, Huntsville, AL
Science Applications International Corporation, San Diego, CA
Stewart and Stevenson Services, Incorporated, Sealy, TX
Texas Instruments, Incorporated, Lewisville, TX
Williams International Corporation, Walled Lake, MI