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AUDIT OF THE UNION VALLEY SAMPLE
PREPARATION FACILITY AT OAK RIDGE

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AUDIT OF THE UNION VALLEY SAMPLE
PREPARATION FACILITY AT OAK RIDGE

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OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDIT SERVICES

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Audit Report Number: ER-B-98-03

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SUMMARY

In 1991, Lockheed Martin Energy Systems (Energy Systems) determined that new bioassay and environmental sampling laboratories were needed to meet increasing workload and staffing requirements. Energy Systems proposed and the Department of Energy (Department) approved a solicitation for a private company to construct a facility which Energy Systems would lease back on behalf of the Department. Energy Systems entered into a lease for this purpose in August 1994 and moved into the facility in October 1995. We initiated this audit to determine if the Department's acquisition of the Union Valley Sample Preparation Facility (UVSPF) was necessary and cost effective.

Departmental policy requires that management and operating contractors acquire new facilities only when essential to the Department's mission. However, Energy Systems did not base the acquisition of the UVSPF on valid mission requirements. This occurred because Energy Systems did not follow Departmental procedures in planning and developing the lease, and the Department approved the lease without adequate justification. As a result, the Department planned to spend between \$4 million and \$18.9 million to lease a facility which was not necessary. We recommended that the Manager, Oak Ridge Operations Office, (1) direct Energy Systems to follow Departmental policies and procedures and base acquisitions of property on valid mission requirements and an analysis of all viable alternatives; (2) direct project managers to follow Departmental orders and require approvals of construction projects and property leases to include (a) verification that the projects are essential to meet mission requirements and (b) an analysis of all viable alternatives; and (3) direct Energy Systems to give the required 365-day notice and discontinue the lease.

Also, Federal regulations require that agencies and their contractors develop purchase descriptions and specifications in a manner designed to promote full and open competition. Contractors are required to develop specifications which reflect the agency's minimum needs without arbitrary or unduly restrictive provisions. However, Energy Systems restricted the location of the UVSPF to an approximate 16-square-mile area without establishing a programmatic need for the restriction. The restriction gave an Energy Systems subcontractor a competitive advantage over other potential bidders and may have caused the Department to pay

more than necessary for the facility. We recommended that the Manager, Oak Ridge Operations Office, direct Energy Systems to discontinue the practice of restricting the location of facilities acquired or leased on the Department's behalf unless the restrictions are justified to meet mission requirements.

Management did not concur with the audit findings nor the recommendation to direct Energy Systems to discontinue the lease. However, management did concur with the other recommendations. Management stated that the acquisition of the UVSPF was based on valid mission requirements that were not documented in the acquisition file, but were evidenced by the approval of Energy Systems' management and the concurrence of Departmental programmatic personnel. Also, management stated that no formal assessment was prepared because the cost to renovate clearly exceeded the cost of leasing short-term, temporary space. Further, management stated that the work could not be contracted out because there were no commercial laboratories which could meet the detection limits and required delivery schedules proposed for bioassay analyses. Finally, management stated that the delineated area in the solicitation for bids did not give an Energy Systems subcontractor a competitive advantage and did not cause the Department to pay more than necessary for the facility.

We concluded that the UVSPF was not necessary. In response to our initial draft report, management performed a cost-benefit analysis which showed construction and renovation costs exceeded the lease cost. However, Energy Systems' estimates for construction and renovation were based on the architectural drawings of the UVSPF without any justification for a facility of that size. Also, contrary to management's statement that the work could not be contracted out, Energy Systems identified two commercial laboratories which could meet the detection limits and required delivery schedules for bioassay analyses. Further, we determined that the subcontractor, who purchased land in the delineated area before the request for proposal was issued, had a competitive advantage over other potential bidders who did not already own land in the area.

/s/
Office of Inspector General

PART I

APPROACH AND OVERVIEW

INTRODUCTION

In 1991, Lockheed Martin Energy Systems (Energy Systems) determined that new bioassay and environmental sampling laboratories were needed to meet increasing workload and staffing requirements. Energy Systems proposed and the Department of Energy (Department) approved a solicitation for a private company to construct a facility which Energy Systems would lease back on behalf of the Department. Energy Systems entered into a lease for this purpose in August 1994 and moved into the facility in October 1995. We conducted the audit to determine if the Department's acquisition of the Union Valley Sample Preparation Facility (UVSPF) was necessary and cost effective.

SCOPE AND METHODOLOGY

The audit was performed from September 23, 1996, through August 28, 1997, at the Department's Oak Ridge Reservation in Oak Ridge, Tennessee. To accomplish the audit objective, we:

- Reviewed applicable laws and regulations;
- Analyzed the procurement files for the lease of the UVSPF and interviewed appropriate Departmental and contractor officials;
- Evaluated justifications for the facility; and
- Assessed the workload and staffing requirements of Energy Systems' Analytical Services Organization.

The audit was conducted in accordance with generally accepted Government auditing standards for performance audits, and included tests of internal controls and compliance with laws and regulations to the extent necessary to satisfy the audit objective. Because our review was limited, it would not necessarily have identified all internal control deficiencies that may have existed. We did not conduct a reliability assessment of computer-processed data because only a very limited amount of computer-processed data was used during the audit.

In our opinion, the matters discussed in this report identified material internal control weaknesses within the Department that should be considered when preparing the yearend assurance memorandum on internal controls. Internal control weaknesses identified in this report are discussed in Part II.

We discussed the audit results with the Branch Chief for the Contracts and Property Management Branch of the Oak Ridge Operations Office (Operations Office) during an exit conference on October 9, 1997.

BACKGROUND

In 1989, Energy Systems anticipated that the Y-12 facility's analytical workload for environmental and bioassay sampling would increase substantially. The formation of the Office of Environmental Restoration and the placement of the Oak Ridge Reservation on the National Priorities List contributed to this assumption. Y-12 personnel determined that they did not have adequate laboratory space to perform the increased tests and that additional space would have to be acquired.

In December 1991, Energy Systems requested approval from the Operations Office to proceed with the solicitation for the construction and lease back of a special purpose laboratory. The laboratory space was requested for personnel preparing samples in its bioassay and environmental sampling areas. Upon receipt of the Operations Office approval in January 1993, Energy Systems issued the solicitation. After evaluation, the award was made in August 1994.

The lease agreement included the construction of a new facility containing 28,253 net usable square feet of laboratory and office space built to Energy Systems' specifications. It was awarded for an initial 5-year term which runs from October 25, 1995, through October 24, 2000, and included four 5-year options which, if exercised, would run through October 24, 2020. The lease cost for the initial 5-year term would be about \$4 million. If all four options are exercised, the total lease cost would be about \$18.9 million. The lease also contains a termination clause which Energy Systems can exercise with a 365-day notice to the landlord.

PRIOR REPORTS

In November 1996, the Office of Inspector General (OIG) issued Report DOE/IG-0398, *Special Report on the Audit of the Management of Department of Energy Construction Projects*. The audit summarized the two primary themes associated with five previous OIG reports that dealt with the Department's construction process. The report illustrated several cases where projects were not needed or alternatives to construction were not fully evaluated prior to proceeding with the construction of new facilities, and that construction plans were not always reassessed when mission needs changed.

Additionally, in April 1997, the OIG issued Report DOE/IG-0402, *Audit of the Management of the Department of Energy's Leased Administrative Facilities*. This audit showed that the Department leased more office space than it used and that it could not determine future space needs. The Department reported a decrease in its total Federal and contractor personnel. However, during this same time period, the total square feet of leased space increased. Staffing

levels decreased 16.7 percent, while the amount of leased space increased 32.7 percent during the same 4-year period.

Further, in June 1997, the OIG issued Report WR-B-97-06, *Audit of Renovation and New Construction Projects at Lawrence Livermore National Laboratory*. This audit found that Lawrence Livermore National Laboratory (Lawrence Livermore) may not have selected the best alternatives for meeting the Department's needs. The Oakland Operations Office did not ensure that Lawrence Livermore had performed cost-benefit analyses of all alternatives before renovating or constructing new facilities.

Finally, in October 1997, the OIG issued Report ER-B-98-02, *Audit of Environmental Monitoring and Health Physics Laboratories at the Savannah River Site*. The audit concluded that Westinghouse Savannah River Company did not perform life-cycle cost analyses and periodic reassessments and could not ensure that the construction of new laboratories was the most cost-effective alternative available to accomplish the Department's environmental monitoring and health physics missions.

PART II

FINDINGS AND RECOMMENDATIONS

1. Justification for the New Facility

FINDING

Departmental policy requires that management and operating contractors acquire new facilities only when essential to the Department's mission. However, Energy Systems did not base the acquisition of the UVSPF on valid mission requirements. Energy Systems did not follow Departmental procedures in planning and developing the lease, and the Department approved the lease without adequate justification. As a result, the Department planned to spend between \$4 million and \$18.9 million to lease a facility which was not necessary.

RECOMMENDATIONS

We recommend that the Manager, Oak Ridge Operations Office:

1. Direct Energy Systems to follow Departmental policies and procedures and base acquisitions of property on valid mission requirements and an analysis of all viable alternatives;
2. Direct project managers to follow Departmental orders and require approvals of construction projects and property leases to include (a) verification that the projects are essential to meet mission requirements and (b) an analysis of all viable alternatives; and
3. Direct Energy Systems to give the required 365-day notice and discontinue the lease.

MANAGEMENT REACTION

Management did not concur with the audit finding, Recommendation 3, and the estimated monetary impact. However, management did concur with Recommendations 1 and 2. Management stated that the acquisition of the UVSPF was based on valid mission requirements as evidenced by the approval of senior Energy Systems' management and the Department's concurrence for the project. Also, management stated that no formal assessment was prepared because the cost to renovate clearly exceeded the cost of leasing short-term, temporary space. Further, management stated that the work could not be contracted out because there were no other laboratories which could meet the detection limits and required delivery schedules

proposed for bioassay analyses. Comments received from management are summarized and addressed in Part III of this report.

DETAILS OF FINDING

REQUIREMENTS FOR JUSTIFICATIONS

Departmental Order 4300.1C, *Real Property Management*, requires that all real property holdings be planned, developed, and managed efficiently and economically. The order requires that all real property be used effectively and that only real property essential to the mission of the Department be acquired. Also, the order states that program senior officials are responsible for ensuring that documented studies and proposals to acquire real property are made with full consideration of economy, efficiency, and programmatic needs (both current and future). An analysis of all viable options and alternatives considered, including the advantages and disadvantages of each, along with the recommended option, must be submitted by the managing and operating contractor to the Department for approval in the Preliminary Real Estate Plan (PREP). In addition, the Department's *Leasing Handbook* requires that the decision to lease or purchase be made only after studying the type of space needed, time elements, and economic considerations.

LEASE OF THE UNION VALLEY SAMPLE PREPARATION FACILITY

Energy Systems did not base the acquisition of the UVSPF on valid mission requirements. Energy Systems stated in its PREP that expanding bioassay and environmental programs resulted in an immediate and critical need for laboratory and office space to accommodate the requirements of approximately 20 additional personnel in Energy Systems' Y-12 Plant Quality Services Division. However, Energy Systems did not perform any formal workload projections or studies demonstrating that the existing facilities were inadequate to handle the anticipated increase in workload. The increase in workload actually occurred before the UVSPF was constructed, and Energy Systems was able to accommodate the increase with its existing facilities.

During and after construction of the UVSPF, the laboratories' workload declined. The number of tests performed by the bioassay and environmental support programs decreased from about 54,700 in Fiscal Year (FY) 1994, when the lease was signed, to about 45,900 in FY 1996, when Energy Systems moved into the UVSPF. The workload continued to decline to about 32,100 tests performed in FY 1997.

Accompanied with the decline in workload was a decline in personnel. The Analytical Services Organization (ASO), which included the Y-12 bioassay and environmental support programs and all similar Energy Systems programs in Oak Ridge, peaked at 586 employees in

1994. By October 1995, when Energy Systems moved into the UVSPF, the ASO had declined to 490 employees. As of April 1997, the ASO was down to about 300 employees.

Additionally, around the same time that Energy Systems moved into the UVSPF, the ASO was planning to vacate existing office and laboratory space on the Oak Ridge Reservation. The ASO vacated about 95,000 square feet in existing buildings after acquiring about 28,000 square feet at the UVSPF. Also, as of August 1997, ASO was planning to vacate an additional 35,000 square feet of existing office and laboratory space.

In response to our initial draft report, Energy Systems performed a cost-benefit analysis of viable alternatives and associated costs, including upgrading its laboratory space and contracting the activities to commercial laboratories. However, Energy Systems' analysis did not provide justification for the space proposed. The estimates for construction and renovation were based on the architectural drawings of the UVSPF without any justification for a facility of that size.

Energy Systems' cost-benefit analysis disclosed that all 51 types of environmental support tests and 2 of the 7 types of bioassay tests performed at the UVSPF could be contracted out at less cost to the Department. Energy Systems determined that the cost to contract out environmental support tests in FY 1997 was \$1.2 million, and the cost to perform the same tests in house, at the UVSPF, was \$1.6 million. Therefore, the Department could save about \$400,000 by contracting out all types of environmental support tests. Additionally, two types of bioassay tests could be contracted out at less cost to the Department, resulting in additional savings of about \$11,000 in FY 1997. Finally, the cost-benefit analysis shows that if UVSPF lease costs were included, it would cost less to contract out all types of environmental support and bioassay tests.

After the audit was completed, the Operations Office stated that the UVSPF was needed because the old laboratory space was technically insufficient for bioassay and low-activity radiochemical preparation work. Management stated that the space had to be vacated because of the potential for cross-contamination, false positive readings, and the increased failure rate for bioassay (the rate that samples must be reanalyzed due to quality problems). However, management provided no evidence that cross-contamination or false positive readings had occurred. Furthermore, data provided by management showed that the failure rate for bioassay samples was only one-half percent higher at the old laboratory space than at the UVSPF. This would have resulted in about 60 additional samples having to be reanalyzed in FY 1997, and would not have justified the acquisition of the UVSPF.

ENERGY SYSTEMS' ANALYSIS AND THE DEPARTMENT'S APPROVAL

These conditions occurred because Energy Systems did not follow Departmental procedures requiring analyses of all viable options and the Department approved the lease without adequate justification. Energy Systems did not perform a thorough analysis to determine that the construction and lease back of the UVSPF was the most viable option. Internal

memorandums in the procurement file refer to an assessment of existing space and a proposed line item for a new laboratory ranging from \$100 million to \$240 million. However, Energy Systems could not provide any documentary evidence that it studied upgrading its laboratory space, contracting the activities out, or other possible alternatives until after our audit was completed.

The Operations Office approved the lease on the basis of concurrence by program senior officials. However, the program senior officials did not require Energy Systems to provide documented studies showing that the proposal to lease the UVSPF was made with full consideration of economy, efficiency, and programmatic needs.

POTENTIAL COSTS

As a result, the Department planned to spend up to \$18.9 million to lease a facility which was not necessary. Under the lease terms, the Department will pay \$4 million over the first 5 years and could pay \$18.9 million over the 25-year life of the lease.

In the February 1996 issue of *DOE This Month*, the Department reported that the bioassay activities at Oak Ridge National Laboratory had been privatized and that leasing the UVSPF was expected to result in annual savings of \$2 million over the next 20 years. Through discussions with personnel at the Operations Office and Energy Systems, we determined that the bioassay activities were not privatized, the costs savings were never anticipated, and the source for the projected savings was unknown.

2. Restrictive Specifications

FINDING

Federal regulations require that agencies and their contractors develop purchase descriptions and specifications in a manner designed to promote full and open competition. Contractors are required to develop specifications which reflect the agency's minimum needs without arbitrary or unduly restrictive provisions. However, Energy Systems restricted the location of the UVSPF to an approximate 16-square-mile area without establishing a programmatic need for the restriction. The restriction gave an Energy Systems subcontractor a competitive advantage over other potential bidders and may have caused the Department to pay more than necessary for the facility.

RECOMMENDATION

We recommend that the Manager, Oak Ridge Operations Office, direct Energy Systems to discontinue the practice of restricting the location of facilities acquired or leased on the Department's behalf unless the restrictions are justified to meet mission requirements.

MANAGEMENT REACTION

Management did not concur with the audit finding, but it did concur with the recommendation. The Operations Office issued a memorandum to Energy Systems stating that lease restrictions must be fully justified based on mission requirements. However, the Operations Office did not direct Energy Systems to discontinue its practice of restricting the location of new facilities to a small area within the City of Oak Ridge. Management disagreed that the geographic restriction gave the UVSPF subcontractor a competitive advantage over other potential bidders and may have caused the Department to pay more than necessary for the facility. Comments received from management are summarized and addressed in Part III of this report.

DETAILS OF FINDING

ACQUISITION REQUIREMENTS

Federal Acquisition Regulation Subpart 10.002 requires that agencies and their contractors develop purchase descriptions and specifications in a manner designed to promote full and open competition. Agencies and contractors are required to use market research to

develop specifications which reflect the agency's minimum needs without arbitrary or unduly restrictive provisions. Also, the Comptroller General has ruled that an agency cannot impose a geographic restriction or select a delineated area which does not represent actual needs.

In addition to Federal regulations and Comptroller General decisions, Departmental Order 4300.1C, *Real Property Management* (Order), and the Department's *Leasing Handbook* (Handbook) encourage full and open competition and specify that any geographic restriction must be based on programmatic needs and must be large enough to provide adequate competition. Any geographic restriction must be approved by the Department in a PREP. The Order and the Handbook also require that a market survey be conducted to ensure that there are adequate sites for competition within the designated area.

The Handbook states that the market survey is the most crucial step in the leasing procedure. The market survey is where the realty specialist becomes familiar with the marketplace and gathers data for the negotiation strategy. The market survey determines which proposed properties meet mission requirements and which might be acceptable to the Department. The Handbook states that the information gathered must thoroughly document the availability and quality of space, services offered, and rental rates being paid for similar space.

GEOGRAPHIC RESTRICTION IMPOSED BY ENERGY SYSTEMS

Energy Systems did not obtain the advantages of full and open competition for the Department in the construction and lease back of the UVSPF. Energy Systems imposed a geographic restriction without justifying it on the basis of mission requirements.

Energy Systems prepared the required PREP and submitted it to the Operations Office for approval in January 1992. The PREP stated that the facility should be located within 3 miles of the City of Oak Ridge (City). The PREP did not include a justification for the geographic restriction. The Operations Office officially approved the PREP in January 1993.

In its May 1993 request for proposal, Energy Systems further restricted the location of the facility to an approximate 16-square-mile area within the City. This geographic restriction was not based on programmatic mission requirements, nor was it justified in the procurement file. During our audit, Energy Systems personnel stated that the restriction was normal procedure to exclude "undesirable" areas of the City and to avoid exorbitant costs of extending telecommunications outside the City. However, Energy Systems did not produce any evidence that the Department's needs could not be met outside the delineated area, and there were no cost analyses to support the claim that telecommunication costs outside the City would be exorbitant. Also, Energy Systems did not perform a market survey to ensure that the proposed area would offer enough potential sites for adequate competition.

In response to an initial draft of this report, the Operations Office stated that the restriction was necessary to reduce transportation of samples and travel for Energy System's employees between the laboratory and the Y-12 Plant, and to enhance the sharing of equipment among Energy Systems' laboratories. Also, management stated that Knox County has never been included in the delineated area for any Departmental or contractor lease. However, management did not provide a market survey or any other documented study to support its statements.

If Energy Systems had conducted the required market survey, it would have found that 92 percent of the delineated area was zoned residential or commercial and could not be used to build this type of laboratory. Furthermore, less than 2 percent of the area, or about 170 acres, was available for development. The majority of the land available for development was owned by a wholly-owned subsidiary of Lockheed Martin Corporation. In essence, Energy Systems restricted the geographic area to about one-fourth of a square mile, most of which was owned by Lockheed Martin Corporation.

COMPETITIVE ADVANTAGE

The geographic restriction excluded bidders who did not own or have access to land within the delineated area and gave a competitive advantage to an Energy Systems subcontractor. Only two responsive bids were received, and they varied significantly. The subcontractor bid \$4 million for the initial 5-year term of the lease compared to \$23.1 million for the other bidder. Also, the subcontractor bid \$18.9 million for the 25-year life of the lease compared to \$67.1 million for the other bidder.

Events surrounding the solicitation and award of the lease indicated that the subcontractor may have received advance information regarding the solicitation and award. The subcontractor purchased 14 acres of land within the area delineated by Energy Systems just 10 days after the PREP was submitted to the Operations Office for review and approval. Also, just four days after Energy Systems received the Department's approval of the PREP, the subcontractor wrote a letter to its bank stating that it had architectural plans prepared in anticipation of building a laboratory for Energy Systems, and that it was awaiting the request for proposal.

The unduly restrictive requirement for the location of the UVSPF may have caused the Department to pay more than necessary for the facility. If the Department continues to lease the UVSPF for the full 25-year term of the lease agreement, it will pay a total of \$18.9 million to lease a facility which costs the subcontractor only \$4.7 million to construct. It is impossible to determine what the facility might have cost if Energy Systems had not restricted the facility's location to a 16-square-mile area.

The Operations Office disagreed with our findings, Recommendation 3 in Finding 1, and the estimated monetary impact. However, management did concur with Recommendations 1 and 2 in Finding 1 and the recommendation in Finding 2. Management's specific comments are summarized and addressed below.

Finding 1—Justification for the New Facility

Recommendation No. 1. We recommended that the Manager, Oak Ridge Operations Office direct Energy Systems to follow Departmental policies and procedures and base acquisitions of property on valid mission requirements and an analysis of all viable alternatives.

Management Comments. Management concurred with the recommendation. The Contracting Officer issued a letter to Energy Systems on August 19, 1997, formally reminding Energy Systems management that Departmental policies and procedures must be followed, and that acquisitions of property must be based on valid mission requirements and an analysis of all viable alternatives.

Auditor Comments. We consider management's actions responsive to the recommendation.

Recommendation No. 2. We recommended that the Manager, Oak Ridge Operations Office, direct project managers to follow Departmental orders and require approvals of construction projects and property leases to include (a) verification that the projects are essential to meet mission requirements and (b) an analysis of viable alternatives.

Management Comments. Management concurred with the recommendation and stated that a memorandum will be developed and sent to all Operations Office assistant managers by November 14, 1997, directing them to follow Departmental orders and require approvals of construction projects and property leases to include proper verification and analyses.

Auditor Comments. We consider the planned action responsive to our recommendation.

Recommendation No. 3. We recommended that the Manager, Oak Ridge Operations Office, direct Energy Systems to give the required 365-day notice and discontinue the lease for the UVSPF.

Management Comments. Management did not concur. Management stated that the acquisition of the UVSPF was based on valid mission requirements as evidenced by the approval of senior Energy Systems management and the concurrence of the Department. Management stated that Energy Systems' approval and Departmental concurrence were based upon

programmatic knowledge of the need for the facility. Also, management stated that even though the evaluation of viable options contained in the PREP was not supported by a formal analysis, the standard real estate procedure was complied with by obtaining the concurrence of programmatic officials. Additionally, management stated that no formal assessment was prepared because the costs to renovate clearly exceeded the cost of leasing short-term, temporary space. Further, management stated that the work could not be contracted out because there were no other laboratories that could meet the detection limits and required delivery schedules proposed for bioassay analyses.

Management stated that the increases in the ASO's workload were accommodated by using existing facilities; however, the facilities were not designed for that type of analytical process. Management stated that the hood and duct systems in some of the laboratories were severely damaged or destroyed in the process. Also, management stated that if Energy Systems had not acquired the UVSPF, it would have had to replace the damaged hood and duct systems. Further, management stated that the large areas of floor space that were vacated would not have been suitable for bioassay or would have been suitable only after major modification.

Auditor Comments. We disagree with management's statement that Energy Systems' approval and the Department's concurrence is evidence that the acquisition of the UVSPF was based on valid mission requirements. Management's approvals were based on the statements made by Energy Systems in the PREP and not on the results of documented studies. Departmental Order 4300.1C states that program senior officials are responsible for ensuring that documented studies and proposals are made with full consideration of economy, efficiency, and programmatic needs. We concluded that the requirements of Order 4300.1C were not met in this instance because there were no documented studies showing the cost of renovation or contracting out. Contrary to management's statement that the work could not be contracted out, Energy Systems has identified two commercial laboratories which could meet the detection limits and required delivery schedules for environmental support and bioassay tests.

We believe the hood space which was severely damaged or destroyed is not needed based on the current workload, which has declined by about 40 percent since the lease was executed. Also, the required laboratory space is decreasing and the ASO is consolidating into less space.

Finding 2—Restrictive Specifications

Recommendation: We recommended that the Manager, Oak Ridge Operations Office, direct Energy Systems to discontinue the practice of restricting the location of facilities acquired or leased on the Department's behalf unless the restrictions are justified to meet mission requirements.

Management Comments. Management concurred with our recommendation. However, management disagreed with our conclusion that the geographic restriction gave an Energy Systems subcontractor a competitive advantage over other potential bidders and may have caused the Department to pay more than necessary for the facility. Management stated that the

subcontractor in question purchased land to construct the new facility, and land was available for other interested parties to purchase. Additionally, management stated that the low number of bidders was attributable to a combination of the special-purpose nature of the facility and the required 365-day cancellation notice. In response to our initial draft report, the Operations Office Contracting Officer issued a memorandum to Energy Systems stating that lease restrictions must be fully justified based on mission requirements.

Auditor Comments. We concluded that the subcontractor who purchased land in the delineated area, totaling about one-fourth of a square mile zoned for industrial use, had a competitive advantage over other potential bidders who did not already own or have ready access to land in the delineated area. We believe that the restrictive specification was the primary reason that only two responsive bids were received. As a result of the restriction and its effect on potential bidders, the Department may have paid more than necessary for the facility. Furthermore, we do not consider the action taken by the Operations Office responsive to our recommendation. The memorandum was presented as a reminder to Energy Systems to follow procedures, and it did not direct Energy Systems to change its current practices.

Estimated Monetary Impact

Management Comments. Management stated that the acquisition was planned to be a short-term, temporary requirement that would be replaced by a line item project within six years. Therefore, for renovation to be a less expensive alternative than leasing, the renovation cost would have to be less than the cost of leasing for six years. Since the UVSPF contains approximately 40,000 gross square feet and the cost of leasing for 6 years is \$4.8 million, renovation cost would have to be less than \$120 per square foot. Energy Systems stated that the cost to renovate would exceed \$400 per square foot, which significantly exceeds the break-even cost of \$120. Therefore, management stated that the cost of leasing is less than the cost to renovate and there is no monetary impact.

Auditor Comments. The estimated monetary impact was based on the Department's plan to spend \$4 million over the first 5 years for a facility which was not necessary. Management's comments suggest that the UVSPF was required to replace existing laboratory space in need of repair. However, the new facility was not justified as a replacement item. The new facility was justified in January 1992 to meet *an immediate and critical need* for additional space for increases in personnel. However, the increase in workload was handled in the existing facilities. By the time the UVSPF was ready for occupancy in October 1995, the workload had decreased significantly. Thus, we concluded the new facility was not needed.

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