Audit Report

OFFICE OF THE INSPECTOR GENERAL

ARMY CONTRACTING PROCEDURES ON CONTRACT DAAA21-91-C-0105 FOR M829A1 TANK AMMUNITION

Report No. 94-074 March 31, 1994

Department of Defense

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Acronyms

DCAA	Defense Contract Audit Agency
PCO	Procurement Contracting Officer

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884

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MEMORANDUM FOR AUDITOR GENERAL, DEPARTMENT OF THE ARMY

SUBJECT: Audit Report on the Army Contracting Procedures on Contract DAAA21-91-C-0105 for M829A1 Tank Ammunition (Project No. 4CF-5001)

Introduction

We are providing this final report for Army information and use. We performed the audit in response to a request from the Defense Contract Audit Agency (DCAA). In January 1993, during a postaward audit, DCAA reported on improper procurement procedures concerning contract DAAA21-91-C-0105, and in June 1993, requested the Inspector General, DoD, to review the procurement practices related to the contract.

Because of information received during a routine postaward audit, DCAA became concerned that contract DAAA21-91-C-0105 may have been awarded using procedures that conflicted with the requirements of Public Law 87-653, "Truth in Negotiations Act." DCAA was further concerned that the procurement contracting officer's (PCO) failure to request a preaward audit resulted in the unit price on contract DAAA21-91-C-0105 being higher than a similar, previously awarded contract, DAAA21-91-C-0008. DCAA was also concerned that the preaward audit was waived so as not to impede obligation of money.

DCAA suggested a review to determine if the PCO was negligent in the performance of his duties.

Audit Results

A review of contract files concerning the M829A1 tank ammunition and interviews with contracting and legal office personnel determined that, although the contract pricing did occur as reported by DCAA, contracting officials involved followed all applicable Federal and DoD acquisition regulations.

Objectives

The primary objective of the audit was to determine whether the Army followed Federal and DoD acquisition regulations when awarding contract DAAA21-91-C-0105. We also examined applicable internal controls.

Scope and Methodology

We performed the audit at the organizations listed in Enclosure 1. We reviewed files and records applicable to three contracts, valued at $246 million, for Army procurement of M829A1 tank ammunition. The documentation we reviewed covered the period 1990 through 1993.

We performed this economy and efficiency audit from October through November 1993 in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD. Accordingly, we included such tests of internal controls as were considered necessary. We did not use computer-processed data or statistical sampling procedures to perform the audit.

Internal Controls

We evaluated the effectiveness of the Army's internal controls applicable to the negotiation and award of contracts. This evaluation consisted of reviews of programmatic controls and contract records and interviews with contracting personnel. The internal controls and the Army's implementation of the DoD Internal Management Control Program applicable to the audit objectives were deemed to be effective in that the audit disclosed no material deficiencies.

Prior Audits and Other Reviews

No audits addressed this specific topic in the last 5 years.

Background

The Truth in Negotiations Act. The Truth in Negotiations Act protects the Government against defective pricing by contractors. The act requires contractors to submit certified cost or pricing data when adequate price competition does not exist. A price is "based on" adequate price competition if the proposed price results directly from price competition or if price analysis alone clearly demonstrates that the proposed price is reasonable in comparison with current or recent prices for the same or substantially the same items purchased in comparable quantities, terms, and conditions under contracts that resulted from adequate price competition. If such certified cost or pricing data are subsequently found to have been inaccurate, incomplete, or noncurrent as of the effective date of the certificate, the Government is entitled to reduce the price to what it would have been if the contractor had submitted accurate, complete, and current data. However, contracting officer reliance on the certified cost or pricing data is a critical element to proving any defective pricing.

Truth in Negotiations Act requirements are stated in Federal Acquisition Regulation 15.804-2, "Cost or Pricing Data," and Defense Federal Acquisition Regulation Supplement 215.804-3, "Cost or Pricing Data." Defense Federal Acquisition Regulation Supplement 215.804-3 further states that in dual-source awards, the PCO must determine whether adequate price competition exists.

Circumstances of Contract Award for Contract DAAA21-91-C-0008. On December 12, 1990, the contracting officer at the Army Armament, Munitions, and Chemical Command, Picatinny Arsenal, New Jersey, (Picatinny Arsenal) awarded contract DAAA21-91-C-0008 to Alliant Techsystems, Incorporated (Alliant), without a negotiated unit price because of an urgent need for M829A1 tank ammunition to support Operation Desert Storm. The unit price and a firm contract price were negotiated in August 1991, 8 months after the contractor began work on the contract.

Circumstances of Award for Contract DAAA21-91-C-0105. On September 30, 1991, Picatinny Arsenal awarded contract DAAA21-91-C-0105 to supplement contract DAAA21-91-C-0008 and to fulfill the FY 1992 Army requirement for M829A1 tank ammunition. Contract DAAA21-91-C-0105 was the result of a competitive dual-source procurement, which is a procurement in which the requirement is split into two portions. The low bidder (winner) is awarded the larger portion of the requirement and the high bidder (loser), the smaller portion. Alliant was the high bidder, thus receiving the loser's portion of the award, which was based on a preestablished quantity for the loser's share of the dual-source procurement. The unit price agreed to for contract DAAA21-91-C-0105 was higher than the unit price in contract DAAA21-91-C-0008.

Because Alliant believed that the Truth in Negotiations Act applied, and as advised by the PCO, Alliant did provide a certificate of cost or pricing data to the PCO on November 12, 1991, which certified the data for contract DAAA21-91-C-0105 as of September 18, 1991, the date Alliant submitted the cost or pricing data. Alliant provided the certificate because the PCO did not consider the loser's award to be competitive.

DCAA Concerns Resulting From Postaward Audit. The North Lakes Branch Office, DCAA, Minneapolis, Minnesota, initiated a postaward audit of contract DAAA21-91-C-0105, which DCAA routinely performs on selected noncompetitively awarded contracts.

During the postaward audit, DCAA received conflicting information from the PCO and the Picatinny Arsenal legal office about whether contract DAAA21-91-C-0105 was subject to Truth in Negotiations Act requirements. Picatinny Arsenal legal office personnel were apparently unaware that Alliant had received the loser's share of the award and, therefore, incorrectly told North Lakes Branch Office personnel that Truth in Negotiations Act requirements did not apply to the contract.

As a result, the North Lakes Branch Office terminated its postaward audit and sent a memorandum to the Director, DCAA, on January 29, 1993, that addressed the apparent faulty procurement practices on contract DAAA21-91-C-0105.

Discussion

Our audit disclosed that Picatinny Arsenal awarded contract DAAA21-91-C-0105 in compliance with Federal and DoD regulations, and the PCO was not negligent in performing his responsibilities.

Truth in Negotiations Act Applicability to the Contract. DCAA's concerns about the application of the Truth in Negotiations Act were unfounded, because the Truth in Negotiations Act does apply to contract DAAA21-91-C-0105. The Government did rely on Alliant's certified cost or pricing data in making the award. A defective pricing case could be made against Alliant, if warranted, and therefore, the Truth in Negotiations Act applies and DCAA can initiate a postaward audit.

Execution Date of Certificate. Alliant submitted the certificate of cost or pricing data 6 weeks after the contract award; however, Alliant properly certified the data as of September 18, 1991, the date Alliant submitted cost or pricing data. Although the certification was executed and provided to the PCO 6 weeks after the unit price was agreed to, the Truth in Negotiations Act still applied.

Government Reliance on Cost or Pricing Data. The PCO relied on Alliant's cost or pricing data submitted as of September 18, 1991, in awarding contract DAAA21-91-C-0105 to Alliant. The Picatinny Arsenal contracting office prebusiness clearance memorandum, dated September 21, 1991, stated that Alliant's proposed costs for the contract were accepted as certified. During our audit, the PCO verbally confirmed that he relied on Alliant's cost or pricing data in making the award to Alliant.

Legal Office Concerns. The Picatinny Arsenal legal office provided incorrect information to DCAA. The legal office thought Picatinny Arsenal awarded Alliant the winner's share in a dual-source competitive procurement and, therefore, was not subject to the Truth in Negotiations Act. The award of the winner's share of a dual-source competitive procurement is considered to be a competitive award. However, Picatinny Arsenal awarded Alliant the loser's share in a dual-source procurement. The Alliant contract was subject to the Truth in Negotiations Act because the PCO determined that adequate price competition did not exist in the award of the loser's share to Alliant and therefore the contract was subject to Truth in Negotiations Act requirements. In addition, the Picatinny Arsenal legal office mistakenly thought that the PCO did not rely on Alliant's submitted cost or pricing data in making the award to Alliant.

Higher Negotiated Unit Price. It is true that the September 18, 1991, certified unit price for contract DAAA21-91-C-0105 was higher than the unit price negotiated 1 month earlier, in August 1991, for contract DAAA21-91-C-0008; however, the lack of a preaward audit did not affect the agreed-upon unit price. The Army awarded contract DAAA21-91-C-0008 on December 12, 1990, without a negotiated unit price because of the urgent need for M829A1 ammunition to support Operation Desert Storm. Although the price was negotiated in August 1991, the price applied to the December 12, 1990, contract award and included costs incurred throughout that production period. The unit price awarded September 30, 1991, for contract DAAA21-91-C-0105 considered costs for the production period FYs 1992 through 1994 and included cost escalation beyond the period covered by contract DAAA21-91-C-0008.

PCO Cost-Realism Analysis. The PCO accepted the higher unit price for contract DAAA21-91-C-0105 based on the PCO's cost-realism analysis. The cost-realism analysis used data and rates from contract DAAA21-91-C-0008 as well as comparative analysis and data obtained from recent audit reports. The PCO also confirmed current rate information in telephone requests to DCAA. Although the cost-realism analysis resulted in costs of $4.9 million less than Alliant's proposed costs, the PCO was able to justify award at the proposed amount based on significant unanticipated cost growth on subcontracts at Government-owned and contractor-operated plants. The cost growth was attributable to a loss of business base by the plants, causing their overhead rates to increase.

Waived Preaward Audit. The PCO waived the preaward audit requirement for contract DAAA21-91-C-0105 because he was able to use recent audit information available from contract DAAA21-91-C-0008. The PCO believed sufficient information was available from other sources to properly analyze the price. To establish the reasonableness of the proposed price, the PCO used historical pricing data and a cost-realism analysis conducted by the Picatinny Arsenal contracting office. The PCO also considered the effect of a management adjustment, which reduced proposed costs by $8.1 million. The management adjustment was included by Alliant to make its proposal more competitive.

Year-end Spending. The requirement for this tank ammunition procurement was first determined in May 1991. The Army had set a milestone of mid-October 1991 for awarding the loser's share of the dual-source procurement. Picatinny Arsenal may have slightly expedited the procurement process to take advantage of the available FY 1991 funds, but the compressed award schedule was not considered significant. We concluded that the Picatinny Arsenal PCO did not abuse year-end spending authority.

Management Comments

DCAA Comments. We provided a draft of this report to the Army on January 26, 1993. Because the report contained no recommendations, no comments were required of management, and none were received from the Army. However, comments were received from DCAA. DCAA expressed

concern as to whether the Army PCO did in fact rely on the contractor's cost or pricing data to establish the Government's pricing position. Because a defective pricing case would depend on the PCO's reliance on the cost or pricing data, DCAA suggested that we obtain a written statement from the PCO or the buying office that the cost or pricing data were relied upon.

Audit Response. We have obtained a memorandum from the contracting officer at Picatinny Arsenal, dated March 1, 1994, stating that he fully relied on Alliant's cost or pricing data in developing a Government pricing position. A copy of the contracting officer's statement of reliance was provided to DCAA for use in any postaward evaluation of defective pricing of Alliant's certified cost or pricing data submission.

The courtesies extended to the audit staff are appreciated. If you have questions on this audit, please contact Mr. Salvatore D. Guli, Audit Program Director, at (703) 692-3025 (DSN 222-3025) or Mr. Bruce A. Burton, Audit Project Manager, at (703) 692-3118 (DSN 222-3118). Copies of this report will be distributed to the organizations listed in Enclosure 2. Audit team members are listed inside the back cover.

Robert J. Lieberman
Assistant Inspector General
for Auditing

Enclosures

Organizations Visited or Contacted

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition, Washington, DC

Department of the Army

Army Armament, Munitions, and Chemical Command, Army Materiel Command, Picatinny Arsenal, NJ
Auditor General, Department of the Army, Washington, DC

Defense Organizations

Defense Logistics Agency, Alexandria, VA
Defense Contract Audit Agency, Alexandria, VA
Field Office, Defense Criminal Investigative Service, Minneapolis, MN

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