

# Audit

# Report



## FINANCIAL AND COST ASPECTS OF OTHER TRANSACTIONS

Report Number 98-191

August 24, 1998

Office of the Inspector General  
Department of Defense

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### **Acronyms**

|       |                                            |
|-------|--------------------------------------------|
| CECOM | Army Communications - Electronics Command  |
| DARPA | Defense Advanced Research Projects Agency  |
| DDP   | Director, Defense Procurement              |
| DCMC  | Defense Contract Management Command        |
| DDR&E | Director, Defense Research and Engineering |



INSPECTOR GENERAL  
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August 24, 1998

MEMORANDUM FOR DIRECTOR, DEFENSE RESEARCH AND ENGINEERING  
DIRECTOR, DEFENSE PROCUREMENT  
ASSISTANT SECRETARY OF THE AIR FORCE  
(FINANCIAL MANAGEMENT AND COMPTROLLER)  
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING  
SERVICE  
DIRECTOR, DEFENSE LOGISTICS AGENCY  
AUDITOR GENERAL, DEPARTMENT OF THE ARMY

SUBJECT: Audit Report on Financial and Cost Aspects of Other Transactions  
(Report No. 98-191)

We are providing this final report for review and comment. This is the first of two audit reports concerning the DoD use of "other transactions." We considered comments from the Director, Defense Research and Engineering; the Director, Defense Procurement; the Army; the Air Force; the Defense Finance and Accounting Service; and the Defense Logistics Agency on a draft of this report in preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. We request the Director, Defense Research and Engineering, provide comments that identify the date of the planned action in response to Recommendations 1.b., 1.d., 1.g., 1.h., and 2. We also request the Director, Defense Procurement, provide additional comments that identify the date of planned action on Recommendations 2. and 3.a., 3.b., 3.d., and 3.e., and provide comments on Recommendation 3.c. The Army is requested to provide additional comments on Recommendation 5. All additional comments should be provided by October 23, 1998. The Defense Finance and Accounting Service provided comments to the draft report and as a result of those comments, we deleted the recommendation addressed to them.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Raymond A. Spencer at (703) 604-9071 (DSN 664-9071) or Mr. Roger H. Florence at (703) 604-9067 (DSN 664-9067). See Appendix D for the report distribution. The audit team members are listed inside the back cover.

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## Office of the Inspector General, DoD

Report No. 98-191  
(Project No. 7AB-0051)

August 24, 1998

### Financial and Cost Aspects of Other Transactions

#### Executive Summary

**Introduction.** This audit was a joint audit effort involving the Inspector General, DoD, and the Defense Contract Audit Agency. The Inspector General, DoD, had overall cognizance for this audit. Also, personnel from the Defense Research and Engineering, Defense Procurement, Defense Advanced Research Projects Agency, and the Defense Contract Management Command participated in this audit and contributed to its positive outcome. This is the first of two audit reports concerning the DoD use of "other transactions." This report discusses the DoD administration of "other transactions." The second audit report will discuss the review of costs charged to the agreements by the "other transaction" participant(s).

"Other transactions" are instruments other than contracts, grants, and cooperative agreements that are used to stimulate, support, or acquire research or prototype projects. "Other transactions" were authorized as instruments to be used to reduce barriers to participation of commercial firms in DoD research, thereby contributing to a broadening of the technology and industrial base available to the DoD and fostering new relationships and practices with the technology and industrial base that support national security. "Other transactions" are generally not subject to statutes or regulations associated with contracts, grants, and cooperative agreements.

The authority to use "other transactions" for research projects is in Section 2371 of Title 10, United States Code, "Research Projects: Transactions Other Than Contracts and Grants."

Section 845 of the National Defense Authorization Act for Fiscal Year 1994 augmented the "other transactions" authority to allow prototype projects to be developed that are directly relevant to weapons or weapons systems for the Defense Advanced Research Projects Agency. This authority was expanded to the Military Departments. "Other transactions" for prototype authority is scheduled to end on September 30, 1999.

For the period of fiscal years 1990 to 1997, the Department issued 210 "other transaction" and prototype agreements valued at about \$3.4 billion.

**Audit Objectives.** The overall audit objective was to evaluate the financial and cost aspects of "other transactions." Specifically, the audit evaluated the administration of "other transactions" for research and prototypes by the Defense Advanced Research Projects Agency, Army Communications - Electronics Command, the Air Force Wright Laboratory, and the Defense Contract Management Command. We also evaluated the adequacy of management controls related to "other transactions" at the Army Communications - Electronics Command, the Air Force Wright Laboratory, and the Defense Contract Management Command centers in Seattle and Syracuse.

**Audit Results.** Administration of "other transactions" for research and prototypes was improving and was generally adequate for 77 "other transactions" reviewed, valued at \$1.7 billion, issued during fiscal years 1992 through 1997. However, the Army, the Air Force, and the Defense Contract Management Command need to improve their management controls relating to the administration of "other transactions." As a result, DoD officials did not have all the information necessary to adequately monitor "other transactions," did not adjust milestone payments when necessary, forfeited interest, and did not receive information necessary to preclude duplicating research. Finally, the Directors, Defense Research and Engineering and Defense Procurement, did not establish quantifiable performance measures to determine the costs and benefits resulting from the use of "other transactions."

**Summary of Recommendations.** We recommend that the Directors, Defense Research and Engineering and Defense Procurement, issue policy guidance to improve research and prototype performance reporting, to require maintenance of DoD funds in interest bearing accounts and prohibit the reinvestment of interest from DoD funds into the research programs, and establish quantifiable performance measures for "other transactions." We recommend that the Army Communications - Electronics Command require submission of research status reports. We also recommend that the Commanders for the Army Materiel Command and the Air Force Materiel Command and the Director, Defense Logistics Agency, include "other transactions" in the management control programs.

**Management Comments.** The Directors, Defense Research and Engineering and Defense Procurement concurred and will issue policy to comply with the intent of the recommendations. The Office of the Assistant Secretary of the Army (Research Development and Acquisition) partially concurred with the two recommendations addressed to the Army. However, the Army believed it was premature to include the "other transactions" in the management control program until the Office of the Secretary of Defense level policy was issued. The Air Force and the Defense Logistics Agency concurred with the recommendation addressed to their organizations. Management comments are discussed in Part I and the complete text of management comments is in Part III.

**Audit Response.** Comments from the Directors, Defense Research and Engineering and Defense Procurement, were responsive to the intent of the recommendations but did not identify when all actions would be accomplished. In addition, the Director, Defense Procurement, needs to provide comments on the recommendation requiring the maintenance of DoD funds in interest-bearing accounts. Comments provided by the Assistant Secretary of the Army (Research Development and Acquisition) satisfied one of two recommendations. The Assistant Secretary is requested to reconsider when to include "other transactions" in the management control program. All management comments to this report are requested by October 23, 1998.

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## **Part I - Audit Results**

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## Audit Background

**History.** "Other transactions" are instruments other than contracts, grants, and cooperative agreements that are used to stimulate, support, or acquire research or prototype projects. "Other transactions" were authorized to reduce barriers to commercial firms in DoD contracting for research, to contribute to a broadening of the technology and industrial base available to the DoD, and to foster new relationships and practices with commercial technology and industrial base firms that support national security. "Other transactions" remove many of the acquisition regulation normally established for contracts or grants, including the Federal Acquisition Regulation, Defense Federal Acquisition Regulation Supplement, and cost accounting principles.

In 1989, Congress enacted Title 10, United States Code, Section 2371 (Title 10 U.S.C. 2371) authorized the use of "other transactions" for basic, applied, and advanced research projects. Title 10 U.S.C. 2371, "Research Projects: Transactions Other Than Contracts and Grants," was enacted as a 2-year pilot effort for the Defense Advanced Research Projects Agency (DARPA). The National Defense Authorization Act for FY 1992 broadened the authority to the Military Departments and made it permanent. In issuing an "other transactions," the Military Departments and Defense agencies must ensure that DoD funding of the research does not exceed that provided by the non-Government parties to the maximum extent practical, and that the research should not duplicate research already performed. "Other transactions" are usually issued to a consortium consisting of private companies, not-for-profit agencies, universities, and Government organizations. "Other transactions" may be used when a standard contract, grant, or cooperative agreement is not feasible or appropriate.

The National Defense Authorization Act of FY 1994, Section 845, augmented the "other transactions" authority and allowed prototype projects directly relevant to weapons or weapon systems to be issued. Section 845 was a 3-year pilot authority allowing DARPA to use "other transactions" for prototype projects. Later, the National Defense Authorization Act of FY 1997, Section 804, broadened the authority to the Secretaries of the Military Departments and other officials designated by the Secretary of Defense. Section 804 also extended the authority to September 30, 1999. "Other transactions" for prototypes does not require cost sharing by the research participant(s), must be awarded using competitive procedures, and may be used even when a traditional contract would be feasible or appropriate.

**Management of "Other Transactions."** The DARPA contracting office plans, negotiates, issues, and administers "other transactions" to support the DARPA mission. The Military Departments or research laboratories also administer some of DARPA "other transactions." In January 1995, DARPA began a pilot project with the Defense Contract Management Command (DCMC) to use DCMC offices to administer the agreements. Initially, DCMC Seattle was the center responsible for administering "other transactions" for DARPA.

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DCMC Seattle administrative responsibilities include authority to modify agreements, revise payable milestones, monitor financial aspects, administer payments, negotiate changes, monitor property acquired with Government funds, monitor agreement progress, and to ensure receipt of research progress reports. DARPA considered the administrative efforts on "other transactions" by DCMC Seattle a success. Later, DCMC expanded the administrative responsibilities to three additional centers (DCMC Syracuse, DCMC San Diego, and DCMC Atlanta) and encouraged the Military Departments to assign administrative responsibility for "other transactions" that they issued to the centers.

**Department Guidance for Using "Other Transactions."** DoD responsibility for issuing guidance in the use of "other transactions" is divided as to whether the principal purpose of the agreement is to provide support or assistance or to acquire goods or services. The Director, Defense Research and Engineering (DDR&E), is responsible for "other transactions" guidance for research. The Director, Defense Procurement (DDP), is responsible for "other transactions" guidance for acquiring prototypes.

**Research "Other Transactions."** In 1994, the DDR&E issued interim guidance to the Military Departments and DARPA on using research "other transactions." The DDR&E updated the 1994 draft guidance for "other transactions" in December 1997 and March 1998 as a result of legislative changes and lessons learned by using the agreements. In the revised guidance, the DDR&E established a new class of assistance instruments called "technology investment agreements," which includes types of "other transactions" and cooperative agreements used by DARPA and the Military Departments to increase participation of commercial firms in DoD research. The policies and procedures in the 1994 DDR&E guidance are applicable to the "technology investment agreements."

**Prototype "Other Transactions."** The guidance issued for Section 845 "other transactions" for prototypes is an Under Secretary of Defense for Acquisition and Technology memorandum on December 14, 1996, "10 U.S.C. (United States Code) 2371, Section 845, Authority to Carry Out Certain Prototype Projects." The memorandum states that the Directors of the Defense agencies have the authority to use Section 845. The memorandum also states that, to the maximum extent practicable, competitive procedures will be used to award a Section 845, the applicability of particular statutes or regulations is limited in prototype "other transactions," and good business sense and appropriate safeguards must be incorporated. The memorandum also listed statutes that may not necessarily apply to Section 845 "other transactions." DDP also issued guidance in October 1997 on the assignment of agreement identification numbers and collection of data for Section 845 "other transactions."

**Administering "Other Transactions."** Either the Military Department or a Defense agency administers "other transactions" for research or prototypes or the administration is delegated to the DCMC. In the Military Departments and Defense agencies, administering an "other transaction" is a team effort that includes the contracting officer, a buyer, and a Government technical representative. At DCMC, an agreements administrator under the authority of

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the administrative contracting officer administers "other transactions," which includes participating in program reviews, monitoring receipt of quarterly reports, monitoring cost sharing where applicable, processing agreement modifications, processing payments, monitoring and controlling property acquired with project funds, and processing agreement close-outs. The technical representative monitors the technical aspects of the research or prototype effort while the agreement administrator monitors the nontechnical aspects. DCMC Seattle is developing an "Other Transactions Handbook" to provide guidance in administering agreements.

Administering "other transactions" is different from administering traditional contracts or grants because "other transactions" have unique elements, which include cost sharing, whenever practical, and a mutual interest in the research subject by DoD and the research participants. Because of their unique elements, "other transactions" may even be different from each other. "Other transactions" for research are different from contracts for research because the "other transaction" supports and stimulates research efforts as opposed to acquiring research services. Administering "other transactions" for research includes monitoring the research effort through quarterly status reports, monitoring research expenditures, processing research payments to the lead participant, and ensuring receipt of final research technical reports.

Administering an "other transaction" for a prototype differs from research in that cost sharing is not required, it usually involves one participant instead of a group of participants, payments may be based on cost instead of a predetermined payment schedule, and final reports may not be required. When the prototype "other transaction" effort is complete, the prototype may be delivered to the Government.

**Use "Other Transactions."** The Military Departments, DARPA, and Defense agencies use "other transactions" for both research (10 U.S.C. 2371) and prototypes (Section 845), as shown in the following table.

**Table 1. Research and Prototype Agreements Issued by the Department**

|                     | FY 1995     |                      | FY 1996     |                | FY 1997     |                       |
|---------------------|-------------|----------------------|-------------|----------------|-------------|-----------------------|
|                     | <u>2371</u> | <u>845</u>           | <u>2371</u> | <u>845</u>     | <u>2371</u> | <u>845</u>            |
| Army                | 0           | 0                    | 10          | 0              | 1           | 10                    |
| Navy                | 0           | 0                    | 5           | 0              | 1           | 20                    |
| Air Force           | 0           | 0                    | 2           | 0              | 1           | 8                     |
| DARPA               | 34          | 6 <sup>1,2</sup>     | 19          | 8 <sup>1</sup> | 17          | 4 <sup>2</sup>        |
| NIMA <sup>3</sup>   | <u>0</u>    | <u>0</u>             | <u>0</u>    | <u>0</u>       | <u>0</u>    | <u>3</u>              |
| <b>Total</b>        | <b>34</b>   | <b>6<sup>2</sup></b> | <b>36</b>   | <b>8</b>       | <b>20</b>   | <b>45<sup>2</sup></b> |
| Value<br>(millions) | \$570.3     | \$181.9              | \$430.7     | \$55.2         | \$145.3     | \$405.0               |

<sup>1</sup>DARPA was the only agency within DoD that had the authority to issue "other transactions" for prototypes until FY 1997.

<sup>2</sup>Section 845 efforts that had multiple phases were not counted as separate agreements in this report. FY 1995, DARPA had one phased effort for a total of seven agreements versus the six shown in the table total. For FY 1997, DARPA had 3 phased efforts and NIMA had 2 phased efforts for a DoD total of 50 agreements versus the 45 shown.

<sup>3</sup>National Imagery and Mapping Agency.

## Audit Objectives

The overall audit objective was to evaluate the financial and cost aspects for "other transactions." Specifically, this audit evaluated the administration of "other transactions" for research and prototypes by DARPA, the Army Communications - Electronics Command (CECOM), Air Force Wright Laboratory, and DCMC. We also evaluated the adequacy of management controls related to "other transactions" at the CECOM, Wright Laboratory, and the DCMC centers at Seattle and Syracuse. We did not review "other transactions" issued by the Navy or Defense agencies because of the limited number of "other transactions" that they issued at the time of our audit selection. Appendix A describes the audit scope and methodology, and identifies two prior audits that address "other transactions."

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## **Administering Other Transactions**

The DoD administration of "other transactions" for research and prototypes generally has been adequate. However, the Army, the Air Force, and the Defense Contract Management Command need to improve their management controls. This condition exists because guidance was insufficient for administering "other transactions," and management did not devote sufficient attention to develop a process to quantify the benefits from using "other transactions." As a result, DoD officials did not have the information necessary to adequately monitor "other transaction" efforts, did not adjust milestone payments when necessary, forfeited interest, and did not receive information necessary to preclude duplicating research. Finally, the Directors, Defense Research and Engineering and Defense Procurement, did not establish quantifiable performance measures to determine the costs and benefits resulting from using "other transactions."

### **Summary of Audit Results**

The audit judgmentally selected and examined 77 "other transactions" reviewed, valued at \$1.7 billion, issued during FYs 1992 through 1997. The 77 "other transactions" included 60 agreements for research and 17 agreements for prototypes. DARPA, CECOM, Air Force Wright Laboratory, and DCMC centers administered the 77 "other transactions." Details are in Appendix B. The following table summarizes the audit results by 10 U.S.C. 2371 (research) and Section 845 (prototype). The details are in Appendix C.

**Table 2. Summary of Audit Sample Results**

|                                                     | <u>Number of Occurrences</u> |                  | <u>Percent of Occurrences</u> |                  |
|-----------------------------------------------------|------------------------------|------------------|-------------------------------|------------------|
|                                                     | <u>Research</u>              | <u>Prototype</u> | <u>Research</u>               | <u>Prototype</u> |
| Reports on hand                                     |                              |                  |                               |                  |
| o Technical                                         | 52 of 58                     | 17 of 17         | 89                            | 100              |
| o Business                                          | 48 of 56                     | 16 of 16         | 86                            | 100              |
| Business status reports submitted that show cost by |                              |                  |                               |                  |
| o Participant                                       | 42 of 48                     | 16 of 16         | 88                            | 100              |
| o Task                                              | 23 of 42                     | 13 of 16         | 55                            | 81               |
| Annual program plan submitted                       | 35 of 57                     | 4 of 6           | 61                            | 66               |
| Interest provision in agreement                     | 6 of 60                      | 0 of 11          | 10                            | 0                |
| Modification in files                               | 40 of 40                     | 2 of 2           | 100                           | 100              |
| Invoices properly certified                         | 59 of 60                     | 17 of 17         | 98                            | 100              |
| Research effort complete and final report submitted | 4 of 21                      | 0 of 0           | 19                            | 0                |

## Monitoring Performance

Government technical representatives and administrative officials monitor research and prototype efforts by attending program management reviews and annual meetings, by continuing discussions with research participants, and by reviewing technical and business status reports. DARPA, CECOM, and Wright Laboratory issue "other transaction" agreements that usually require technical and business status reports on a quarterly basis. Although the participants generally submitted the quarterly reports for both research and prototype "other transactions," the quarterly reports for research were late or did not provide the required expenditure information.

**Technical Status Reports.** Government technical officials use the quarterly technical status reports as a tool to monitor research. The technical status reports provide information on developments, report problems, and identify technical issues or major developments. Technical reports also provide a documented record, which is necessary if the Government technical representative is reassigned. Quarterly reports were required for 58 research and 17 prototype "other transaction" agreements (Appendix C). For research "other transactions," 52 of the 58 agreements reports were submitted as required. Therefore, six "other transactions" for research did not have the required quarterly report submitted as required. In addition, of the 52 research "other transactions" that had reports submitted, 5 agreement reports were submitted more than 3 months late. All the reports were submitted for the prototype "other transactions."

An example of late technical reports concerns an agreement that Wright Laboratory administered for DARPA. The \$14.8 million DARPA research "other transaction" No. MDA972-94-3-0016 required developing high-performance analog optoelectronic modules. The DARPA agreement was a two-phased research effort that required the consortia to submit quarterly

## Administering Other Transactions

technical reports to the Government technical officials at the Wright Laboratory. The consortium submitted late reports during both phases of the research effort. For Phase Two, the consortium combined the quarterly reports into one submission.

An example of what to do if a technical report was not submitted was illustrated in an agreement that DCMC Seattle administered. DCMC Seattle was responsible for monitoring a \$7.9 million DARPA MicroModule Systems research "other transaction" No. MDA972-96-3-0002 to develop industry-standard high-performance embedded processor applications. The consortium had not submitted the technical or business status reports required in the agreement. The agreement administrator requested the reports from the consortium lead but was unsuccessful; therefore, the agreement administrator informed the consortium program manager that future invoices would not be paid until he received the reports.

**Business Status Reports.** The research participant submits quarterly business status reports to the technical representative and the agreement administrator to assist them in monitoring the status of the research or prototype efforts. The "other transaction" agreements require the research participant to summarize expenditures of all the participants in a business status report. The business status reports require quarterly status expenditures as outlined in the Annual Program Plan, with an explanation of major expenditure deviations and a discussion of any necessary adjustments. Quarterly business status reports were required for 56 research and 16 prototype "other transaction" agreements (Table 2). Business status reports were submitted for 48 of the 56 research agreements and for all 16 prototype agreements. The 48 research "other transactions" that had business status reports submitted, 3 research agreements had reports submitted more than 3 months late.

The absence and untimely receipt of business status reports inhibit the agreement administrators' monitoring efforts in relation to the Annual Program Plan and identifying potential problems. For example, DARPA agreement No. MDA972-94-3-0033 was a \$14.2 million effort with DARPA providing \$5.7 million. The research participant effort was a two-phased joint effort with six private-sector businesses providing different amounts of cost sharing for the next generation of high-speed communications networks. Although the Phase One effort began in 1994, the later stages of Phase One research occurred at the same time that the Phase Two research efforts began. Both Phase One and Phase Two business status reports were submitted as much as 9 months late and combined quarterly reports for multiple quarters. As a result, the agreement administrator did not receive the information necessary to effectively monitor expenditures, and precluded the reports from being used as a tool in monitoring the research progress.

CECOM issued an "other transactions" for research that did not always require quarterly business status reports. Of the six "other transactions" issued by CECOM, three did not require business status reports. For example, CECOM issued a \$2.6 million "other transaction" No. DAAB07-96-3-J017 for research on mass production of low-cost optical systems. CECOM and four private-sector businesses shared the cost of the research effort. Although the CECOM agreement required quarterly technical status reports, it did not require quarterly

business status reports. After the research effort began, the Government technical representative requested the CECOM contracting officer to modify the "other transaction" to identify costs associated with specific research tasks.

The three CECOM agreements did not require quarterly business status reports because the contracting officer believed they were unnecessary and that DDR&E policy did not require them. DARPA and Wright Laboratory "other transaction" agreements have always required the consortium to submit quarterly business status reports.

Wright Laboratory administered a DARPA research "other transaction" No. MDA972-93-2-0007, valued at \$9.6 million, to develop ceramic matrix composite components. The DARPA research agreement require quarterly business status reports; however, the consortium did not submit them for the research effort. Wright Laboratory officials did not enforce the requirement because they were not monitoring the cost associated with the research effort.

Government technical representative and administrative officials need timely quarterly technical and business status reports to effectively monitor research and prototype progress. The quarterly reports provide a history of the progress and help identify problem areas. The contracting officer and administrative official should continue to encourage the timely receipt of quarterly reports; however, if unsuccessful, the administrative contracting officer should withhold milestone payments to the participant(s). In addition, CECOM should require quarterly status reports for all "other transactions."

## Expenditure Reporting

Participants did not always report costs adequately. Of the 48 research "other transactions" that submitted business status reports, 42 reported costs by individual participant. Of the 42 research agreements, 23 reported costs by task or milestone. The business status reports assist in monitoring the financial performance of participant(s) and ensure that financial obligations of the participant(s) are met. In addition, business status reports assist the agreement administrator to identify expenditure underruns and overruns at different phases of the effort in relation to the expenditure plan for individual tasks.

Expenditure reporting by the individual participant and task is important when multiple participants are conducting the research effort and when reimbursements to individual participants are based on task accomplishments. Because of the nature of the effort, tasks may move, requiring adjustments to the milestone payment schedule. The agreement administrator needs to monitor expenditures associated with research "other transactions" because the DoD contributions should not exceed the cost ratio in the agreement when the research effort nears completion. Monitoring expenditures is less important for prototype agreements because they usually have one participant and do not require cost sharing.

**Expenditure Reporting.** To monitor expenditures, agreement administrators need participants to report expenses by participant and task. Expenditure reporting for the 48 research agreements that submitted business status reports

## **Administering Other Transactions**

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encompassed a wide spectrum, including reporting milestone payments as actual expenses, reporting expenditures at the consortia total, reporting expenditures by only research participant, and reporting expenditures by research participant and task. For example, CECOM issued research "other transaction" No. DAAB07-96-3-D759 to develop Digital Wireless Communications and Networking Systems, and the cost reporting was inadequate to monitor expenditures. The CECOM agreement was an equal cost sharing of the \$2.8 million effort between CECOM and the consortium. The consortium, composed of four private-sector companies, submitted two business status reports for a 12-month period and reported the CECOM payment values in both reports were costs incurred for conducting the research. The agreement states that the business status reports should include a quarterly reporting of current expenditures as outlined in the Semi-Annual Plan with major deviations explained along with discussions of the adjustment actions proposed. The consortium's reporting of the CECOM payments as current expenditures did not comply with the agreement, and CECOM could not determine the actual costs of the research effort.

Insufficient cost reporting was also illustrated in an agreement in which business status reports combined actual expenditures and DARPA funding. The "other transaction," No. MDA972-94-3-0016, administered by Wright Laboratory, was to develop an Analog Optoelectronic Module. The DARPA agreement required equal cost sharing of \$14.8 million with six research participants. Although the consortium lead reported quarterly expenditures to Wright Laboratory, the business status reports showed that some participants reported actual expenditures while other participants reported the DARPA payments as their research costs. Research participants who report DARPA payments as research expenditures inhibit the administrators in accomplishing their responsibility to monitor expenditure underruns or overruns.

Without sufficient expenditure reporting, agreement administrators cannot effectively monitor the actual cost of research efforts and, therefore, cannot ensure that research efforts are progressing adequately and that research participants are satisfying their cost-share responsibilities. Because prototype "other transactions" usually involve only one participant, reporting at the participant level was sufficient.

**DCMC Module for Expenditure Reporting.** DCMC Seattle developed a module to report participant expenditures for "other transactions." The Seattle module required quarterly expenditure reporting by research participant, by task or milestone, and by type of expenditure (cash or non-cash). The Seattle module also required identifying expenditure variances in relation to the program plan with an explanation for the cause of the variance. The DCMC Seattle encouraged participants to report expenditures according to the module because Seattle believed that they needed detailed information to effectively administer the agreements.

DARPA conducted periodic assessments of DCMC Seattle's administration of "other transactions" and concluded that DCMC Seattle was conducting an effective program. However, DARPA issued an assessment report stating that DCMC Seattle needed to obtain better information on consortia expenditures.

The DARPA assessment report stated that the DCMC Seattle expenditure module represents the necessary expenditure reporting and tracking needed to effectively monitor the research efforts.

Participant cost reporting has generally not been sufficient to properly monitor research costs. The participant should report expenditures at the research participant, milestone, or task level, and the participant should compare expenditures with the annual program plan to identify variances. We agree with the DARPA assessment of the DCMC Seattle expenditure module, and agree that DDR&E should require the module to be incorporated in "other transaction" agreements with DARPA, the Military Departments, and other Defense agencies. "Other transactions" for prototypes generally involve one participant, and detail cost reporting at the task level may not be appropriate for that type of agreement.

### Adjusting Payable Milestones

The agreement administrators were not adjusting the reimbursement schedules when reimbursement payments exceeded research expenditures. DARPA, CECOM, and Wright Laboratory established payable milestones to reimburse research participants for achieving preestablished technical milestones. DCMC Seattle established criteria that state that when payable milestone schedules exceed actual expenditures by 10 percent, the agreement administrator should reevaluate the agreement for potential payment adjustments. The agreement administrators did not take timely action when payable milestones exceeded the actual research expenditures. For example, DARPA issued "other transaction" No. MDA972-95-3-0004 to conduct research in holographic data storage collections systems. The DARPA agreement, valued at \$32.2 million, required equal cost sharing between DARPA and the consortium. DARPA assigned the agreement administration to DCMC Seattle in October 1995.

Milestone payments to the consortium exceeded actual expenditures for five of seven quarters beginning in December 1995, and the unspent balance steadily increased from \$68,000 to more than \$1 million. However, DCMC Seattle did not take action on the excess payments until April 1997, when the actual costs were 30 percent below the total amount of reimbursement. The agreement administrator requested the consortium to explain the cause of the variance and requested the consortium to submit a revised expenditure plan. Agreement administrators need to take more concerted action to evaluate adjusting payable milestones when excess DoD milestone payments exceed expenditures. The DoD Grant and Agreement Regulations require that research advance payments be limited to the minimum amounts needed to carry out the program. The preceding example identifies an agreement in which the milestone payment schedule exceeded the research expenditures, and the agreement administrator needed to review the milestone payment schedule. However, as reported in the section on "Expenditure Reporting" the agreement administrators do not always have the detail expenditure information to conduct comparisons of payable milestone values to research or prototype expenditures.

### Annual Program Plan

DARPA, CECOM, and Wright Laboratory "other transaction" agreements generally require the participant to submit an Annual Program Plan (the Plan) to the Government technical representative for research and prototype efforts. The Plan provides a detailed schedule of research or prototype activities, outlines how the agreement participant(s) will meet specific performance objectives, forecasts expenditures, and describes payable milestones. The Plan consolidates all prior adjustments in the research or prototype schedule, including revisions and modifications to the agreement. Research and prototype participants did not always submit the Plan as required. For 57 research agreements that required submission of the Plan, participants submitted the Plan for 35 agreements. For the six prototype agreements that required the Plan, participants submitted the Plan for four agreements. Therefore, research participants did not always comply with the terms of the agreement.

Although the Plan is a useful management tool, the DARPA "other transactions" agreements did not require participants to submit the Plan to the agreements administrator responsible for monitoring the efforts. DARPA delegated the administrative responsibility of 42 "other transactions" to either CECOM, Wright Laboratory, or DCMC. Of the DARPA agreements for research or prototypes, 41 agreements required the submission of the Plan; however, none of the agreements required submission of the Plan to the organization responsible for administering the agreement. CECOM, Wright Laboratory, and DCMC personnel obtained the Plan for 24 of the 41 agreements through their own initiative. The agreement administrator would be able to monitor the research more effectively if participants were required to submit the Plan to the responsible organization.

DARPA retained the administration for 28 "other transactions," and 17 of the research and prototype agreements required participants to submit the Plan. Examination of DARPA files showed that DARPA had the Plans for 12 of 17 agreements. DARPA administration of the agreements was inhibited by not having the Plans to use as a historical record of technical achievements.

### Interest Income

The Inspector General, DoD, Report No. 97-114, "Award and Administration of Contracts, Grants, and Other Transactions Issued by the Defense Advanced Research Projects Agency," March 28, 1997, identifies that "other transaction" agreements did not require consortium leads to maintain Government funds in interest-bearing accounts before disbursement to the research participants. For 11 "other transactions," the consortium earned \$1.9 million in interest on Government funds. In response to our recommendation, the Director, Defense Research and Engineering (DDR&E), agreed to establish policy for research "other transactions" requiring the use of interest-bearing accounts whenever practical. Contracting officers included the interest provision in 6 of 60 research "other transactions" and in none of the 11 prototype "other transactions" using payable milestone schedules. In addition, research

participants reinvested interest in the research efforts, and agreement administrators did not examine consortia claims that retaining Government funds in an interest-bearing account would be ineffective.

**Interest Income Reinvestment.** The research participants reinvested interest on excessive DARPA milestone payments in the program for four DARPA "other transactions." Earning interest by participants on milestone payments is contrary to the goals of the "other transaction" in providing assistance in the accomplishment of research. In addition, allowing the reinvestment of the interest into the research effort is in conflict with a DDR&E recommendation in response to Report No. 97-114 that requires the participant to submit interest to the U.S. Treasury. For example, DARPA issued "other transaction" No. MDA972-92-2-0007 for research in developing fiber technology composites use with gas turbine engine components. The agreement was for \$13 million, with DARPA funding \$6.7 million. DCMC Syracuse, as the administrator of the agreement, identified that the consortium deposited DARPA milestone payments in an interest-bearing account. DCMC Syracuse determined that the interest earned on the excess milestone payments was more than \$391,000. In addition, DCMC Syracuse found that research participants had not contributed their required cost share because the DARPA payments satisfied all of the research expenditures.

Another DARPA "other transaction," No. MDA972-93-2-0008, valued at \$9.2 million and administered by DCMC Syracuse, required research in new high-performance composites material technology. DARPA agreed to equal sharing of the research costs with DARPA payments made by quarterly milestone payments. DCMC Syracuse identified that the consortium maintained DARPA payments in an interest-bearing account that earned \$221,000 in interest. The consortium reinvested the interest into the research program.

**Noninterest-Bearing Accounts.** DCMC agreement administrators allowed consortia to deposit DARPA milestone payments into noninterest-bearing accounts based on consortium statements that interest-bearing accounts would not be cost-effective. For example, DARPA "other transaction" No. MDA972-95-3-0029 was for developing the high-resolution and color thin film electroluminescent displays. The \$29.2 million agreement with equal cost share was changed by DCMC Seattle officials who required Government funds to be deposited in an interest-bearing account. The DCMC Seattle official later allowed the use of a noninterest-bearing account when the consortium claimed that bank fees would offset any interest earned. However, the consortium cash flow statements submitted to DCMC Seattle showed that interest earned exceeded the bank fees charged. Interest of \$9,000 was earned and submitted to the U.S. Treasury. Discussion with the DCMC Seattle agreement administrator identified that the administrator did not examine the consortium bank fee claim before allowing it to use the noninterest-bearing account.

Although DDR&E plans to issue policy requiring that DoD funds are maintained in an interest-bearing account, DDR&E needs to issue additional guidance that prohibits reinvesting the interest earned on DoD funds into research programs. Although we did not identify that condition with the prototype "other transactions," 11 of 17 prototype agreements used milestone payment schedules. Those 11 prototype agreements did not contain an interest

## **Administering Other Transactions**

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provision. Therefore, the Director, Defense Procurement, should also issue policy for prototype "other transactions" using payable milestone schedules that the participant deposit the DoD payments in an interest-bearing account and submit the interest to the U.S. Treasury. The additional policy is needed because Military Departments and Defense agencies are also using of "other transactions" for research and prototypes.

## **Proposal Evaluations**

DDR&E did not require DCMC agreement administrators to review cost proposals associated with potential "other transaction" awards, although its benefits were demonstrated in a DARPA negotiated "other transaction" issued in 1995. In that agreement with the Giant Magnetoresistance Consortium, DARPA contracting officials negotiated for research and development for magnetic materials and devices having giant magneto resistance. The DARPA agreement No. MDA972-95-3-0014, valued at about \$12.2 million, required equal cost sharing among DARPA and the research participants. DCMC Syracuse monitored the effort in August 1996. To better understand the research effort, DCMC Syracuse agreement administrators reevaluated the cost proposal and found that it included profit from the four research participants that totaled \$501,945. The DARPA award of profit is not appropriate in a cost-share agreement, and during the audit, DCMC Syracuse officials discussed the profit with DARPA and the research participants to resolve the issue. DDR&E still needs to issue guidance to prohibit the award of profit for "other transactions."

## **Agreement Modifications**

DARPA was properly distributing "other transaction" modifications to the agreement administrators. DARPA issues agreement modifications to satisfy a variety of agreement changes, including scope-of-work revisions, changes in research participants or level of participation, and changes in agreement funding or cost share. Distributing agreement modifications to the agreement administrators is necessary for proper administration. The DARPA and agreement administrator files for 42 "other transactions" for research and prototypes delegated to CECOM, the Wright Laboratory, and DCMC had the modifications to administer the agreements.

## **Invoice Certifications**

Government technical representatives properly certified invoices for research and prototype agreements before the agreement administrator approved payment. The research or prototype participant submits an invoice to the agreement administrator requesting payment for completion of a technical effort. The agreement administrator requires certification from the Government

technical representative for payment approval, based on satisfactory technical accomplishment. For the 77 "other transactions" reviewed, the Government technical representative certified most of the invoices for payment before they were approved by the agreement administrator. When Government technical representative approval was not evident, the agreement administrator did not retain the approval documentation. However, one research agreement had two invoices that the Government technical representative had not certified before payment.

### Final Research Reports

Research participants are required to submit a final research report to the Government technical representative and to the Defense Technical Information Center (the Center). The final report discloses all major developments during the research effort. Research participants are required to submit final reports to the Center because the Center acts as the central depository for DoD-funded technical efforts. DoD procurement organizations must query the Center's depository before they initiate an acquisition to avoid unnecessarily duplicate scientific and engineering efforts. The Center received only 4 of the 21 final research reports.

For example, DARPA entered into "other transaction" No. MDA972-93-2-0003, to develop an advanced manufacturing process for vibration control devices for defense and nondefense applications. The DARPA agreement value was \$9.9 million, with the DARPA contribution being \$4.7 million. DCMC Seattle was assigned responsibility for administering the agreement in October 1995 as the research effort neared completion. As of October 1997, the lead research participant had not submitted the final report, and the research group has disbanded. Although DCMC Seattle was withholding the remaining \$70,000 of the total \$4.7 million DARPA payment to encourage the lead research participant to submit the final report, receipt of the report is doubtful.

"Other transactions" that Wright Laboratory issued contain a provision that the final agreement payment will not be made until an acceptable final report is received. DDR&E should issue policy to require withholding the final milestone payments to the research participant until the Government technical representative has approved the final report and has submitted the report to the Center.

### Management Control Programs

The Army, the Air Force, and DCMC organizations responsible for the administration of "other transactions" need to revise their management control programs to include the unique administrative elements of the agreements. The management control programs at CECOM, the Wright Laboratory, and DCMC in Seattle and Syracuse include guidance that provides reasonable assurance that contracts and grants are effectively managed; however, the management control

## **Administering Other Transactions**

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program procedures were not effective in reviewing "other transactions." Therefore, agreement administrators for "other transactions" were not subject to reviews to determine whether they were following internal procedures.

## **Performance Measures**

Government Performance Results Act of 1993 (Public Law 103-62) requires agencies to establish a system to measure the effectiveness of their programs. The Act requires the establishment of annual goals, the establishment of a process for performance measurement against the goals, and the establishment of a reporting process on the degree to which the goals are met. Although DDR&E and the Director, Defense Procurement, are responsible for the Military Departments' and Defense agencies' use of "other transactions" for research and prototypes, respectively, neither DDR&E nor the Director, Defense Procurement, had established a system for measuring the performance, costs, and benefits derived from the use of the "other transactions." DDP has initiated a program requiring the Military Departments and Defense agencies to report expected benefits versus actual benefits from using a prototype "other transaction." DDR&E and the Director, Defense Procurement, could establish performance measures that include the amount of reduced lead time required to award an "other transaction" as opposed to a contract; the number of research efforts that continued after DoD funding ended; the number of new products or processes established as a result of the "other transaction," and how well the Military Departments and Defense agencies are awarding, managing, and competing "other transactions." On March 7, 1998, the Acting Director, DDR&E, informed us that he planned to establish performance measures and metrics for "other transactions" within 120 days.

## **Recommendations, Management Comments, and Audit Response**

**Deleted Recommendation.** As a result of comments to the draft report from the Defense Finance and Accounting Service, we deleted the section in the finding and the recommendation that discussed the finance center maintaining signature cards for verification of invoices submitted for payment. As a result, draft report Recommendation 6. has been renumbered to Recommendation 5.

**1. We recommend that the Director, Defense Research and Engineering, issue guidance in the DoD Grant and Agreement Regulations for awarding and administering research "other transactions" that:**

**a. Requires withholding research milestone payments when the research participant does not submit technical and business status reports and annual program plans within the terms of the agreement.**

**Defense Research and Engineering Comments.** DDR&E partially concurred, stating that the agreements officer must have sufficient remedies for enforcement when a recipient fails to comply with the terms of an agreement. DDR&E stated that guidance should not mandate the use of one remedy and should provide the latitude to exercise good business judgment and select the most appropriate remedy in each circumstance. DDR&E stated that the interim guidance makes available a range of remedies but agreed to issue a clarification of the remedies available to agreement administrators.

**b. Requires the research participant to submit business status reports that identify research expenditures by participant, milestone, or task, and that identify expenditure variances in relation to the research Annual Program Plan.**

**Defense Research and Engineering Comments.** DDR&E partially concurred, stating that periodic reports are necessary for stewardship but should not be mandated in every case as described in the recommendation. DDR&E agreed to issue guidance that permits the agreements officer to require business status reports to include such details needed for good stewardship after consultation with the program official. DDR&E will also issue guidance stressing the importance of clearly communicating the reporting requirements to the office responsible for agreement administration.

**c. Requires the adjustment of payable milestone schedules when DoD reimbursement unreasonably exceeds actual cost.**

**Defense Research and Engineering Comments.** DDR&E concurred and stated that guidance issued on March 24, 1998, provides the necessary instructions in monitoring the payable milestone schedules.

**d. Requires the research participant to submit the Annual Program Plan to the agreements administrator responsible for monitoring the effort.**

**Defense Research and Engineering Comments.** DDR&E concurred and will issue the appropriate guidance.

**e. Prohibits the investment of interest on DoD funds in research programs.**

**Defense Research and Engineering Comments.** DDR&E concurred, stating that guidance issued in March 24, 1998, satisfies the intent of the recommendation.

**f. Encourages the use of the Defense Contract Management Command in reviewing "other transaction" cost proposals.**

**Defense Research and Engineering Comments.** DDR&E concurred in principle with the recommendation but stated that additional guidance is not required because general guidance has already been issued stating that DCMC is a valuable source of expertise in preaward and postaward functions.

**g. Prohibits the award of cost-of-money and profit for "other transactions."**

**Defense Research and Engineering Comments.** DDR&E partially concurred, stating that it agrees with providing guidance that prohibits the payment of profit on assistance instruments; however, DDR&E stated that disallowing cost-of-money for "other transactions" would be inconsistent with Government guidance on other Federal assistance agreements.

**h. Requires withholding a substantial amount of the final milestone payment until the Government technical representative has approved the final technical report and the research participant has submitted the technical report to the Defense Technical Information Center.**

**Defense Research and Engineering Comments.** DDR&E partially concurred, stating that the submission and receipt of the final technical report should be outlined in the initial agreement and be incorporated as one of the payable milestone events, and DDR&E will issue guidance to make that a requirement. However, DDR&E stated that payment should be predicated only on acceptance by the Government representative.

**Audit Response.** Comments provided by DDR&E were responsive to the intent of the recommendations. We agree with DDR&E that cost-of-money is a legitimate cost for "other transactions" and that DDR&E should state that when issuing its policy in response to Recommendation 1.g. We request DDR&E to provide comments to the final report that identify when the policy for Recommendations 1.b., 1.d., 1.g., and 1.h. will be issued.

**2. We recommend that the Directors, Defense Research and Engineering and Defense Procurement, establish an integrated process team to develop quantifiable performance measures and metrics for "other transactions" for research and prototypes.**

**Defense Research and Engineering Comments.** DDR&E concurred and stated that he will try to develop ways to assess the value of "other transactions," although the measure may include both qualitative and quantifiable methods. DDR&E is participating with DDP as a team member in developing the metrics.

**Defense Procurement Comments.** DDP concurred and stated that she has been participating as a team member to develop quantifiable metrics for "other transactions" for prototypes.

**Audit Response.** Comments provided by DDR&E and DDP were responsive to the intent of the recommendations. However, we request additional comments from DDR&E and DDP that identify when they will establish "other transaction" performance measures.

3. We recommend that the Director, Defense Procurement, issue policy for prototype "other transactions" that:

a. Requires the withholding of prototype milestone payments when the prototype participant does not submit technical and business status reports and annual plans within the terms of the agreement.

**Defense Procurement Comments.** DDP partially concurred, stating that she agrees that appropriate actions should be taken when the terms of the agreement are not met but that withholding milestone payments may not necessarily be the appropriate action. DDP stated that the appropriate actions should be left to the discretion of the agreement administrator and that DDP will issue guidance on the possible actions that should be taken when the agreement terms are not met.

b. Requires the participant to submit the Annual Program Plan to the organization responsible for monitoring the prototype effort.

**Defense Procurement Comments.** DDP partially concurred, stating that DDP will issue guidance that requires the agreement administrator to receive reports needed for administering the agreements but does not believe that every prototype agreement should require an annual program plan.

c. Requires the participant to maintain DoD funds in an interest-bearing account and submit the interest to the U.S. Treasury when the prototype "other transaction" uses performance payable milestones.

d. Emphasizes the need to adjust payable milestone schedules when DoD reimbursement unreasonably exceeds actual cost.

**Defense Procurement Comments.** DDP partially concurred with Recommendations 3.c. and 3.d. stating that the recommendations assume that milestone payments are intended to track with expenditures. DDP stated that when risk is low, fixed-price type milestone payments may be established, and in those cases, payments and expenditures may not necessarily track and payment adjustments are not necessary. However, DDP stated that she will issue guidance to adjust payments where appropriate when payments are intended to track with expenditures.

e. Requires withholding a substantial amount of the final milestone payment until the Government technical representative has approved the final technical report and the report is submitted to the Defense Technical Information Center.

**Defense Procurement Comments.** DDP partially concurred, stating that if the final report is a significant requirement in the agreement, the acceptance of the report should be incorporated as a condition in one of the payment milestones. DDP will issue guidance that states that if the report is not delivered, the milestone payment should be adjusted accordingly.

## **Administering Other Transactions**

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**Audit Response.** Comments provided by DDP were responsive to the intent of the recommendations. However, additional comments from DDP to the final report are requested that identify when the policy will be issued. In addition, DDP did not respond to Recommendation 3.c., and therefore, we request comments to that recommendation.

**4. We recommend that the Commander, Army Communications - Electronics Command, require technical and business status reports in all "other transactions" that the agency issues.**

**Army Comments.** The Office of the Assistant Secretary of the Army (Research Development and Acquisition) partially concurred and stated that it agrees that technical and business status reports are necessary and the reports will be required for all "other transactions" issued by the Army. However, the Army stated that it disagrees with mandating the detail reports (as identified in Recommendation 1.b.) because such detail may not be needed by the agreements administrator.

**Audit Response.** Comments provided by the Army Assistant Secretary (Research Development and Acquisition) were responsive to the intent of the recommendation. We agree that only necessary information should be provided.

**5. We recommend that the Commander, Army Materiel Command; the Commander, Air Force Materiel Command; and the Director, Defense Logistics Agency, include the administrative process of "other transactions" in their management controls programs.**

**Army Comments.** The Office of the Assistant Secretary of the Army (Research Development and Acquisition) partially concurred and stated that the inclusion of a formal checklist is dependent upon comments provided by DDR&E and DDP and whether they accept the actions included in the recommendations. However, the Army will provide a copy of the final report to all affected Army organizations alerting them to the Inspector General, DoD, recommendations.

**Air Force Comments.** The Air Force concurred and agreed to take actions accordingly.

**Defense Logistics Agency Comments.** The Defense Logistics Agency concurred and agreed to take actions accordingly.

**Audit Response.** Comments provide by the Assistant Secretary of the Army (Research Development and Acquisition) were not fully responsive. This recommendation was made to require organizations to include in their management control programs reviews of the administration of "other transactions" to evaluate whether agreement administrators are properly overseeing these efforts. This audit identified areas that needed improvement.

We believe the inclusion of "other transactions" in organizations' management control programs should not be totally dependent upon DDR&E or DDP issuing guidance on recommendations in this report. The inclusion of "other transactions" in the management control reviews would be an addition to reviews already being conducted on other procurement instruments. The comments received from DDR&E and DDP on this report should assist the Army in developing guidance to include "other transactions" in the management control program. Therefore, we request that Assistant Secretary (Research Development and Acquisition) reconsider his position and provide comments to the final report.

## **Part II - Additional Information**

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## Appendix A. Audit Process

### Scope

**Work Performed.** We performed this audit from July 1997 through February 1998. To accomplish the audit objective, we reviewed 60 research (10 U.S.C. 2371) agreements, valued at \$1.2 billion, and 17 prototype (Section 845) agreements, valued at \$0.5 billion. The "other transactions" agreements were issued from October 1, 1992, through June 30, 1997, by either DARPA, CECOM, or Wright Laboratory. We did not review "other transactions" issued by the Navy or Defense agencies because of the limited number of "other transactions" that they issued at the time of our audit selection. The Military Departments and the Defense agencies did issue 43 "other transactions"; however, 41 agreements were awarded in the fourth quarter of FY 1997. We also did not review "other transactions" that were bailment agreements or no-cost research efforts.

**DoD-wide Corporate Level Government Performance and Result Act Goals.** In response to the Government Performance and Results Act, the DoD has established 6 DoD-wide corporate level performance objectives and 14 goals for meeting those objectives. This report pertains to achievement of the following objective and goal:

**Objective:** Fundamentally reengineer the DoD and achieve a 21st century infrastructure.

**Goal** Reduce costs while maintaining required military capabilities across all DoD mission areas. (DoD-6)

**DoD Functional Area Reform Goals.** Most major DoD functional areas have also established performance improvement reform objective and goals. This report pertains to achievement of the following functional area objective and goal:

**Objective:** Internal reinvention.

**Goal** Eliminate layers of management by streamlining processes while reducing the DoD acquisition-related workforce by 15 percent. (ACQ-3.1)

**General Accounting Office High Risk Area.** The General Accounting Office has identified several high risk areas in the DoD. This report provides coverage of the Defense Contract Management high risk area.

## Methodology

We reviewed policies and procedures applicable to the administration of "other transactions;" examined selected "other transaction" agreements; reviewed contracting officer, Government technical representative, and agreement administrator files; and conducted interviews with officials responsible for monitoring research efforts. Specifically, we:

- o reviewed guidance issued by DARPA, the Air Force, and DCMC in the administration of "other transactions";

- o reviewed judgmentally selected DARPA, CECOM, and Wright Laboratory "other transactions";

- o reviewed the receipt of status reports and annual program plans, examined agreement administrator files for correspondence to determine level of administration, examined cost reporting by research and prototype participant(s), examined the monitoring of expenditure variance, examined processing of agreement modifications, reviewed the agreement administrator processing of invoices, and the submission of final research reports; and

- o interviewed DARPA, CECOM, Wright Laboratory, and DCMC agreement administrators and technical representatives.

We also reviewed the payment process at Defense Finance and Accounting Service - Indianapolis to determine whether duplicative payments were made on "other transactions."

**Use of Computer-Processed Data.** We did not rely on computer-processed data during the review of the administration of "other transactions" at DARPA, CECOM, Wright Laboratory, or DCMC. We did rely on computer-processed data during our review of duplicative payments at the Defense Finance and Accounting Service - Indianapolis without testing the system to confirm the reliability of the data. At the Defense Finance and Accounting Service - Indianapolis, we used the Commercial Accounts Processing System. However, in reviewing the Defense Finance and Accounting Service data, we did not identify any inaccuracies in the information obtained from the database.

**Auditing Period and Standards.** We performed this program results audit in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. We included tests of management controls considered necessary.

## **Contacts During the Audit**

We visited or contacted individuals and organizations within DoD. Further details are available upon request.

## **Management Control Program**

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, requires DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls.

**Scope of Review of Management Control Program.** We reviewed the management control programs at the CECOM, Wright Laboratory, the DCMC centers at Seattle and Syracuse, and the Defense Finance and Accounting Service - Indianapolis. We examined the CECOM, Wright Laboratory, DCMC, and Defense Finance and Accounting Service - Indianapolis management control assessments and the reports issued to their higher commands. We did not review the management control program at DARPA because of prior coverage in Report No. 97-114, "Award and Administration of Contracts, Grants, and Other Transactions Issued by the Defense Advanced Research Projects Agency," March 28, 1997.

**Adequacy of Management Controls.** We identified material management control weaknesses as defined in DoD Directive 5010.38 in the administration of "other transactions" in that the established management control programs did not include the unique administrative functions that "other transaction" agreements contain. The "Administration of Other Transactions" finding in this report identified areas in which the administration of "other transactions" needed improvement. Recommendations 5 and 6 will correct the identified weaknesses.

The recommendations could result in future potential benefits, but we could not determine the amount. A copy of the report will be provided to the senior official responsible for management controls in the Army, the Air Force, DCMC, and the Defense Finance and Accounting Service - Indianapolis.

**Adequacy of Management's Self-Evaluation.** The CECOM, the Wright Laboratory, and the DCMC Centers Seattle and Syracuse had established effective management control programs within their organizations. The management control programs provided reasonable assurance the contracts and grants were effectively managed; however, the management control program procedures were not effective in reviewing "other transactions." The management control programs were not effective for "other transactions" because "other transactions" were not identified as an assessable unit and, therefore, CECOM, the Wright Laboratory, and the DCMC Centers Seattle and Syracuse management did not perform evaluations of the administration of the agreements.

## Summary of Prior Coverage

During the last 5 years, two reports were issued on using "other transactions." The General Accounting Office issued a report discussing nontraditional instruments that DARPA used to acquire research. The Inspector General, DoD, issued a report on the DARPA contracting method, and one of the findings discussed "other transactions."

**General Accounting Office, National Security and International Affairs Division 96-11 (OSD Case No. 1074), "DoD Research, Acquiring Research by Nontraditional Means," March 29, 1996.**

**Inspector General, DoD, Report No. 97-114, "Award and Administration of Contracts, Grants, and Other Transactions Issued by the Defense Advanced Research Projects Agency," March 28, 1997.**

## Appendix B. Other Transactions Reviewed

### Administering Office: Defense Advanced Research Projects Agency

| <u>Type of<br/>Instrument</u> | <u>10 U.S.C. 2371 (Research)<br/>Consortium or Contractor Name</u>    | <u>Value of<br/>Instrument</u> |
|-------------------------------|-----------------------------------------------------------------------|--------------------------------|
| <u>MDA972-</u>                |                                                                       |                                |
| 92-H-0001                     | Intel Corporation                                                     | 98,241,500                     |
| 92-H-0002                     | Cray Research Incorporated                                            | 12,700,000                     |
| 92-H-0010                     | Optical Network Technology Consortium                                 | 24,225,552                     |
| 93-H-0005                     | Materials Synthesis Processing Consortium                             | 10,275,000                     |
| 93-2-0013                     | Display Materials Consortium                                          | 4,205,166                      |
| 93-2-0017                     | Cray Research Incorporated                                            | 25,965,000                     |
| 94-2-0011                     | Boeing Company (Defense and Space Group)                              | 37,348,500                     |
| 94-3-0034                     | Solid State Oxygen Generators Consortium                              | 310,813                        |
| 94-3-0038                     | The Parallel Optical Link Organization<br>Consortium                  | 17,545,225                     |
| 94-3-0044                     | Aircraft Surface Contamination Detection<br>Consortium                | 2,606,906                      |
| 95-3-0002                     | Submerged Electric-Drive Cargo Pump<br>Commercial Spin-Off Consortium | 8,810,482                      |
| 95-3-0006                     | Hewlett-Packard Incorporated                                          | 7,240,000                      |
| 95-3-0033                     | American Waterways Shipyard Consortium                                | 162,200                        |
| 96-3-0013                     | Allison Engine Company                                                | <u>27,546,111</u>              |
| <b>Total</b>                  |                                                                       | <b>\$277,182,455</b>           |

## Appendix B. Other Transactions Reviewed

### Administering Office: Defense Advanced Research Projects Agency (Cont'd)

| <u>Type of Instrument</u> | <u>10 U.S.C. 2371, Section 845 (Prototype)</u><br><u>Consortium or Contractor Name</u> | <u>Value of Instrument</u> |
|---------------------------|----------------------------------------------------------------------------------------|----------------------------|
| <u>MDA972-</u>            |                                                                                        |                            |
| 94-3-0042                 | Lockheed Advanced Development Company                                                  | 191,650,000                |
| 95-3-0009                 | Loral Systems Company                                                                  | 4,000,000                  |
| 95-3-0010                 | Raytheon Advanced Systems Company                                                      | 3,973,188                  |
| 95-3-0011                 | Orbital Sciences Corporation                                                           | 3,998,790                  |
| 95-3-0012                 | Grumman Aerospace Company                                                              | 3,990,598                  |
| 95-3-0013                 | Teledyne Industries                                                                    | 161,348,000                |
| 95-3-0034                 | Westinghouse Electric Corporation                                                      | 8,751,307                  |
| 96-C-0006                 | E-Systems Incorporated                                                                 | 32,446,945                 |
| 96-C-0802                 | Lockheed Martin Corporation                                                            | 16,000,000                 |
| 96-C-0803                 | Bath Iron Works Corporation                                                            | 16,000,000                 |
| 96-C-0804                 | Hughes Aircraft Company                                                                | 1,000,000                  |
| 96-C-0805                 | Metro Machine Corporation                                                              | 1,000,000                  |
| 96-C-0806                 | Northrop Grumman Corporation                                                           | 16,000,000                 |
| 97-C-0804                 | L-3 Communications                                                                     | <u>2,616,000</u>           |
| <b>Total</b>              |                                                                                        | <b>\$462,774,828</b>       |

### Administering Office: Army Communications - Electronics Command

| <u>Type of Instrument</u> | <u>10 U.S.C. 2371 (Research)</u><br><u>Consortium or Contractor Name</u> | <u>Value of Instrument</u> |
|---------------------------|--------------------------------------------------------------------------|----------------------------|
| <u>MDA972-</u>            |                                                                          |                            |
| 94-3-0021                 | EcoScan Consortium                                                       | \$ 3,877,000               |
| 94-3-0036                 | Wireless Communication Engine Consortium                                 | <u>7,910,000</u>           |
| <b>Total</b>              |                                                                          | <b>\$ 11,787,000</b>       |

| <u>Type of Instrument</u> | <u>10 U.S.C. 2371 (Research)</u><br><u>Consortium or Contractor Name</u> | <u>Value of Instrument</u> |
|---------------------------|--------------------------------------------------------------------------|----------------------------|
| <u>DAAB07-</u>            |                                                                          |                            |
| 96-3-D758                 | Digital Wireless Communications                                          | \$ 15,036,810              |
| 96-3-D759                 | Wireless Interworking Testbed Consortium                                 | 2,870,000                  |
| 96-3-D760                 | Handheld Multi-Media Terminal Consortium                                 | 6,897,908                  |
| 96-3-J016                 | Diffraction Optics Technology Consortium                                 | 14,593,574                 |
| 96-3-J017                 | Hybrid Diffraction/Refractive Optics Consortium                          | 2,648,235                  |
| 96-3-J020                 | Consortium for Electron Bombarded Coupled Charged Device Camera          | <u>2,886,863</u>           |
| <b>Total</b>              |                                                                          | <b>\$ 44,933,390</b>       |

## Appendix B. Other Transactions Reviewed

### Administering Office: Air Force Wright Laboratory

| <u>Type of Instrument</u> | <u>10 U.S.C. 2371 (Research)</u><br><u>Consortium or Contractor Name</u> | <u>Value of Instrument</u> |
|---------------------------|--------------------------------------------------------------------------|----------------------------|
| <u>MDA972-</u>            |                                                                          |                            |
| 93-2-0007                 | Low-Cost Ceramic Composites Virtual Consortium                           | \$ 14,627,922              |
| 93-2-0016                 | Optical Imaging Systems Incorporated                                     | 100,743,992                |
| 94-3-0013                 | Coltec Industries                                                        | 4,499,279                  |
| 94-3-0014                 | The Fly-by-Light Advanced Systems Hardware Team                          | 24,325,060                 |
| 94-3-0015                 | Electronic Actuation and Control System Consortium                       | 13,080,000                 |
| 94-3-0016                 | Analog Optoelectronic Module Consortium                                  | 18,817,981                 |
| 95-3-0001                 | Wafer Level Known Good Die Consortium                                    | <u>2,305,000</u>           |
| Total                     |                                                                          | <b>\$178,399,234</b>       |

|                | <u>10 U.S.C. 2371, Section 845 (Prototype)</u> |               |
|----------------|------------------------------------------------|---------------|
| <u>F33615-</u> |                                                |               |
| 97-4-5130      | Scaled Composites Incorporated                 | \$ 12,003,997 |

## Appendix B. Other Transactions Reviewed

### Administering Office: Defense Contract Management Command Seattle

| <u>Type of<br/>Instrument</u> | <u>10 U.S.C. 2371 (Research)</u><br><u>Consortium or Contractor Name</u>                             | <u>Value of<br/>Instrument</u> |
|-------------------------------|------------------------------------------------------------------------------------------------------|--------------------------------|
| <u>MDA972-</u>                |                                                                                                      |                                |
| 93-2-0003                     | Smart Materials and Structures Consortium                                                            | \$ 9,940,000                   |
| 94-2-0005                     | Northeast Alternative Vehicle Consortium                                                             | 30,305,725                     |
| 94-3-0025                     | In-Situ Process Control Consortium                                                                   | 4,892,000                      |
| 94-3-0030                     | Advanced Composites Technology Transfer/Bridge<br>Infrastructure Renewal Consortium                  | 40,305,324                     |
| 94-3-0033                     | Synchronous Optical Network/Asynchronous<br>Transfer Mode Self-Healing Ring Consortium               | 18,678,553                     |
| 95-3-0004                     | National Storage Industry Consortium                                                                 | 32,152,167                     |
| 95-3-0022                     | Uncooled Low-Cost Technology Reinvestment<br>Alliance Consortium                                     | 7,673,751                      |
| 95-3-0025                     | Todd Pacific Shipyards Corporation                                                                   | 5,793,836                      |
| 95-3-0029                     | Next-Generation Display Consortium                                                                   | 45,321,937                     |
| 95-3-0030                     | Thin Cathode Ray Tube Consortium                                                                     | 50,318,327                     |
| 95-3-0031                     | Low-Cost Flip Chip Consortium                                                                        | 21,097,981                     |
| 95-3-0036                     | Flexible Thin Film Copper Indium<br>Diselenide Photovoltaics Vapor Phase<br>Manufacturing Consortium | 27,630,319                     |
| 96-3-0001                     | Microwave and Analog Front End Technology<br>Design Environment Consortium                           | 58,974,653                     |
| 96-3-0002                     | Processor Applications Electronics Consortium                                                        | 8,464,800                      |
| 97-3-0008                     | Parallel Optics for Network Interconnects<br>Consortium                                              | 23,576,973                     |
| <b>Total</b>                  |                                                                                                      | <b>\$385,126,346</b>           |

### 10 U.S.C. 2371, Section 845 (Prototype)

|                |                                        |               |
|----------------|----------------------------------------|---------------|
| <u>MDA972-</u> |                                        |               |
| 96-C-0800      | Conformal Optics Technology Consortium | \$ 12,340,581 |

## Appendix B. Other Transactions Reviewed

### Administering Office: Defense Contract Management Command Syracuse

| <u>Type of Instrument</u> | <u>Consortium or Contractor Name</u>                                                   | <u>Value of Instrument</u> |
|---------------------------|----------------------------------------------------------------------------------------|----------------------------|
|                           | <u>10 U.S.C. 2371 (Research)</u>                                                       |                            |
| <u>MDA972-</u>            |                                                                                        |                            |
| 92-2-0007                 | The Integrated High Performance Turbine Engine Technology Fiber Development Consortium | \$ 12,312,501              |
| 93-2-0008                 | High-Performance Composites Consortium                                                 | 9,158,593                  |
| 93-H-0001                 | The Investment Casting Cooperative Arrangement                                         | 16,712,783                 |
| 93-H-0002                 | Ferrite Development Consortium                                                         | 16,919,000                 |
| 94-3-0018                 | Air Quality Monitoring Consortium                                                      | 3,774,817                  |
| 94-3-0028                 | Digital X-Ray Team                                                                     | 27,139,640                 |
| 94-3-0041                 | Diamond Film Process Development Consortium                                            | 16,209,289                 |
| 94-3-0047                 | National Academic Center Information Consortium                                        | 10,484,377                 |
| 95-3-0014                 | Giant Magnetoresistance Consortium                                                     | 12,258,000                 |
| 95-3-0021                 | Consortium for Vehicle Electronics                                                     | 11,965,912                 |
| 95-3-0032                 | Cray Research Incorporated                                                             | 60,000,000                 |
| 95-3-0042                 | Seamless High Off-Chip Connectivity Consortium                                         | 24,977,256                 |
| 96-3-0008                 | Nondestructive Evaluation of High Performance Composites Alliance                      | 1,400,696                  |
| 96-3-0010                 | Cray Research Incorporated                                                             | 25,184,000                 |
| 96-3-0018                 | Osiris Therapeutics                                                                    | 6,638,999                  |
| 96-3-0019                 | Superconducting Filters for Base Station Applications Consortium                       | 5,969,190                  |
| <b>Total</b>              |                                                                                        | <b>\$ 261,105,053</b>      |

### 10 U.S.C. 2371, Section 845 (Prototype)

|                |                                                                   |               |
|----------------|-------------------------------------------------------------------|---------------|
| <u>MDA972-</u> |                                                                   |               |
| 97-C-0800      | Advanced Logistics Program Integration and Engineering Consortium | \$ 59,600,000 |

## Appendix C. Summary of Other Transactions Issues

### Defense Advanced Research Projects Agency

| Agreement Number | Type | Reports on Hand<br>Technical | Business<br>ness | Business Report<br>Shows Cost by<br>Participant Task | Interest<br>Clause in<br>Agreement | Annual<br>Plan<br>Received | All Mods <sup>1</sup><br>in<br>Files | M/S <sup>3</sup><br>Certified | Research<br>Effort<br>Complete | DTIC <sup>2</sup> Has<br>Final<br>Report |
|------------------|------|------------------------------|------------------|------------------------------------------------------|------------------------------------|----------------------------|--------------------------------------|-------------------------------|--------------------------------|------------------------------------------|
| MDA972-          |      |                              |                  |                                                      |                                    |                            |                                      |                               |                                |                                          |
| 92-H-0001        | 2371 | Yes                          | Yes              | Yes                                                  | No                                 | No                         | Yes                                  | Yes                           | Yes                            | No                                       |
| 92-H-0002        | 2371 | Yes                          | Yes              | Yes                                                  | No                                 | No                         | Yes                                  | Yes                           | Yes                            | No                                       |
| 92-H-0010        | 2371 | Yes                          | Yes              | Yes                                                  | No                                 | Yes                        | Yes                                  | Yes                           | Yes                            | No                                       |
| 93-2-0013        | 2371 | Yes                          | No               | Yes                                                  | No                                 | No                         | Yes                                  | Yes                           | Yes                            | No                                       |
| 93-2-0017        | 2371 | Yes                          | Yes              | Yes                                                  | No                                 | N/R <sup>4</sup>           | Yes                                  | Yes                           | Yes                            | N/A <sup>5</sup>                         |
| 93-H-0005        | 2371 | Yes                          | Yes              | Yes                                                  | No                                 | Yes                        | Yes                                  | Yes                           | Yes                            | No                                       |
| 94-2-0011        | 2371 | Yes                          | Yes              | Yes                                                  | No                                 | Yes                        | Yes                                  | Yes                           | Yes                            | No                                       |
| 94-3-0034        | 2371 | Yes                          | No               | No                                                   | Yes                                | Yes                        | Yes                                  | Yes                           | Yes                            | Yes                                      |
| 94-3-0038        | 2371 | Yes                          | Yes              | Yes                                                  | No                                 | Yes                        | Yes                                  | Yes                           | Yes                            | No                                       |
| 94-3-0042        | 845  | Yes                          | Yes              | Yes                                                  | N/A                                | N/R                        | Yes                                  | Yes                           | Yes                            | N/A                                      |
| 94-3-0044        | 2371 | No                           | No               | No                                                   | No                                 | No                         | Yes                                  | Yes                           | Yes                            | Yes                                      |
| 95-3-0002        | 2371 | Yes                          | Yes              | Yes                                                  | No                                 | Yes                        | Yes                                  | Yes                           | No                             | N/A                                      |
| 95-3-0006        | 2371 | Yes                          | Yes              | No                                                   | No                                 | Yes                        | Yes                                  | Yes                           | No                             | N/A                                      |
| 95-3-0009        | 845  | Yes                          | Yes              | Yes                                                  | No                                 | N/R                        | Yes                                  | Yes                           | Yes                            | N/A                                      |
| 95-3-0010        | 845  | Yes                          | Yes              | Yes                                                  | No                                 | N/R                        | Yes                                  | Yes                           | Yes                            | N/A                                      |
| 95-3-0011        | 845  | Yes                          | Yes              | Yes                                                  | No                                 | N/R                        | Yes                                  | Yes                           | Yes                            | N/A                                      |
| 95-3-0012        | 845  | Yes                          | N/R              | N/A                                                  | No                                 | N/R                        | Yes                                  | Yes                           | Yes                            | N/A                                      |
| 95-3-0013        | 845  | Yes                          | Yes              | Yes                                                  | N/A                                | Yes                        | Yes                                  | Yes                           | No                             | N/A                                      |
| 95-3-0033        | 2371 | Yes                          | Yes              | Yes                                                  | No                                 | Yes                        | Yes                                  | Yes                           | Yes                            | No                                       |
| 95-3-0034        | 845  | Yes                          | Yes              | Yes                                                  | N/A                                | Yes                        | Yes                                  | Yes                           | No                             | N/A                                      |
| 96-3-0013        | 2371 | Yes                          | Yes              | Yes                                                  | No                                 | Yes                        | Yes                                  | Yes                           | No                             | N/A                                      |
| 96-C-0006        | 845  | Yes                          | Yes              | Yes                                                  | N/A                                | Yes                        | Yes                                  | Yes                           | No                             | N/A                                      |
| 96-C-0802        | 845  | Yes                          | Yes              | Yes                                                  | No                                 | N/R                        | Yes                                  | Yes                           | No                             | N/A                                      |
| 96-C-0803        | 845  | Yes                          | Yes              | Yes                                                  | No                                 | Yes                        | Yes                                  | Yes                           | Yes                            | N/A                                      |
| 96-C-0804        | 845  | Yes                          | Yes              | Yes                                                  | No                                 | No                         | N/R                                  | Yes                           | Yes                            | N/A                                      |

## Appendix C. Summary of Other Transactions Issues

### Defense Advanced Research Projects Agency (Cont'd)

| Agreement Number | Type | Reports on Hand<br>Tech-<br>nical | Business<br>ness | Business Report<br>Shows Cost by<br>Participant Task | Interest<br>Clause in<br>Agreement | Annual<br>Plan<br>Received | All Mods <sup>1</sup><br>in<br>Files | M/S<br>Certified | Research<br>Effort<br>Complete | DTIC Has<br>Final<br>Report |
|------------------|------|-----------------------------------|------------------|------------------------------------------------------|------------------------------------|----------------------------|--------------------------------------|------------------|--------------------------------|-----------------------------|
| MDA972-          |      |                                   |                  |                                                      |                                    |                            |                                      |                  |                                |                             |
| 96-C-0805        | 845  | Yes                               | Yes              | Yes                                                  | No                                 | N/R                        | Yes                                  | Yes              | Yes                            | N/A                         |
| 96-C-0806        | 845  | Yes                               | Yes              | Yes                                                  | No                                 | N/R                        | Yes                                  | Yes              | Yes                            | N/A                         |
| 97-C-0804        | 845  | Yes                               | Yes              | Yes                                                  | No                                 | N/R                        | N/A                                  | Yes              | Yes                            | N/A                         |

### Army Communications - Electronics Command

| Agreement Number | Type | Reports on Hand<br>Tech-<br>nical | Business<br>ness | Business Report<br>Shows Cost by<br>Participant Task | Interest<br>Clause in<br>Agreement | Annual<br>Plan<br>Received | All Mods <sup>1</sup><br>in<br>Files | M/S<br>Certified | Research<br>Effort<br>Complete | DTIC Has<br>Final<br>Report |
|------------------|------|-----------------------------------|------------------|------------------------------------------------------|------------------------------------|----------------------------|--------------------------------------|------------------|--------------------------------|-----------------------------|
| DAAB07-          |      |                                   |                  |                                                      |                                    |                            |                                      |                  |                                |                             |
| 96-3-D758        | 2371 | Yes                               | Yes              | Yes                                                  | No                                 | Yes                        | Yes                                  | Yes              | No                             | N/A                         |
| 96-3-D759        | 2371 | No                                | No               | Yes                                                  | No                                 | No                         | Yes                                  | Yes              | No                             | N/A                         |
| 96-3-D760        | 2371 | Yes                               | Yes              | Yes                                                  | No                                 | Yes                        | Yes                                  | Yes              | No                             | N/A                         |
| 96-3-J016        | 2371 | No                                | N/R              | N/A                                                  | No                                 | Yes                        | Yes                                  | Yes              | No                             | N/A                         |
| 96-3-J017        | 2371 | Yes                               | N/R              | N/A                                                  | No                                 | N/R <sup>6</sup>           | Yes                                  | No               | No                             | N/A                         |
| 96-3-J020        | 2371 | N/R                               | N/R              | N/A                                                  | No                                 | No                         | Yes                                  | Yes              | No                             | N/A                         |
| MDA972-          |      |                                   |                  |                                                      |                                    |                            |                                      |                  |                                |                             |
| 94-3-0021        | 2371 | No                                | No               | No                                                   | No                                 | No                         | Yes                                  | Yes              | Yes                            | No                          |
| 94-3-0036        | 2371 | Yes                               | Yes              | Yes                                                  | No                                 | No                         | Yes                                  | Yes              | No                             | N/A                         |

## Appendix C. Summary of Other Transactions Issues

| <u>Air Force Wright Laboratory</u> |             |                        |                                                       |                                     |                             |                                      |                      |                                 |                              |
|------------------------------------|-------------|------------------------|-------------------------------------------------------|-------------------------------------|-----------------------------|--------------------------------------|----------------------|---------------------------------|------------------------------|
| <u>Agreement Number</u>            | <u>Type</u> | <u>Reports on Hand</u> | <u>Business Report Shows Cost by Participant Task</u> | <u>Interest Clause in Agreement</u> | <u>Annual Plan Received</u> | <u>All Mods<sup>1</sup> in Files</u> | <u>M/S Certified</u> | <u>Research Effort Complete</u> | <u>DTIC Has Final Report</u> |
| F33615-                            |             |                        |                                                       |                                     |                             |                                      |                      |                                 |                              |
| 97-4-5130                          | 845         | Yes                    | Yes                                                   | N/A                                 | N/R                         | N/A                                  | Yes                  | No                              | N/A                          |
| MDA972-                            |             |                        |                                                       |                                     |                             |                                      |                      |                                 |                              |
| 93-2-0007                          | 2371        | Yes                    | No                                                    | No                                  | Yes                         | Yes                                  | Yes                  | Yes                             | N/A                          |
| 93-2-0016                          | 2371        | Yes                    | Yes                                                   | No                                  | Yes                         | Yes                                  | Yes                  | No                              | N/A                          |
| 94-3-0013                          | 2371        | Yes                    | Yes                                                   | No                                  | Yes                         | Yes                                  | Yes                  | Yes                             | Yes                          |
| 94-3-0014                          | 2371        | Yes                    | Yes                                                   | No                                  | Yes                         | Yes                                  | Yes                  | Yes                             | No                           |
| 94-3-0015                          | 2371        | Yes                    | Yes                                                   | No                                  | Yes                         | Yes                                  | Yes                  | No                              | N/A                          |
| 94-3-0016                          | 2371        | Yes                    | Yes                                                   | No                                  | Yes                         | Yes                                  | Yes                  | No                              | N/A                          |
| 95-3-0001                          | 2371        | Yes                    | Yes                                                   | No                                  | No                          | Yes                                  | Yes                  | No                              | N/A                          |

## Appendix C. Summary of Other Transactions Issues

### Defense Contract Management Command Seattle

| Agreement Number | Type | Reports on Hand Technical | Business Shows Cost by Participant | Interest Clause in Agreement | Annual Plan Received | All Mods <sup>1</sup> in Files | M/S Certified | Research Effort Complete | DTIC Has Final Report |
|------------------|------|---------------------------|------------------------------------|------------------------------|----------------------|--------------------------------|---------------|--------------------------|-----------------------|
| MDA972-          |      |                           |                                    |                              |                      |                                |               |                          |                       |
| 93-2-0003        | 2371 | Yes                       | Yes                                | Yes                          | No                   | Yes                            | Yes           | Yes                      | No                    |
| 94-2-0005        | 2371 | Yes                       | Yes                                | No                           | No                   | Yes                            | Yes           | No                       | N/A                   |
| 94-3-0025        | 2371 | Yes                       | No                                 | No                           | Yes                  | Yes                            | Yes           | No                       | N/A                   |
| 94-3-0030        | 2371 | Yes                       | Yes                                | Yes                          | Yes                  | Yes                            | Yes           | No                       | N/A                   |
| 94-3-0033        | 2371 | Yes                       | Yes                                | No                           | No                   | Yes                            | Yes           | No                       | N/A                   |
| 95-3-0004        | 2371 | Yes                       | Yes                                | No                           | Yes                  | Yes                            | Yes           | No                       | N/A                   |
| 95-3-0022        | 2371 | Yes                       | No                                 | No                           | No                   | Yes                            | Yes           | Yes                      | No                    |
| 95-3-0025        | 2371 | Yes                       | No                                 | No                           | Yes                  | Yes                            | Yes           | No                       | N/A                   |
| 95-3-0029        | 2371 | Yes                       | Yes                                | Yes                          | Yes                  | Yes                            | Yes           | No                       | N/A                   |
| 95-3-0030        | 2371 | Yes                       | Yes                                | No                           | No                   | Yes                            | Yes           | No                       | N/A                   |
| 95-3-0031        | 2371 | Yes                       | Yes                                | Yes                          | No                   | Yes                            | Yes           | No                       | N/A                   |
| 95-3-0036        | 2371 | Yes                       | Yes                                | Yes                          | No                   | Yes                            | Yes           | No                       | N/A                   |
| 96-3-0001        | 2371 | Yes                       | Yes                                | No                           | No                   | Yes                            | Yes           | No                       | N/A                   |
| 96-3-0002        | 2371 | No                        | No                                 | No                           | Yes                  | Yes                            | Yes           | No                       | N/A                   |
| 96-C-0800        | 845  | Yes                       | Yes                                | No                           | No                   | Yes                            | Yes           | No                       | N/A                   |
| 97-3-0008        | 2371 | N/A                       | N/A                                | No                           | N/R                  | N/A                            | Yes           | No                       | N/A                   |

## Appendix C. Summary of Other Transactions Issues

### Defense Contract Management Command Syracuse

| Agreement Number | Type  | Reports on Hand<br>Tech-<br>Business | Business Report<br>Shows Cost by<br>Participant Task | Interest<br>Clause in<br>Agreement | Annual<br>Plan<br>Received | All Mods. <sup>1</sup><br>in<br>Files | M/S<br>Certified | Research<br>Effort<br>Complete | DTIC Has<br>Final<br>Report |
|------------------|-------|--------------------------------------|------------------------------------------------------|------------------------------------|----------------------------|---------------------------------------|------------------|--------------------------------|-----------------------------|
| 92-H-0007        | 2371  | Yes                                  | Yes                                                  | No                                 | Yes                        | Yes                                   | Yes              | Yes                            | No                          |
| 93-2-0008        | 2371  | Yes                                  | Yes                                                  | Yes                                | No                         | Yes                                   | Yes              | Yes                            | No                          |
| 93-H-0001        | 2371  | Yes                                  | Yes                                                  | No                                 | Yes                        | Yes                                   | Yes              | No                             | N/A                         |
| 93-H-0002        | 2371  | Yes                                  | No                                                   | No                                 | Yes                        | Yes                                   | Yes              | Yes                            | No                          |
| 94-3-0018        | 2371  | Yes                                  | Yes                                                  | No                                 | No                         | Yes                                   | Yes              | Yes                            | No                          |
| 94-3-0028        | 2371  | Yes                                  | Yes                                                  | No                                 | Yes                        | Yes                                   | Yes              | No                             | N/A                         |
| 94-3-0041        | 2371  | Yes                                  | Yes                                                  | No                                 | Yes                        | Yes                                   | Yes              | No                             | N/A                         |
| 94-3-0047        | 2371  | Yes                                  | Yes                                                  | No                                 | Yes                        | Yes                                   | Yes              | Yes                            | N/A                         |
| 95-3-0014        | 2371  | Yes                                  | Yes                                                  | No                                 | Yes                        | Yes                                   | Yes              | No                             | N/A                         |
| 95-3-0021        | 2371  | Yes                                  | No                                                   | No                                 | Yes                        | Yes                                   | Yes              | No                             | N/A                         |
| 95-3-0032        | 2371  | Yes                                  | Yes                                                  | No                                 | Yes                        | Yes                                   | Yes              | Yes                            | Yes                         |
| 95-3-0042        | 2371  | Yes                                  | Yes                                                  | No                                 | No                         | Yes                                   | Yes              | Yes                            | No                          |
| 96-3-0008        | 2371  | Yes                                  | Yes                                                  | Yes                                | Yes                        | Yes                                   | Yes              | No                             | N/A                         |
| 96-3-0010        | 2371  | Yes                                  | Yes                                                  | No                                 | Yes                        | Yes                                   | Yes              | No                             | N/A                         |
| 96-3-0018        | 2371  | No                                   | No                                                   | No                                 | Yes                        | Yes                                   | Yes              | No                             | N/A                         |
| 96-3-0019        | 2371  | Yes                                  | Yes                                                  | No                                 | No                         | Yes                                   | Yes              | No                             | N/A                         |
| 97-C-0800        | 845   | Yes                                  | Yes                                                  | N/A                                | Yes                        | Yes                                   | Yes              | No                             | N/A                         |
| FOC <sup>7</sup> | 69/75 | 64/72                                | 58/72                                                | 6/71                               | 39/63 <sup>8</sup>         | 73/73                                 | 76/77            | 35/77                          | 4/21                        |
| POF <sup>9</sup> | 92    | 89                                   | 81                                                   | 8                                  | 62                         | 100                                   | 99               | 45                             | 19                          |

<sup>1</sup> Modifications.

<sup>2</sup> Defense Technical Information Center.

<sup>3</sup> Milestones certified by project manager, payment approved by agreement administrator or contracting officer.

<sup>4</sup> Not required.

<sup>5</sup> Not applicable.

<sup>6</sup> Work effort suspended, pending revision to statement of work.

<sup>7</sup> Frequency of occurrences.

<sup>8</sup> Agreements administered: for DARPA, 24 of 41, or 59 percent; by DARPA, 12 of 17, or 71 percent.

<sup>9</sup> Percent of frequencies.

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## **Appendix D. Report Distribution**

### **Office of the Secretary of Defense**

Under Secretary of Defense for Acquisition and Technology  
Director, Defense Logistics Studies Information Exchange  
Under Secretary of Defense (Comptroller)  
Deputy Chief Financial Officer  
Deputy Comptroller (Program/Budget)  
Director, Defense Research and Engineering  
Assistant Secretary of Defense (Public Affairs)  
Deputy Under Secretary of Defense (Acquisition Reform)  
Director, Defense Procurement

### **Department of the Army**

Assistant Secretary of the Army (Financial Management and Comptroller)  
Assistant Secretary of the Army (Research, Development, and Acquisition)  
Commander, Communications - Electronics Command  
Auditor General, Department of the Army

### **Department of the Navy**

Assistant Secretary of the Navy (Financial Management and Comptroller)  
Auditor General, Department of the Navy

### **Department of the Air Force**

Office of the Assistant Secretary (Acquisition)  
Assistant Secretary of the Air Force (Financial Management and Comptroller)  
Director, Air Force Materiel Command  
Commander, Air Force Research Laboratory  
Auditor General, Department of the Air Force

## **Other Defense Organizations**

Director, Defense Advanced Research Projects Agency  
Director, Defense Contract Audit Agency  
Director, Defense Finance and Accounting Service  
Director, Defense Logistics Agency  
    Director, Defense Contract Management Command  
        Director, Defense Contract Management Command - Seattle  
        Director, Defense Contract Management Command - Syracuse  
    Director, Defense Supply Service  
Director, National Imagery and Mapping Agency  
Director, National Security Agency  
    Inspector General, National Security Agency  
Inspector General, Defense Intelligence Agency

## **Non-Defense Federal Organizations and Individuals**

Office of Management and Budget  
Technical Information Center, National Security and International Affairs Division,  
    General Accounting Office

Chairman and ranking minority member of each of the following congressional committees and subcommittees:

Senate Committee on Appropriations  
Senate Subcommittee on Defense, Committee on Appropriations  
Senate Committee on Armed Services  
Senate Committee on Governmental Affairs  
House Committee on Appropriations  
House Subcommittee on National Security, Committee on Appropriations  
House Committee on Government Reform and Oversight  
House Subcommittee on Government Management, Information, and Technology,  
    Committee on Government Reform and Oversight  
House Subcommittee on National Security, International Affairs, and Criminal Justice,  
    Committee on Government Reform and Oversight  
House Committee on National Security

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## **Part III - Management Comments**

# Defense Research and Engineering Comments



DIRECTOR OF DEFENSE RESEARCH AND ENGINEERING  
3030 DEFENSE PENTAGON  
WASHINGTON, D.C. 20301-3030



JUN 11 1998

## MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL (AUDITING)

SUBJECT: Draft Report on Financial and Cost Aspects of Other Transactions

The attachment to this memorandum provides comments on recommendations 1.a. through 1.h. and recommendation 2 of a draft report entitled "Financial and Cost Aspects of Other Transactions." The draft report is dated April 16, 1998, and is associated with Project Number 7AB-0051. In addition to the attached, formal comments on the recommendations, please consider informal suggestions for the text of the report that staff members of this office separately provided to you.

I appreciate having this opportunity to comment on the draft report.

Lance A. Davis  
Acting

Attachment



**COMMENTS ON RECOMMENDATIONS 1.a. THROUGH 1.h. AND  
RECOMMENDATION 2. OF DRAFT INSPECTOR GENERAL REPORT FOR  
PROJECT 7AB-0051**

The target completion date for actions resulting from the responses below would be late 1998, through updates to the interim DDR&E guidance for Technology Investment Agreements. That guidance applies to the type of "other transaction" for research that is described in the draft OIG report.

**Recommendation 1.a.** We recommend that the Director, Defense Research and Engineering (DDR&E) issue guidance in the DoD Grant and Agreement Regulations for awarding and administering research "other transactions" that requires the withholding of research milestone payments when the research participant does not submit technical and business status reports and annual program plans within the terms of the agreement.

**Response:** The DDR&E partially concurs. The DoD guidance must provide the agreements officer with sufficient remedies for the purposes of enforcement when a recipient fails to provide required technical or business status reports or materially fails to comply in any other way with the terms of an agreement. It is sufficient to identify the remedies that may be used, because the mandate for agreements officers to enforce requirements of assistance awards already is integrated throughout DoD 3210.6-R and ensuring timely submission of required reports is explicitly a function of grants administration offices in subpart G of part 22 of those regulations. However, DoD guidance should not mandate the use of one specific remedy, withholding payments, in all cases. The agreements officer should have the latitude to exercise good business judgment and select the most appropriate remedy in each circumstance. The interim DDR&E guidance for technology investment agreements (TIAs) makes available a range of remedies for enforcement purposes. There likely is benefit in providing further clarification in the guidance that those remedies are available, and the DDR&E concurs with doing so.

<<< ♦ >>>

**Recommendation 1.b.** We recommend that the Director, Defense Research and Engineering (DDR&E) issue guidance in the DoD Grant and Agreement Regulations for awarding and administering research "other transactions" that requires the research participant to submit business status reports that identify research expenditures by participant, milestone, or task, and that identify expenditure variances in relation to the research Annual Program Plan.

**Response:** The DDR&E partially concurs. The DDR&E agrees that periodic technical and business reports are necessary to the stewardship of research performed under a TIA, but does not concur with mandating in every case the details described in the recommendation. Under the current guidance for TIAs, business status reports are to provide summarized details on the status of federal funds and non-federal cost sharing, data that are used to help ensure good overall cash management. The guidance further notes that the reports should

compare the status of resources with original payment and expenditure schedules or plans, explain any major deviations, and discuss actions that will be taken to address them. In cases where the details on expenditures by participant, milestone or task are not needed by agreements administrators or program officials, requiring that they be provided creates an unnecessary added administrative burden for recipients. Therefore, the DDR&E concurs with issuing guidance that: (1) permits the agreements officer to require that business status reports include such details in cases where he or she, after consultation with the program official, judges that those details are needed for good stewardship; and (2) stresses the importance of clearly communicating the reporting requirements to the office responsible for post-award administration of the agreement.

<<< ♦ >>>

**Recommendation 1.c.** We recommend that the Director, Defense Research and Engineering (DDR&E) issue guidance in the DoD Grant and Agreement Regulations for awarding and administering research "other transactions" that requires the adjustment of payable milestone schedules when DoD reimbursement unreasonably exceeds actual cost.

**Response:** The DDR&E concurs with the substance of the recommendation, which is substantively equivalent to a recommendation made in 1997 in OIG Report 97-114. However, there is no need to issue additional guidance because the DDR&E issued guidance to implement the 1997 recommendation. That guidance, issued on March 24, 1998, with the concurrence of the Inspector General, DoD, states that:

*"To ensure good cash management, an agreements officer shall work with the responsible Government program official either at the completion of each payable milestone or upon receipt of the quarterly business status report to:*

- Compare the total amount of project expenditures, as recorded in the payable milestone report or quarterly business status report, with the amount of payments for completed milestones; and*
- Adjust future payable milestones, as needed to closely match the payments to the recipient's cash needs for the project."*

<<< ♦ >>>

**Recommendation 1.d.** We recommend that the Director, DDR&E issue guidance in the DoD Grant and Agreement Regulations for awarding and administering research "other transactions" that requires the research participant to submit the Annual Program Plan to the agreements administrator responsible for monitoring the effort.

**Response:** The DDR&E concurs and will issue guidance for the agreements officer to include a provision for submission of the annual program plan in any award document under which the recipient is required to prepare such a plan.

<<< ♦ >>>

**Recommendation 1.e.** We recommend that the Director, DDR&E issue guidance in the DoD Grant and Agreement Regulations for awarding and administering research "other transactions" that prohibits the investment of interest on DoD funds in research programs.

**Response:** The DDR&E concurs with the substance of the recommendation, but notes that additional guidance is not needed. The DDR&E guidance issued in March, 1998 as a result of a recommendation in the OIG report No. 97-114, "Award and Administration of Contracts, Grants, and Other Transactions Issued By The Defense Advanced Research Projects Agency," requires an agreements officer to forward interest received from a recipient to the responsible payment office for return to the Department of the Treasury's miscellaneous receipts account; that guidance is sufficient to preclude the use of interest for any other purpose.

<<< ♦ >>>

**Recommendation 1.f.** We recommend that the Director, DDR&E issue guidance in the DoD Grant and Agreement Regulations for awarding and administering research "other transactions" that encourages the use of the Defense Contract Management Command in reviewing "other transaction" cost proposals.

**Response:** The DDR&E concurs with the principle that agreements officers should take full advantage of the expertise of the Defense Contract Management Command (DCMC) and other offices that provide field administration services, but does not concur that it is necessary to write additional guidance in this area. The DoD Grant and Agreement Regulations (DoD 3210.6-R) already make the general point that the Defense Contract Management Command is a valuable source of pre-award, as well as post-award, expertise for assisting agreements officers.

<<< ♦ >>>

**Recommendation 1.g.** We recommend that the Director, DDR&E issue guidance in the DoD Grant and Agreement Regulations for awarding and administering research "other transactions" that prohibits the award of cost-of-money and profit for "other transactions."

**Response:** The DDR&E partially concurs. There would be value in adding a statement in the interim guidance on TIAs that prohibits the payment of profit. That statement would parallel the DoD policy prohibiting profit for other assistance instruments that appears in section 22.205(b) of the DoD Grant and Agreement Regulations (DoD 3210.6-R). The rationale for the prohibition, which is the same in the two cases, is that profit is inappropriate in an assistance relationship, whether or not cost sharing is involved.

The DDR&E cannot concur with the recommendation to disallow cost-of-money for TIAs, however, because cost-of-money is allowable for other Federal assistance to for-profit firms under applicable Governmentwide guidance in OMB Circulars A-102 and A-110. The Circulars apply the cost principles in part 31 of the Federal Acquisition Regulation (FAR) to assistance subawards that are made to for-profit firms by State and local governments,

universities, and other nonprofit organizations. Using those cost principles, for-profit firms performing Federal programs as subawardees under assistance awards are allowed to recover cost-of-money. It would be inconsistent to prohibit those same firms from recovering cost-of-money in conjunction with Federal assistance that they receive as prime awardees.

<<< ♦ >>>

**Recommendation 1.b.** We recommend that the Director, DDR&E issue guidance in the DoD Grant and Agreement Regulations for awarding and administering research "other transactions" that requires withholding a substantial amount of the final milestone payment until the Government technical representative has approved the final technical report and the research participant has submitted the technical report to the Defense Technical Information Center.

**Response:** The DDR&E partially concurs. The agreements officer, in consultation with the program official, must decide at the time of award whether to require a final technical report. If a report is required, its submission and acceptance by the government representative should be incorporated as an event for one of the payable milestones, and the DDR&E concurs with revising the guidance to make that a requirement. The DDR&E also concurs with adding guidance for awarding offices that have recipients submit technical reports directly to the Defense Technical Information Center (DTIC); the guidance would require those offices to instruct recipients (e.g., through an award term or condition) to include a fully completed DD Form 298 with each such report, so that the DTIC can recognize the document as being related to a particular DoD award and properly record its receipt. The DDR&E does not concur with withholding a payment until a report has been received, recognized, and properly recorded by the DTIC; the payment should be predicated only on the acceptance of the recipient's report by the government representative.

<<< ♦ >>>

**Recommendation 2.** We recommend that the Directors, DDR&E and Defense Procurement, establish an integrated process team to develop quantifiable performance measures and metrics for "other transactions" for research and prototypes.

**Response:** The DDR&E concurs with the recommendation to try to develop ways to assess the value of these assistance instruments, although appropriate measures may necessarily include both qualitative and quantitative methods. The ODDR&E is participating with the ODDP in an integrated process team chartered to develop metrics for "other transactions" for prototype projects, acquisition instruments that may be more amenable to quantitative metrics than assistance instruments used to support research. The DoD Grant and Agreement Regulations Working Group will consider whether the metrics identified for those "section 845 other transactions" may also be applied to "other transactions" for research, and whether there are other meaningful measures that could be used.

# Defense Procurement Comments



ACQUISITION AND  
TECHNOLOGY

## OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON  
WASHINGTON, DC 20301-3000

June 16, 1998

DP/DSPS

MEMORANDUM FOR DEPUTY ASSISTANT INSPECTOR GENERAL FOR AUDIT  
POLICY AND OVERSIGHT, DOD INSPECTOR GENERAL

SUBJECT: DODIG Draft Audit Report on Financial and Cost Aspects  
of Other Transactions (Project No. 7AB-0051)

This is in response to your request of April 16, 1998, to provide comments on the subject draft report. Our comments are provided on recommendation 2, recommendation 3.a through 3.e, and other statements in the draft report.

Thank you for the opportunity to comment on the draft.

Eleanor R. Spector  
Director, Defense Procurement

Attachments



DODIG DRAFT AUDIT REPORT ON FINANCIAL AND COST ASPECTS OF OTHER  
TRANSACTIONS (PROJECT NO. 7AB-0051)

OFFICE OF THE UNDER SECRETARY OF DEFENSE  
(ACQUISITION AND TECHNOLOGY) DIRECTOR DEFENSE PROCUREMENT

COMMENTS ON SELECTED RECOMMENDATIONS

\*\*\*\*\*

**Recommendation 2.** The DODIG recommends that the Directors, Research and Engineering and Defense Procurement, establish an integrated process team to develop quantifiable performance measures and metrics for "other transactions" for research and prototypes.

**DDP's Response:** Concur. DDP has been participating in an integrated process team since March 1998 to develop quantifiable metrics for other transactions for prototype projects.

**Recommendation 3.a.** The DODIG recommends that the Director, Defense Procurement, issue policy for prototype "other transactions" that requires the withholding of prototype milestone payments when the prototype participant does not submit technical and business status reports and annual plans within the terms of the agreement.

**DDP's Response:** Partially concur. DDP agrees that appropriate action should be taken when the terms of the agreement are not met. DDP does not agree that it is necessarily appropriate to withhold prototype milestone payments because a report or plan has not been submitted. The appropriate action should be left to the discretion of the agreement administrator. DDP will issue guidance that requires the agreement administrator to ensure the participant is complying with the terms of the agreement and to take prompt, appropriate action when the terms of the agreement are not met.

**Recommendation 3.b.** The DODIG recommends that the Director, Defense Procurement, issue policy for prototype "other transactions" that requires the participant to submit the Annual Program Plan to the organization responsible for monitoring the prototype effort.

**DDP's Response:** Partially concur. DDP will issue guidance for other transactions for prototypes to require reports needed for agreement administration to be delivered to the agreement administrators. DDP does not agree that every prototype other transaction must require an annual program plan.

**Recommendation 3.c.** The DODIG recommends that the Director, Defense Procurement, issue policy for prototype "other transactions" that requires the participant to maintain DoD funds in an interest-bearing account and submit the interest to the U.S. Treasury when the prototype "other transaction" uses performance payable milestones.

**Recommendation 3.d.** The DODIG recommends that the Director, Defense Procurement, issue policy for prototype "other transactions" that emphasizes the need to adjust payable milestone schedules when DoD reimbursement unreasonably exceeds actual cost.

**DDP's Response to 3.c. and 3.d.:** Partially concur. These recommendations assume that all milestone payments are intended to track directly to expenditures. There may be instances for prototype projects, when risk is low and price can be realistically determined, that fixed-price type milestones will be established. In these cases, payments may not necessarily track to expenditures. DDP will issue guidance requiring payment provisions to specify whether milestone payments are intended to be adjusted for expenditures and to include the procedures for adjustment. In those cases where payments are intended to track to expenditures, DDP guidance will require a statement in the agreement that the milestone payments will be adjusted based on expenditures.

**Recommendation 3.e.** The DODIG recommends that the Director, Defense Procurement, issue policy for prototype "other transactions" that requires withholding a substantial amount of the final milestone payment until the Government technical representative has approved the final technical report and the report is submitted to the Defense Technical Information Center.

**DDP's Response:** Partially concur. DDP will issue guidance that provides for the agreements officer, in consultation with the project manager, to decide if the agreement should require a final report and whether this final report is a significant requirement. If a final report is a significant requirement of the agreement, the acceptance of the report should be incorporated into one of the payment milestones. If the report is not delivered, the milestone payment should be adjusted accordingly. DDP guidance will also require agreement participants to provide evidence of submittal of required reports to Defense Technology Information Center.

## Defense Procurement Comments

Final Report  
Reference

### DODIG DRAFT AUDIT REPORT ON FINANCIAL AND COST ASPECTS OF OTHER TRANSACTIONS (PROJECT NO. 7AB-0051)

#### OFFICE OF THE UNDER SECRETARY OF DEFENSE (ACQUISITION AND TECHNOLOGY) DIRECTOR DEFENSE PROCUREMENT

#### OTHER COMMENTS

\*\*\*\*\*

1. A rewrite of the 2<sup>nd</sup> and 3<sup>rd</sup> paragraph is recommended to correct the following concerns:

a. Page i, 2<sup>nd</sup> paragraph - It is not clear if this paragraph intends to focus on other transactions for research or both types of other transactions. The paragraph inappropriately creates the impression that the FAR/DFARS applies to assistance instruments, such as grants. The paragraph introduces the word "development" when the statute only refers to research or prototype projects.

b. Page i, 3<sup>rd</sup> paragraph. This paragraph incorrectly paraphrases the FY 1994 Authorization Act.

#### Recommended rewrite:

"Other transactions" are instruments other than contracts, grants, and cooperative agreements that are used to stimulate, support, or acquire research or prototype projects. "Other transactions" were authorized as instruments to be used to reduce barriers to participation of commercial firms in DoD research, contributing to the broadening of the technology and industrial base available to the DoD, and fostering within the technology and industrial base new relations and practices that support national security. "Other transactions" are not subject to statutes or regulations that are limited in applicability to the use of a contract, grant, or cooperative agreement.

The authority to use "other transactions" for basic, applied, and advanced research projects is in section 2371 of Title 10, United States Code, "Research projects: transactions other than contracts and grants." Section 2371 was enacted in 1989 as a two-year pilot authority for the Defense Advanced Research Projects Agency (DARPA). The National Defense Authorization Act for Fiscal Year 1992 (P.L. 102-190) broadened the authority to the Military Departments and made it permanent. The authority requires, to the extent practicable, that the government funding for the research not exceed that provided by the non-government parties and that the research not duplicate research already

performed under DoD programs. The authority may be used when a standard contract, grant or cooperative agreement is not feasible or appropriate.

The National Defense Authorization Act for Fiscal Year 1994 (P.L. 103-160), as amended, permits the use of "other transactions" to carry out prototype projects that are directly relevant to weapons or weapon systems proposed to be acquired or developed by the Department. Section 845 of the National Defense Authorization Act for Fiscal Year 1994 provided three-year pilot authority for DARPA to use "other transactions" for prototype projects. Section 804 of the National Defense Authorization Act for Fiscal Year 1997 (P.L. 104-201) broadened the authority to the Military Departments and other designated officials, and extended the authority through September 30, 1999. "Other transactions" for prototype projects are to be awarded using competitive procedures, to the maximum extent practicable, but do not require non-government funding to match or exceed government funding. "Other transactions" for prototype projects can be used even if a contract would be feasible or appropriate.

2. Page 2, first three paragraphs - same concerns as expressed in the comments above. It is recommended that the above rewrite be included in lieu of the current first three paragraphs on this page.

Revised

3. Page 3, last paragraph. This paragraph states that the only guidance on section 845 other transactions is the USD(A&T) memorandum of December 14, 1996. There is also OUSD(A&T)/DDP memorandum of October 16, 1997 that provides guidance on the assignment of instrument identification numbers and collection of common data elements for section 845 other transactions. The military departments have also issued memoranda on the use of section 845 other transactions. Copies of these memoranda can be found in the DoD Deskbook at "[www.deskbook.osd.mil](http://www.deskbook.osd.mil)".

Revised

4. Page 4, 3<sup>rd</sup> paragraph, 1<sup>st</sup> sentence. Recommend deletion of "payments may be based on cost as opposed to a predetermined payment schedule". This statement is true of either an other transaction for research or an other transaction for a prototype project. There is not a mandated payment method for either type of other transaction.

5. Page 4, 3<sup>rd</sup> paragraph, last sentence, states incorrectly that "Upon completion of the prototype 'other transaction' effort, the prototype is delivered to the Government.". Though a prototype may be developed under an other transaction, it may not always be delivered to the Government.

Revised

## Defense Procurement Comments

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Final Report  
Reference

Revised

6. Page 5, Table 1. Corrected statistics on 845 awards have been separately provided to the DoD IG.

3

Attachment (2)

# Office of the Army, Assistant Secretary (Research Development and Acquisition) Comments



REPLY TO  
ATTENTION OF

SARD-PP

DEPARTMENT OF THE ARMY  
OFFICE OF THE ASSISTANT SECRETARY  
RESEARCH DEVELOPMENT AND ACQUISITION  
103 ARMY PENTAGON  
WASHINGTON DC 20315-0103

01 JUN 1996

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL (AUDITING), 400  
ARMY NAVY DRIVE, ARLINGTON VIRGINIA 22202

SUBJECT: Draft Audit Report on Financial and Cost Aspects of Other  
Transactions (Project No. 7AB-0051)

The attachment to this memorandum provides comments on  
Recommendations 4 and 6 of the subject audit report.

I appreciate having the opportunity to comment on the draft report.

  
John R. Conklin, Director  
Procurement and Industrial Base Policy

Attachment

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**Office of the Army, Assistant Secretary (Research Development and Acquisition) Comments**

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**COMMENTS ON RECOMMENDATIONS 4 AND 6 OF DRAFT  
INSPECTOR GENERAL REPORT FOR PROJECT NO. 7AB-0051**

**Recommendation 4.** We recommend that the Commander, Army Communications-Electronics Command, require technical and business status reports in all "other transactions" that the agency issues.

**Response:** Partially concur. The Army partially concurs in this recommendation, and agrees that periodic technical and business status reports are necessary to the responsible stewardship of funds expended for research performed under "Other Transactions." These reports will be required in all "Other Transactions" that the Army issues. The Army, however, does not concur with mandating in every case the level of detail for business status reports, which is described elsewhere in the subject draft report (i.e., Recommendation 1.b -- "identification of research expenditures by participant, milestone, or task, and identification of expenditure variances in relation to the research Annual Program Plan"). Under the existing guidance for Technology Investment Agreements (i.e., "Other Transactions" and Cooperative Agreements designed to increase participation of commercial firms in DoD research, by supporting or stimulating such research), business status reports are to provide summarized details on the status of federal funds and non-federal cost sharing, data that are used to help ensure good overall cash management. The guidance also notes that the reports should compare the status of resources with original payment and expenditure schedules or plans, explain any major deviations, and discuss actions that will be taken to address them. In cases where details on expenditures by participant, milestone, or task are not needed by Agreement Administrators or program officials, requiring that they be provided creates an unnecessary added administrative burden for recipients. The Agreements Officer, in consultation with program officials, should determine the appropriate level of detail required for the business status report, on a case by case basis, to ensure responsible stewardship of federal funds.

**Office of the Army, Assistant Secretary (Research Development and  
Acquisition) Comments**

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Final Report  
Reference

-2-

**Recommendation 6.** We recommend that the Commander, Army Materiel Command; the Commander, Air Force Materiel Command; and the Director, Defense Logistics Agency, include the administrative process of "other transactions" in their management controls programs.

Recommend-  
ation  
renumbered

**Response:** Partially concur. The inclusion of the administrative process of "Other Transactions" in the Management Controls Program (MCP), to include the formulation of an evaluation/checklist for "Other Transactions", is contingent upon DDR&E and the Director, Defense Procurement completing the actions in Recommendations 1-3. Therefore, it is premature to include "Other Transactions" in any MCP before further, definitive guidance is issued by these offices. Moreover, since "Other Transactions" are awarded throughout DoD, not only by the Military Departments, but also by Defense Agencies, the evaluation/checklist, and any other documentation inherent in the MCP process, should be written and approved at the DoD level, with representatives from the Military Departments and Defense Agencies participating in its formulation. This will help to ensure uniform application of MCP to "Other Transactions" throughout DoD.

When the DoD Inspector General Report is finalized, the Office of the Deputy Assistant Secretary of the Army (Procurement) will provide a copy of the report to all Army activities, (to include Army Materiel Command activities), which award "Other Transactions" alerting them to the recommendations found by the DoD IG.

# Office of the Air Force, Assistant Secretary (Acquisition) Comments

Final Report  
Reference



Office of the Assistant Secretary

DEPARTMENT OF THE AIR FORCE  
WASHINGTON DC

23 JUL 1996

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING, OFFICE OF  
THE INSPECTOR GENERAL, DEPARTMENT OF DEFENSE

FROM: SAF/AQC  
1060 Air Force Pentagon  
Washington DC 20330-1060

SUBJECT: Air Force Response to DoDIG Draft Report, Financial and Cost Aspects of Other  
Transactions, (Project No. 7AB-0051)

This is in reply to your memorandum requesting Air Force comments on subject report.

Recommendation 6. We recommend that the Commander, Army Materiel Command; the  
Commander, Air Force Materiel Command; and the Director, Defense Logistics Agency, include  
the administrative process of "other transactions" in their management controls programs.

Air Force Response: Concur. We agree that appropriate action should be taken to  
include the administrative process of "other transactions" in the Air Force Materiel Command's  
management control programs.

A handwritten signature in black ink, appearing to be "Terry L. Raney".

TERRY L. RANEY, Col, USAF  
Acting Associate Deputy Assistant  
Secretary (Contracting)  
Assistant Secretary (Acquisition)

Recommend-  
ation  
renumbered

# Defense Finance and Accounting Service Comments



## DEFENSE FINANCE AND ACCOUNTING SERVICE

1931 JEFFERSON DAVIS HIGHWAY  
ARLINGTON, VA 22240-3291

JUN 29 1998

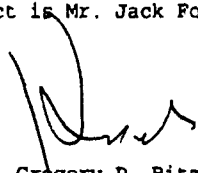
DFAS-HQ/FCC

MEMORANDUM FOR DIRECTOR, ACQUISITION MANAGEMENT DIRECTORATE,  
OFFICE OF THE INSPECTOR GENERAL, DEPARTMENT OF  
DEFENSE

SUBJECT: Response to DoDIG Draft Report, "Financial and Cost  
Aspects of Other Transactions," dated April 16, 1998  
(Project No. 7AB-0051)

In response to your memorandum of April 16, 1998, the  
Defense Finance and Accounting Service has provided the attached  
comments on Recommendation 5.

Our point of contact is Mr. Jack Foust. He can be reached  
at (703) 607-5030.

*for*   
Gregory P. Bitz  
Director for Finance

Attachment:  
As stated

## Defense Finance and Accounting Service Comments

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### Final Report Reference

### Recommend- ation deleted

Defense Finance and Accounting Service Comments on DoDIG Draft Report, Financial and Cost Aspects of Other Transactions, dated April 16, 1998 (Project No. 7AB-0051)

Recommendation 5: We recommend that the Director, Defense Finance and Accounting Service, obtain signature cards from the Defense Contract Management Command Seattle for verification of signatures on invoices submitted for payment.

DFAS Response: Nonconcur. In the Department of Defense Financial Management Regulation, Volume 10, Chapter 9, signature cards or lists of authorized government representatives are not required to be maintained by disbursing offices; however, the delivery receipt must contain the signature of an authorized government representative. The receiving activity is responsible for assuring that receipt and acceptance of goods and services is properly acknowledged and documented. The activity must assure that the function is performed by qualified and competent personnel relevant to the goods or services received. The receiving activities are also responsible for maintaining the list of personnel authorized to sign receiving reports. On a practical level, the number of personnel who may document receipt and acceptance is usually quite large and there is typically a substantial turnover in the personnel assigned. Since the activity has the expertise, knowledge and responsibility for assuring that the government receives appropriate value and DFAS cannot effectively maintain the large, volatile list, the responsibility appropriately remains with the activity and DFAS accepts the signature as valid on its face.

Estimated Completion Date: Action complete.

# Defense Logistics Agency Comments



**DEFENSE LOGISTICS AGENCY**  
**HEADQUARTERS**  
8725 JOHN J. KINGMAN ROAD, SUITE 2533  
FT. BELVOIR, VIRGINIA 22060-6221

10 JUN 1998

REPLY  
REFERTO

DDAI

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING  
DEPARTMENT OF DEFENSE

SUBJECT: Draft Report on Financial and Cost Aspects of Other  
Transactions (Project No. 7AB-0051)

Enclosed are DLA comments in response to your request of  
April 16, 1998. Please contact Zora Henderson, DDAI, 767-6272,  
if you have any questions.

*Sheila P. Raines*

SHEILA P. RAINES  
Team Leader, Liaison & Policy  
Internal Review Office

Federal Recycling Program



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## Defense Logistics Agency Comments

18 JUN 1998

**SUBJECT:** Financial and Cost Aspects of Other Transactions (Project No. 7AB-0051)

**FINDING:** The DoD administration of "other transactions" generally has been adequate. However, the Army, the Air Force, the Defense Finance and Accounting Service, and the Defense Contract Management Command need to improve their management controls. Those conditions exist because guidance was inadequate for the administration of "other transactions," and management did not devote sufficient attention in developing a process to quantify the benefits from using "other transactions." As a result, DoD officials did not have the information necessary to adequately monitor "other transaction" efforts, did not adjust milestone payments when necessary, inappropriately awarded cost of money and profit, forfeited interest, and did not receive information necessary to preclude duplicating research. The Defense Finance and Accounting Service could process invoice payments without proper approval. Finally, the Directors, Defense Research and Engineering and Defense Procurement, did not establish quantifiable performance measures to determine the costs and benefits resulting from the use of "other transactions."

**DLA COMMENTS:** We concur that DCMC guidance is lacking. DCMC will develop and incorporate guidance for the administration of "other transactions" into the DLAD 5000.4, Contract Management. We expect to have this guidance fully developed, coordinated and published by November 30, 1998.

**Internal Management Control Weakness:**

(X ) Concur that DCMC guidance is lacking. Weakness will be considered as part of the DCMC Annual Statement of Assurance.

Action Officer: Tim Frank, DCMC-OC, 703-767-3431

Review/Approval: Gary S. Thurber, Deputy, DCMC

Coordination: Dave Stumpf, DDAI, 767-6266

**DLA APPROVAL:**



E.R. CHAMBERLIN  
Rear Admiral, SC, USN  
Deputy Director

13 JUL 1998

**SUBJECT:** Financial and Cost Aspects of Other Transactions (Project No. 7AB-0051)

**RECOMMENDATION 6:** We recommend that the Commander, Army Materiel Command; the Commander, Air Force Materiel Command; and the Director, Defense Logistics Agency, include the administrative process of "other transactions" in their management controls program.

**DLA COMMENTS:** We concur with the recommendation that we include the administration of "other transactions" in our DCMC management controls program.

**DISPOSITION:**

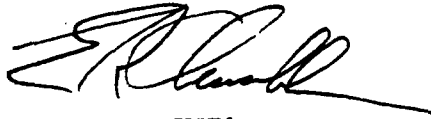
( X ) Action is ongoing. ECD: November 30, 1998

Action Officer: Tim Frank, DCMC-OC, 703-767-3431

Review/Approval: Gary s. Thurber, Deputy, DCMC

Coordination: Dave Stumpf, DDAI, 767-6266

**DLA APPROVAL:**



E.R. CHAMBERLIN  
Rear Admiral, SC, USN  
Deputy Director

## **Audit Team Members**

The Acquisition Management Directorate, Office of the Assistant Inspector General for Auditing, DoD, produced this report.

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Gary B. Dutton  
Vonna D. Swigart

## INTERNET DOCUMENT INFORMATION FORM

**A . Report Title: Financial and Cost Aspects of Other Transactions**

**B. DATE Report Downloaded From the Internet: 09/13/99**

**C. Report's Point of Contact: (Name, Organization, Address, Office  
Symbol, & Ph #):** OAIG-AUD (ATTN: AFTS Audit Suggestions)  
Inspector General, Department of Defense  
400 Army Navy Drive (Room 801)  
Arlington, VA 22202-2884

**D. Currently Applicable Classification Level: Unclassified**

**E. Distribution Statement A: Approved for Public Release**

**F. The foregoing information was compiled and provided by:**  
**DTIC-OCA, Initials: \_\_VM\_\_ Preparation Date 09/13/99**

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