Audit Report

SOLE-SOURCE PRICES FOR COMMERCIAL CATALOG AND NONCOMMERCIAL SPARE PARTS

Report No. 98-088 October 13, 1998

Office of the Inspector General
Department of Defense

This special version of the report has been revised to omit data considered "Boeing Proprietary."

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Acronyms

CICA	Competition In Contracting Act
CY	Calendar Year
DCMC	Defense Contract Management Command
DLA	Defense Logistics Agency
DISC	Defense Industrial Supply Center
DSCC	Defense Supply Center Columbus
DSCR	Defense Supply Center Richmond
FARA	Federal Acquisition Reform Act
FASA	Federal Acquisition Streamlining Act
FAR	Federal Acquisition Regulation
POPS	Paperless Order Processing System
SONIC	Spares Ordering Nonstop Inventory Control
TINA	Truth In Negotiations Act

INSPECTOR GENERAL
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October 13, 1998

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION AND TECHNOLOGY
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Redacted Audit Report on Sole-Source Prices For Commercial Catalog and Noncommercial Spare Parts (Report No. 98-088)

We are providing this redacted report for public release. We performed this audit in response to a complaint to the Defense Hotline. The complaint was substantiated. Although the audit indicated serious flaws in DoD procurement practices, it did not indicate violations of applicable laws and regulations by the contractor, the Boeing Company. DoD management comments on a draft of the report were considered in preparing the final report which was issued on a For Official Use Only basis on March 11, 1998.

We provided the For Official Use Only version of the report to the Boeing Company for its comments on information that could be company confidential or proprietary. Boeing's response contained an extensive discussion of its concerns about the potential harm to its competitive position from the public release of data Boeing considered "Boeing Proprietary" contained in the report.

We recognize that there are competing arguments in this area, and considerable litigation over the nature of the materials that should be considered proprietary, and the extent of which that information is entitled to protection. In the interest of an early public release of the report, and without conceding the validity of each of the arguments advanced by Boeing, we have decided to use for public release a redacted version of the report that deletes all data that could be considered Boeing Proprietary.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Terry L. McKinney, Audit Program Director, at (703) 604-9288 (DSN 664-9288) or Mr. Henry F. Kleinknecht, Audit Project Manager, at (703) 604-9324 (DSN 664-9324). See Appendix H 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. 98-088 **October 13, 1998**
(Project No. 6CF-0068.01)

Sole-Source Prices for Commercial Catalog and Noncommercial Spare Parts

Executive Summary

Introduction. This is the second of two reports in response to complaints to the Defense Hotline. This report discusses a complaint that the Defense Logistics Agency (DLA) was procuring commercial and noncommercial items from the Boeing Company (Boeing) on a sole-source basis at excessive prices. The first report discussed a similar complaint involving another company. We focused our review on 179 sole-source orders to Boeing - 136 orders valued at $25,000 or more and 43 orders valued at less than $25,000 - issued by DLA during calendar years (CYs) 1994 through 1996. These orders were for such items as structural panels, fittings, and supports, along with washers, bolts, and nuts. The 179 orders totaled $12 million; 126 of the orders were placed during CY 1996 and totaled $7.5 million. These orders represent only 14 percent of the total Boeing military replenishment spare parts sales of $55.2 million in that year.

Audit Objectives. The primary audit objective was to determine whether there was merit to the Defense Hotline complaint. Specifically, the complainant alleged that DLA was paying much more for commercial and noncommercial items procured from Boeing on a sole-source basis than had been previously paid by the Air Force when the parts were procured competitively. We also addressed the adequacy of the DLA management control program as it pertained to the audit objectives.

Audit Results. The complaint was substantiated. DLA purchased commercial catalog and noncommercial spare parts from Boeing on a sole-source basis, principally because those items were mistakenly coded by DLA as sole-source when inventory management responsibility was transferred from the Air Force. The sole-source prices were significantly higher than the competitive prices DoD previously paid for the items. Based on our analysis of previous competitive procurements for the same items, DLA paid an average of about 172 percent or $3.2 million more than the fair and reasonable prices. DLA also charged its customers an average cost recovery rate of 28 percent (about $2 million) for its services in procuring Boeing commercial catalog items. The DLA provided questionable value for those charges and the DoD was not reaping the benefits foreseen for the DLA corporate contracting initiative.

Summary of Recommendations. We recommend that the Under Secretary of Defense for Acquisition and Technology take appropriate action to provide the Military Departments with local purchase authority for centrally managed commercial items, when sources other than DLA offer the best value. We recommend that the Director, DLA improve management controls for sole-source procurements, commercial item pricing, and corporate contracting.

Management Actions and Comments. The Under Secretary of Defense for Acquisition and Technology concurred with the report and is taking appropriate action to provide appropriate local purchase authority for centrally managed commercial items. DLA also took aggressive action and on June 9, 1997, the Deputy Director Material Management, DLA sent a memorandum " Action Items from DoD Inspector General (IG) Brief," to the DLA supply centers. It discussed tentative audit findings that had been briefed to DLA management and identified audit issues requiring command attention. Action items included determining whether the Boeing contracts were being used as intended and whether corporate contracts were providing value to DLA customers. The memorandum also addressed a voluntary refund request for overpriced spare parts, coding competitive items correctly, establishing competitive cost baselines before using corporate contract price lists, and procuring future items competitively. Although DLA concurred with the recommendation to DLA and generally agreed with the finding, it disagreed with the specific causes. The DLA generally maintained that no options were available other than to purchase from the Boeing catalog. DLA asserted that the primary causes for excessive prices were the unavailability of the manufacturing drawings and associated technical data necessary to award spare part orders competitively, and Boeing's unwillingness to depart from its policy of selling commercial items at listed price only. DLA also commented that conclusions reached from its vendor stock retention model and price analysis supported award of the corporate contract to Boeing. See Part III for the full text of the comments.

Audit Response. We appreciate the Department's overall responsiveness to the audit results. Unfortunately, the conclusions reached by DLA from its vendor stock retention model and price analysis used to support award of the Boeing corporate contract are seriously flawed and cannot be used to show savings from direct vendor delivery or that the Boeing catalog prices were fair and reasonable. See Appendix E for specific discussion on those DLA conclusions and other comments.

This is the second report issued by this office in FY 1998 addressing problems in a DLA corporate contract arrangement where a mix of commercial and noncommercial materiel was purchased on a sole-source basis. In both cases, the prices being paid were excessive, both in terms of overall value received and in comparison to previous prices for the same items. We agree with the Department's overall strategy of using the lessons learned from our work and possibly from other sources to develop more effective training for DoD acquisition personnel on being astute buyers in the new acquisition environment.

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Part I - Audit Results

Introduction

This report resulted from a review of a complaint to the Defense Hotline, and is the second of two reports on Hotline cases involving commercial pricing of spare parts. This report discusses an allegation that the Defense Logistics Agency (DLA) was procuring commercial and noncommercial items from The Boeing Company (Boeing) on a sole-source basis. The sole-source prices were significantly higher than the competitive prices previously paid by DoD for the items. The first report discussed an allegation that DLA paid another contractor significantly higher catalog prices for commercial items than the cost-based prices previously paid for the items. The allegation was substantiated. A third audit is in process to evaluate similar issues, but is not Hotline related.

We focused our review on 179 orders to Boeing - 136 orders valued at $25,000 or more and 43 orders valued at less than $25,000 - issued by DLA during calendar years (CYs) 1994 through 1996 on contracts F34601-92-G-0024 (92-G-0024), F42600-94-G-7559 (94-G-7559), and SPO400/500-96-D-9501 (96-D-9501). Contract 96-D-9501, a new DLA corporate contract (contract for commercial items that can be used by any supply center), and contract 92-G-0024 were used to purchase commercial catalog items. Contract 94-G-7559 was used to purchase noncommercial military items. The 179 orders totaled $12 million. Of the 179 orders reviewed, 124 orders totaling $7.5 million were purchased from Boeing's commercial catalog and parts on 86 orders totaling $4.9 million ($5 million in 1997 constant dollars) had previously been procured competitively from small businesses. The items DLA procured from Boeing included structural panels, fittings, and supports, along with washers, bolts, and nuts. Of the 179 orders we reviewed, 126 were placed during CY 1996 totaling $7.5 million. These orders represent 14 percent of the total Boeing replenishment spare parts sales of $55.2 million to DoD in that year.

Audit Background

DLA Mission. DLA is the central combat support agency that manages supplies in various commodity areas such as, clothing, construction material, electronic supplies, fuel, food, general supplies, and medical supplies. DLA uses five supply centers to procure supplies.

- Defense Supply Center, Columbus, Ohio, (DSCC);
- Defense Fuel Supply Center, Fort Belvoir, Virginia;
- Defense Supply Center Richmond, Virginia, (DSCR);
- Defense Industrial Supply Center, Philadelphia, Pennsylvania, (DISC);
- Defense Personnel Support Center, Philadelphia, Pennsylvania;

DLA supply centers consolidate the Services' requirements and procure the supplies in sufficient quantities to meet the Services' needs. Supplies are stored and distributed through a complex of depots or by direct vendor delivery. Consolidation of the distribution functions of the military Services and DLA depots was begun in 1990 and completed in March 1992, creating a single, unified supply distribution system managed by DLA. The DLA also provides contract administration services through its Defense Contract Management Command (DCMC). DCMC has offices throughout the world located primarily at or near contractor plants. DCMC professionals provide preaward, post-award, and contract close-out services. The DLA civilian end strength has declined from 60,649 employees in FY 1993 to 44,307 in FY 1998 as part of the overall DoD downsizing.

Consolidation of Inventory Control Points. On July 3, 1990, the Deputy Secretary of Defense approved the recommendation in Defense Management Report Decision 926, "Consolidation of Inventory Control Points," to transfer item management responsibility for approximately one million consumable items from the Military Services to DLA. The report concluded that the transfer of consumable items to DLA was both cost effective and desirable, and would produce an estimated recurring annual savings of between $45 to $49 million (FY 1989 dollars) beginning in FY 1995.

Truth In Negotiations Act and Cost or Pricing Data. Congress historically has expressed concern with the use of other-than-competitive contracts, which were typically negotiated between the parties. These noncompetitive contracts provide additional risks for the Government to pay unreasonable prices and for contractors to earn excessive profits. Based on these concerns, Congress passed the Truth in Negotiations Act (TINA), Public Law 87-653, September 10, 1962, that required contractors to submit cost or pricing data before the award of a negotiated contract; and to certify that the data were accurate, complete, and current. The purpose of TINA was to provide the Government with all the facts on cost and pricing that the contractor used to prepare the proposal, in order for the Government to avoid paying excess prices and profits. Throughout the years, amendments have modified TINA requirements and the appropriate statutory authority is now United States Code, title 10, section 2306a (10 U.S.C. 2306a).

Previous Price Issues. In the 1980's, various audits, congressional investigations and media disclosures indicated that DoD paid excessive prices for many spare parts and supplies, often sole-source procurements from contractors who did not manufacture the items. The disclosures caused both DoD and the Congress to take action to improve procurement prices on DoD spare parts.

Procurement Initiatives. In 1983, the Secretary of Defense directed the Military Departments and the DLA to implement 35 procurement initiatives to reduce overpricing. The initiatives focused on correcting problems related to overspecification, overengineering, small-quantity purchases, inappropriate allocation of corporate overhead in the pricing of individual contract line items, purchasing from other than the actual manufacturer, noncompetitive procurements, and excessive profits. The Competition in Contracting Act of 1984 (CICA), Public Law 98-369, July 18, 1984, established a statutory preference for the use of competitive procedures in awarding Federal contracts for property or services. The Act required Federal agencies to use competitive procedures to purchase goods or services unless a statutory exception existed, and required agencies to appoint a competition advocate to challenge competition barriers. Additional staffing was authorized to identify items for competitive procurements or procurement from the manufacturer rather than from the prime weapons systems contractor (breakout) and to perform more thorough cost and price analyses of items being procured

An article on the benefits of the Competition in Contracting Act in the "Public Contract Law Journal," October 1983, written by the Honorable William S. Cohen (current Secretary of Defense) described the benefits of competition and concluded:

> The Competition in Contracting Act builds on the existing statutes to enhance the use of competition in government contracting and to restrict sole-source procurement to only those cases where it is truly required The Congressional Budget Office [CBO] estimated that "significant" savings could be achieved through the effective implementation of S 338 The CBO estimates that each 1 percent saved on new contract actions reduces costs by about $200 million per year Since studies on the use of competitive contracting have concluded that potential savings range from 15 to 50 percent, a conservative estimate of the savings resulting from this bill would be over $2 billion
>
> While it is important to recognize that, in some cases, the Defense Department and civilian agencies cannot contract competitively, the committee found that agencies routinely award sole-source contracts for property and services when competition was available. I strongly believe that the Competition in Contracting Act sets forth a workable solution to the costly problem of excessive sole-source contracting.

Implementation of the Act and the 35 spare parts procurement initiatives resulted in dramatic increases in reported competitive procurements and savings from 1985 to 1988. Throughout the years, amendments have modified CICA requirements and the appropriate statutory authority is now 10 U.S.C. 2304, "Contracts: Competition Requirements."

After FY 1986, the DoD budget for spare parts began to decline and intensive management of spare parts procurements also began to decline. Competition advocate organizations at the buying centers eventually became targets for reductions or reorganization, and breakout screening became more selective.

Acquisition Reform Legislation. By the early 1990's, Congress and the Executive Branch reached a consensus that it was difficult to make sense out of the complex procurement system because of the proliferation of often contradictory requirements governing almost every aspect of the acquisition process. Congress commissioned an Advisory Panel on Streamlining and

Codifying Acquisition Laws pursuant to Section 800 of the National Defense Authorization Act for FY 1991. In January 1993, the panel completed its report and recommended a comprehensive overhaul of the federal procurement laws to:

> Improve Government access to commercial technologies;
>
> Reduce administrative overhead, especially in light of anticipated reductions in the federal acquisition workforce; and
>
> Reverse a perceived trend toward the incremental enactment of procurement statutes without a clear analysis of their impact on the overall acquisition system [Senate Report 103-258]

In 1993, the Government-wide National Performance Review, headed by the Vice President, reinforced the recommendations made by the advisory panel. The National Performance Review report "From Red Tape to Results: Creating a Government that Works Better and Costs Less," also made recommendations to increase reliance on acquisitions of commercial items, increase the simplified acquisition threshold, and implement other streamlining measures.

In May 1994, Secretary of Defense William Perry described fundamental acquisition reform as his number one priority. The Secretary identified three primary defects in the current system:

> (1) DoD is unable to acquire state of the art commercial technology
>
> (2) DoD is often unable to buy from commercial companies - even when their costs are cheaper. . .
>
> (3) DoD's costs of doing business are too great

The Secretary of Defense also commented that:

> Because the world in which DoD must operate has changed beyond the limits of the existing acquisition system's ability to adjust or evolve - the system must be totally re-engineered If DoD is going to be capable of responding to the demands of the next decade, there must be carefully planned, fundamental re-engineering or re-invention of each segment of the acquisition process.

On October 13, 1994, Congress enacted Public Law 103-355, the "Federal Acquisition Streamlining Act of 1994," (FASA). The purpose of FASA was to:

> . . . revise and streamline the acquisition laws of the Federal Government in order to reduce paperwork burdens, facilitate the acquisition of commercial products, enhance the use of simplified procedures for small purchases, clarify protest procedures, eliminate unnecessary statutory impediments to efficient and expeditious acquisition, achieve uniformity in the acquisition practices of Federal agencies, and increase the efficiency and effectiveness of the laws governing the manner in which the Government obtains goods and services. [Senate Report 103-258]

On February 10, 1996, Congress enacted Public Law 104-106, the "National Defense Authorization Act For Fiscal Year 1996." Division D of the Act was titled the "Federal Acquisition Reform Act of 1996," (FARA). FARA contained various provisions adopted by Congress on competition, commercial items, and other acquisition reform measures.

Audit Objectives

The primary audit objective was to determine whether there was merit to a complaint made to the Defense Hotline. Specifically, the complainant alleged that DLA was paying several hundred percent more for commercial catalog and noncommercial items procured from Boeing on a sole-source basis than DoD previously paid when the items were procured competitively. We also reviewed the adequacy of the management control program as it applied to the other audit objectives. See Appendix A for a discussion of the audit scope and method-ology and the review of the management control program. Appendix B summarizes prior coverage related to the audit objectives.

Sole-Source Prices for Spare Parts

The Defense Logistics Agency (DLA) purchased commercial catalog and noncommercial spare parts from The Boeing Company (Boeing) on a sole-source basis. The sole-source prices were significantly higher than the competitive prices DoD previously paid for the items. This occurred because the DLA acquisition team:

- did not evaluate and implement procedures to effectively use the Boeing "Rights Guard" program established by the Air Force to breakout and compete Boeing spare parts by securing limited rights in Boeing's technical data and incorrectly coded items transferred from the Air Force to reflect that they were for noncompetitive acquisition, when in fact those items had previously been competitively procured;

- did not perform adequate price analysis of previous competitive buys to determine whether Boeing sole-source prices were fair and reasonable or whether the items should have been procured competitively;

- accepted Boeing commercial catalog prices as fair and reasonable without adequate support for price reasonableness, particularly when DoD was the "primary" customer and there was no competitive commercial market to ensure price integrity; and

- implemented a corporate contracting initiative whose benefits, in this case, failed to justify its disadvantages.

As a result, DLA paid an average of about 172 percent or $3.2 million (in 1997 constant dollars) more than previous competitive prices for the $5 million of sole-source spare parts purchased from Boeing during CYs 1994 through 1996. DLA also charged its customers a cost recovery rate of about 28 percent ($2 million) for its services in procuring Boeing commercial catalog items. The DLA provided questionable value for those services and DoD was not reaping the benefits foreseen from the DLA corporate contracting initiative. In response to the audit, the DLA took extensive corrective action.

Laws and Regulations

Competition in Contracting Act. 10 U.S.C. 2304 provides generally that the head of an agency, in procuring property and services, shall obtain full and open competition through the use of competitive procedures, or a combination of procedures, that is best suited under the circumstances. The law provides specific exceptions that would allow noncompetitive procedures, such as preservation of the industrial base, lack of alternative sources, or unusual and compelling urgency. Lack of advance planning or the discovery of funding constraints are not justifications for sole-source procurements. Even for procurements under the simplified acquisition procedures, the Government is required to promote competition to the maximum extent practicable. These statutory requirements are implemented in the FAR and agency supplements to the FAR.

Guidance on competition requirements is found in FAR 6.101, "Policy":

> (a) 10 U S.C 2304 and 41 U S C 253 require, with certain limited exceptions (see Subparts 6 2 and 6.3), that contracting officers shall promote and provide for full and open competition in soliciting offers and awarding Government contracts.
>
> (b) Contracting officers shall provide for full and open competition through use of the competitive procedure(s) contained in this subpart that are best suited to the circumstances of the contract action and consistent with the need to fulfill the Government's requirements efficiently (10 U S.C 2304 and 41 U.S.C 253).

Guidance on soliciting competition when using simplified acquisition procedures is found in FAR 13.106-2, "Purchases exceeding the micro-purchase threshold [$2,500]":

> (a) *Soliciting competition* (1) Contracting officers shall promote competition to the maximum extent practicable to obtain supplies and services from the source whose offer is the most advantageous to the Government, based, as appropriate, on either price alone or price and other factors (e g., past performance and quality) including the administrative cost of the purchase. Contracting officers are encouraged to use best value Solicitations shall notify suppliers of the basis upon which award is to be made

Since the draft was issued, FAR part 15 has been substantially rewritten, and FAR 15.8 was revised and moved within the Chapter. We have revised our citations to reflect where the provisions are currently found, as we believe that the substance of the provisions remained relatively the same.

Guidance and an order of preference for contracting officers in determining the type of information required when negotiating prices for supplies and services is found in FAR 15.402, "Pricing policy":

> Contracting officers shall--
>
> (a) Purchase supplies and services from responsible sources at fair and reasonable prices. In establishing the reasonableness of the offered prices, the contracting officer shall not obtain more information than is necessary To the extent that cost or pricing data are not required by 15.403-4, the contracting officer shall generally use the following order of preference in determining the type of information required
>
> (1) No additional information from the offeror, if the price is based on adequate price competition, except as provided by 15 403-3(b).
>
> (2) Information other than cost or pricing data
>
> (i) Information related to prices (e.g , established catalog or market prices or previous contract prices), relying first on information available within the Government, second, on information obtained from sources other than the offeror; and, if necessary, on information obtained from the offeror When obtaining information from the offeror is necessary, unless an exception under 15 403-1(b)(1) or (2) applies, such information submitted by the offeror shall include, at a minimum, appropriate information on the prices at which the same or similar items have been sold previously, adequate for evaluating the reasonableness of the price
>
> (ii) Cost information, that does not meet the definition of cost or pricing data at 15 401
>
> (3) *Cost or pricing data* The contracting officer should use every means available to ascertain whether a fair and reasonable price can be determined before requesting cost or pricing data. Contracting officers shall not require unnecessarily the submission of cost or pricing data, because it leads to increased proposal preparation costs, generally extends acquisition lead time, and consumes additional contractor and Government resources

(b) Price each contract separately and independently and not--

(1) Use proposed price reductions under other contracts as an evaluation factor, or

(2) Consider losses or profits realized or anticipated under other contracts

(c) Not include in a contract price any amount for a specified contingency to the extent that the contract provides for a price adjustment based upon the occurrence of that contingency

Guidance for contracting officers reviewing contractor proposals is found in FAR 15.404, "Proposal analysis":

15.404-1 Proposal analysis techniques.

(a) *General* The objective of proposal analysis is to ensure that the final agreed-to price is fair and reasonable

(1) The contracting officer is responsible for evaluating the reasonableness of the offered prices The analytical techniques and procedures described in this subsection may be used, singly or in combination with others, to ensure that the final price is fair and reasonable The complexity and circumstances of each acquisition should determine the level of detail of the analysis required

(2) Price analysis shall be used when cost or pricing data are not required (see paragraph (b) of this subsection and 15 404-3)

(3) Cost analysis shall be used to evaluate the reasonableness of individual cost elements when cost or pricing data are required Price analysis should be used to verify that the overall price offered is fair and reasonable

(4) Cost analysis may also be used to evaluate information other than cost or pricing data to determine cost reasonableness or cost realism

(b) *Price Analysis* (1) Price analysis is the process of examining and evaluating a proposed price without evaluating its separate cost elements and proposed profit

(2) The Government may use various price analysis techniques and procedures to ensure a fair and reasonable price, given the circumstances surrounding the acquisition Examples of such techniques include, but are not limited to the following:

(i) Comparison of proposed prices received in response to the solicitation

(ii) Comparison of previously proposed prices and contract prices with current proposed prices for the same or similar end items, if both the validity of the comparison and the reasonableness of the previous price(s) can be established

(iii) Use of parametric estimating methods/application of rough yardsticks (such as dollars per pound or per horsepower, or other units) to highlight significant inconsistencies that warrant additional pricing inquiry

(iv) Comparison with competitive published price lists, published market prices of commodities, similar indexes, and discount or rebate arrangements.

(v) Comparison of proposed prices with independent Government cost estimates.

(vi) Comparison of proposed prices with prices obtained through market research for the same or similar items

Sole-Source Prices for Spare Parts

DLA purchased commercial catalog and noncommercial spare parts from Boeing on a sole-source basis. The sole-source prices were significantly higher than the competitive prices DoD previously paid for the items. Of the 179 orders reviewed totaling $12 million, parts on 86 orders totaling $4.9 million, had previously been procured competitively from small businesses. DLA paid about $3.2 million (in 1997 constant dollars) or an average of about 172 percent, more than previous competitive prices for the sole-source spare parts purchased from Boeing during CYs 1994 through 1996. See Appendix C, "NSN, Boeing Part Number, Item Description, and Contract," for a complete list of the Boeing items reviewed.

Over the years, DoD has devoted significant resources to spare parts breakout from prime contractors such as Boeing. The Defense Federal Acquisition Regulation Supplement, Appendix E, "DoD Spare Parts Breakout Program," provides policies and procedures for management of the program. "The objective of the DoD Spare Parts Breakout Program is to reduce costs through the use of competitive procurement methods, or the purchase of parts directly from the actual manufacturer rather than the prime contractor, while maintaining the integrity of the systems and equipment in which the parts are to be used." The DLA acquisition team (management, contracting officers, cost and price analysts,

procurement analysts, item managers, and technical support representatives) failed to breakout the Boeing spare parts and paid higher sole-source prices to the prime contractor. Higher prices were paid because items were incorrectly coded as sole source, adequate price analysis was not performed, Boeing commercial prices were injudiciously accepted as fair and reasonable, and DLA implemented a corporate contracting initiative without adequate management controls.

The Boeing "Rights Guard" Program

History of the "Rights Guard" Program. The issue of data rights to the KC-135 aircraft (military derivative of the Boeing 707 aircraft) technical data began in 1955. From the beginning there was uncertainty as to whether the Government had originally acquired the right to use technical data furnished by Boeing for the competitive procurement of replenishment spare parts. In 1974, a consensus of opinion was reached that a 1973 contract provided an understanding between Boeing and the Government that data ownership would not be questioned, provided that Boeing allowed the Government to use the technical data for competitive purposes. The original agreement allowed DoD to competitively procure replenishment spare parts and covered only data pertaining to the KC-135 aircraft, but was subsequently broadened to include technical data pertaining to military derivatives of the 707, 727, 737, and 747 commercial aircraft, including but not limited to the KC-135 series, VC-25, VC-137, C-18, C-22, E-3A, E-4, and T-43 aircraft.

The "Rights Guard" agreement, as it has been known since 1986, is a research and reproduction services type contractual arrangement, wherein DoD may order technical data from Boeing. The agreement permits DoD to supply the technical drawings to suppliers for bidding and manufacturing purposes. In return, DoD requires the offerors and awardees to destroy or return the data to DoD thus the term "Rights Guard." The Air Force requires all contractors to whom "Rights Guard" data are provided to submit an annual certification stating that they will comply with the "Rights Guard" agreement. The Air Force, through the Oklahoma City, Air Logistics Center, (OC-ALC) awards and manages the

Rights Guard contract. Without the "Rights Guard" agreement, items could not be procured competitively. Instead Boeing would be the sole-source supplier.

Air Force Procedures to Use the Boeing "Rights Guard" Program. OC-ALC had established procedures to screen all spare parts for breakout where Boeing was the prime contractor regardless of the dollar value. Once it was determined that a part could be procured competitively, the part was assigned a competitive acquisition method code (1G or 2G). Then as part of the procurement solicitation, OC-ALC sent any prospective bidder that had submitted its annual "Rights Guard" certification, a complete set of technical drawings for the spare parts being solicited. The OC-ALC competition advocate indicated that about 95 percent of the Boeing spare parts were competitively coded and that before the consumable item transfer to DLA, OC-ALC maintained hundreds of "Rights Guard" agreements with small businesses. In 1992, OC-ALC calculated that during FYs 1988 through 1991, the "Rights Guard" program was used to competitively procure about 3,500 items at a reduced cost of $13 million.

DLA Procedures to Use the "Rights Guard" Program. After the transfer of acquisition responsibility for the items to DLA, the DLA acquisition team failed to evaluate and implement procedures to effectively use the Boeing "Rights Guard" program to breakout and compete Boeing spare parts. DSCC officials indicated that problems with the first phase of the consumable items transfer such as incomplete or missing technical data packages hindered efforts to evaluate and implement procedures to use the Boeing "Rights Guard" program. However, the memorandum of agreement between the Air Force Logistics Command and DLA provided explicit procedures to resolve cases of missing or illegible technical data during the consumable item transfer. DLA had neither taken aggressive action to obtain "Rights Guard" agreements from small businesses nor obtained the technical data needed to procure parts competitively. Therefore, in those instances when competition was solicited, DLA could not provide small businesses with copies of the technical drawings. In fact, for many of the Boeing items, the DLA contract technical data file states "Adequate data for evaluation of alternative offers is not available at the procurement agency. The offeror must provide a complete data package including data for the approved and alternate part for evaluation." Unfortunately, under the "Rights Guard" program, the offerors are not permitted to maintain copies of the technical data. Therefore, DLA basically eliminated small businesses from providing offers and had no choice but to procure the items from the prime contractor, Boeing. DLA also incorrectly coded items that transferred from the Air Force as noncompetitive.

We identified 38 different orders where the Boeing spare parts had been coded by the Air Force with a competitive acquisition method code, but after the transfer to DLA, were coded as noncompetitive (DSCR 21, DSCC 12, DISC 3). In addition, although 28 items were correctly coded with competitive procurement codes, the parts were procured sole-source from Boeing. All of the parts on the 179 orders reviewed, were either covered by the "Rights Guard" program (159 items) or DoD owned the technical data rights (20 items). See Appendix D, "Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts," for the details.

Price Analysis of Previous Competitive Procurements

Price Analysis for Boeing Commercial Catalog and Noncommercial Items. DLA contracting officers did not perform adequate price analysis of previous competitive buys to determine whether Boeing commercial catalog and noncommercial sole-source prices were fair and reasonable, or whether the items should have been procured competitively. Boeing commercial catalog and noncommercial sole-source prices for 86 orders with previous competitive procurement histories were significantly higher than previous competitive prices paid by DoD. To determine the cost impact in 1997 constant dollars, we used DoD deflators from the "National Defense Budget Estimates for FY 1997," April 1996, to calculate Boeing commercial catalog and noncommercial prices and previous competitive prices in constant 1997 dollars. Contracts 92-G-0024 and 96-D-9501 were used to purchase commercial catalog items, and contract 94-G-7559 was used to purchase noncommercial military items.

Table 1 shows that Boeing commercial catalog and noncommercial prices for spare parts were about $3.2 million or 172 percent (median 210 percent) higher than previous DoD competitive prices.

Table 1. Boeing Commercial Catalog and Noncommercial Prices Were Significantly Higher Than Previous Competitive Prices

		Total Boeing Catalog or Noncommercial Price		Previous DoD Competitive Total Price		Percent Increase	
Contract	Number of Orders	Delivery Orders	1997 Dollars*	1997 Dollars*	Increase	Mean	Median
92-G-0024	28	$1,486,644	$1,546,987	$490,294	$1,056,693	216	215
94-G-7559	20	1,952,530	2,008,810	780,020	1,228,790	158	213
96-D-9501	38	1,459,489	1,490,867	588,065	902,802	154	210
Total	**86**	**$4,898,663**	**$5,046,664**	**$1,858,379**	**$3,188,285**	**172**	**210**

*1997 dollars were calculated using the DoD deflators from the "National Budget Estimates for FY 1997," April 1996

Table 2 shows that the total price increases were slightly higher when the 1997 Boeing catalog prices were used instead of the previous Boeing catalog prices inflated to 1997 dollars. Price increases for the items on the noncommercial contract (94-G-7559) are constant in both tables.

Table 2. 1997 Boeing Commercial Catalog and Noncommercial Prices Were Significantly Higher Than Previous Competitive Prices

		Total Boeing Catalog or Noncommercial Price		Previous DoD Competitive Total Price		Percent Increase	
Contract	Number of Orders	Delivery Orders	1997 Dollars*	1997 Dollars*	Increase	Mean	Median
92-G-0024	28	$1,486,644	$1,638,920	$490,294	$1,148,626	234	296
94-G-7559	20	1,952,530	2,008,810	780,020	1,228,790	158	213
96-D-9501	38	1,459,489	1,528,600	588,065	940,535	160	210
Total	**86**	**$4,898,663**	**$5,176,330**	**$1,858,379**	**$3,317,951**	**178**	**210**

*1997 dollars were calculated using the 1997 Boeing Commercial Catalog for contracts 92-G-0024 and 96-D-9501 and the DoD deflators from the "National Budget Estimates for FY 1997," April 1996, for contract 94-G-7559.

Price increases for individual items ranged even higher. For example, in February 1996, DSCC purchased 246 units of NSN 1650-00-692-7488, a spoiler actuator sleeve, on contract 92-G-0024 at the Boeing commercial unit price of $395. In the price negotiation memorandum, the DSCC contracting officer stated that the item was sole source to Boeing. The 1997 Boeing catalog price that we are using for our comparison is $403.49 for a total price based on purchasing 246 units of $99,259. In September 1993, OC-ALC awarded a competitive order to a small disadvantaged business for 224 units of the same item at a unit price of $22.95. Competitive solicitations were sent to 20 contractors including Boeing, bids were received from 8 of the contractors, and the contractor that was awarded the order had been awarded two previous orders for the item in 1988 and 1989. The competitive unit price in 1997 dollars is $24.72 for a total price based on purchasing 246 units of $6,081 or saving from the 1997 Boeing catalog price of $93,178. The 1997 Boeing catalog price for this item is 1,532 percent higher than the competitive price. In addition, Boeing neither negotiates nor provides discounts from its commercial catalog prices to any customers, including DoD.

Boeing Commercial Catalog Prices

Accepting Commercial Catalog Prices as Fair and Reasonable. DLA contracting officers accepted Boeing commercial catalog prices as fair and reasonable without adequate support for price reasonableness, even when DoD was the "primary" customer procuring significantly larger quantities than other commercial customers and there was no competitive commercial market to ensure the price integrity. The contracting officers made no attempt to exert the leverage that a major customer ought to be able to exert to negotiate significant discounts, as is common commercial practice.

For example, in December 1995 a DSCR contracting officer purchased 25 structural supports from NSNs 1560-01-273-4323 and 1560-01-273-4324. These items were purchased at the same commercial catalog unit price of $19,334 with each order totaling $483,350 from contract 92-G-0024. Prices for these items were listed in the Boeing Spares Ordering Nonstop Inventory Control System (SONIC) -- the on-line commercial catalog listing. The contracting officer determined that the prices were fair and reasonable based on the items being commercially priced and listed in the Boeing SONIC system which were previously reviewed and approved by DCMC Boeing. From 1994 through 1996, Boeing sold non-Government commercial customers a total of three and four units of each part, respectively. DoD last procured the parts in December 1983 from Boeing when 15 of the parts were procured at a unit price of $1,229.65. Inflating the 1983 unit price to 1997 dollars ($1,663.35) and comparing that price to the 1997 Boeing catalog price ($20,040) shows that prices for the parts have increased 1,105 percent or $459,416 on each order. Appendix E (of the draft report), Issue 2, showed other examples where the 1997 Boeing commercial catalog prices were significantly higher than previous Boeing prices.

There is some confusion as to why the DLA contracting officers accepted Boeing commercial catalog prices as fair and reasonable. Documentation in the DLA contract files indicates that DCMC Boeing reviewed and approved prices in the Boeing SONIC system as fair and reasonable because a published price list exists that is available to commercial customers. Based on this documentation, DLA contracting officers accepted the Boeing commercial catalog prices as fair and reasonable even though price analysis identified large price increases with no explanation. Our conversations with DCMC Boeing representatives determined that they never indicated DLA contracting officers should accept Boeing's commercial catalog prices as fair without further review.

Similar Quantities and Substantial Non-Government Sales. Commercial sales information was obtained from Boeing for the part numbers procured on the 124 DLA commercial catalog orders reviewed. The sales data from 1994 through 1996 was used to determine whether DoD or non-Government commercial customers purchased the largest quantities and highest percentage of each item. For each of the 124 DLA commercial item orders, we plotted the point on the Y axis "DLA Order Quantity to Largest Commercial Order Quantity Ratio" based on the quantity of items purchased on each individual DLA order compared to the highest non-Government commercial quantity buy for the item. We developed a

multiple factor based on how many times the DLA order quantity was greater than the highest non-Government order quantity during the period and vice versa. For example, if DLA purchased 100 parts on an order and the highest quantity sold to a non-Government commercial customer for the same part was 5, then DoD purchased 20 times more than any commercial customer. We plotted the point on the X axis "DoD Sales as a Percent of Total Sales" based on the percent of DoD sales compared to total Boeing commercial sales for the item. For example, if Boeing had total sales of 500 for a specific commercial item during the period and DoD purchased 250 of the items, then the point would be plotted on the X axis at 50 percent.

Figure 1 shows that for the majority of the items, DoD purchased significantly larger quantities of individual commercial items measured in multiples of the highest quantity purchased by a non-Government commercial customer and a higher percentage of the overall sales of the commercial items.

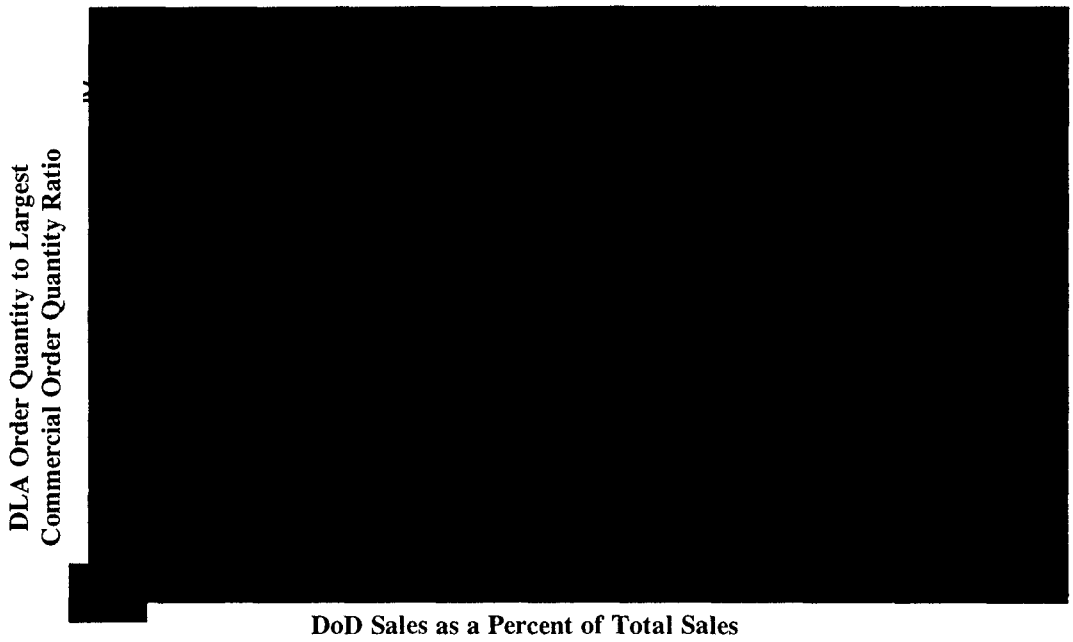

Figure 1. DoD Purchased Larger Quantities (multiples) of Commercial Items Than the Highest Non-Government Purchase Quantity and a Higher Percent of the Total Sales of Commercial Items

Note: Bold figures represent revisions to final report

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For example, for 19 of the 33 individual orders inside the box in Figure 1, DoD purchased [redacted] percent of all commercial items sold by Boeing. For the other 14 orders, DoD purchased quantities at least [redacted] times greater than non-Government commercial customers and at least [redacted] percent of the total sales.

Importance of Recent Sales of Similar Quantities and Substantial Sales. When procuring Boeing commercial catalog items, the quantities of items sold and the forecasted usage for the items are the key factors in determining the catalog price. For example, suppose Boeing was forecasting sales of 10 commercial items per year and the cost to manufacture and stock the 10 items was $400, Boeing's catalog price for the item would be about $50, assuming a 25 percent profit. However, suppose $200 of the manufacturing costs were nonrecurring or setup costs, $50 were for stocking the items, and recurring costs to manufacture the items were only $15 per item. If DLA procured 100 of the items, the $50 catalog price would be fair and reasonable for the 10 items Boeing stocked, but not for the additional 90 items being manufactured. The contractor's costs to manufacture the additional 90 items would be $200 for nonrecurring costs plus $15 times 90 items (assuming no learning curve on recurring costs) for a total cost of $1,550 or $17.22 per item. Add a 25 percent profit and the fair and reasonable price for the additional 90 items would be only $21.53, or less than half of the catalog price. We believe that this example is one of the primary reasons for some of the large price differences between the Boeing commercial catalog prices and previous competitive prices or previous Boeing prices. In addition, the large purchases of commercial items by DLA may not help to lower the Boeing catalog prices because of the infrequency of the purchases and difficulty for Boeing in forecasting requirements. Therefore, by procuring large infrequent quantities of commercial items as opposed to smaller frequent quantities that could be forecasted by Boeing, DLA was actually causing commercial catalog prices to increase.

Conversely, if Boeing was selling large quantities of commercial items to other non-Government customers and DoD wanted to procure a similar or smaller quantity of the item, Boeing's catalog price would most likely be based on the higher forecasted usage and the costs to manufacture the larger quantity. The catalog price for the quantity procured by DoD would most likely be fair and

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reasonable. Unfortunately, as shown in Figure 1, Boeing was not selling similar or sufficient quantities of the commercial catalog items DLA was procuring for the prices to be considered fair and reasonable based on commercial sales.

Commercial Items Evaluated by Boeing. During the audit, we provided Boeing a schedule of the commercial items reviewed and previous competitive prices. We requested that Boeing review 12 of the commercial item orders regarding price reasonableness where the prices appeared out of line. The NSNs for these 12 items were shown as bold on Appendixes E and G (of the draft report) and the price increases for the commercial catalog items from previous competitive prices ranged from 313 to 13,163 percent. Commercial sales data provided by Boeing showed that 4 of the 12 items had no non-Government commercial sales and only one of the items had substantial non-Government commercials sales. For two of the items with no non-Government commercial sales during the review period, DLA procured 246 items of NSN 1650-00-692-7488 and two orders of 100 and 55 items of NSN 5310-00-574-9544. The Boeing Commercial Airplane Group provided the following response to our request to review the price reasonableness of the 12 items.

> Boeing utilized its normal commercial review process to critique the prices of these items and confirmed that all of the items were offered for sale at a fair and reasonable price for the commercial market All of the items were sold at their prevailing catalog prices. No quantity purchase discount was in effect for these items to the Government or to any other customer All of the items have been sold to commercial customers The Government's audit verified that eleven of the items were sold to other customers during the period Boeing's records show that the twelfth item was also sold previously outside of the dates audited. In addition, it should be noted that Boeing did not increase its catalog prices from June 1, 1994 through May 31, 1997

Commercial Item Delivery. One of the advantages of procuring commercial items is that contractors normally stock the items which reduces lead-times for customers. Reduced delivery lead times means that commercial customers can stock fewer items and reduce inventory costs. We reviewed the number of days it took for commercial items to ship on commercial contract 96-D-9501. The contract indicates that orders will be delivered within 10 days of receipt. Boeing did, in fact, ship some items (partial shipments) on [redacted] percent of the orders reviewed within [redacted] days. However, when delivery orders were examined on an item by item basis, we discovered that a majority of the parts ordered actually took significantly longer than [redacted] days for delivery. While customers buying from

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a commercial catalog might normally expect a quicker delivery, with reduced inventory and storage costs, DLA did not achieve those benefits in this instance.

Figure 2 shows that [redacted] percent of the commercial items procured from Boeing took more than [redacted] shipping days. (As of the date of our review March 21, 1997, [redacted] of items had not been shipped and were past the [redacted]-day delivery date included in our analysis. For the items not yet shipped, we used the review date as the actual delivery date, so our calculations are conservative.)

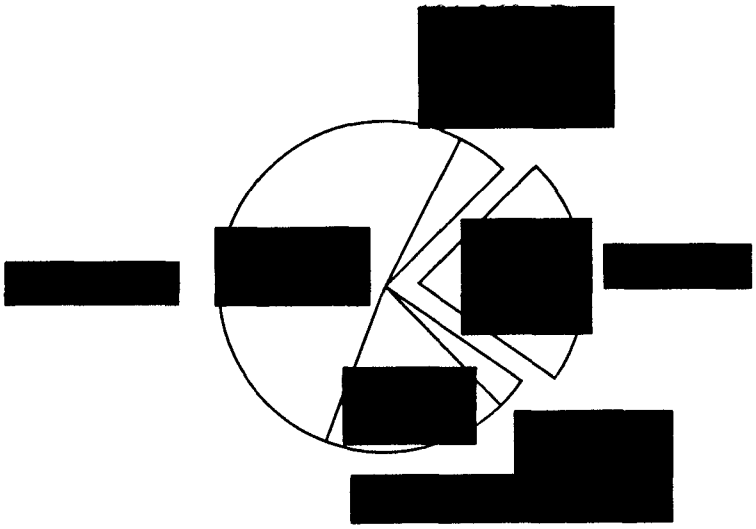

Figure 2. Days for Boeing to Ship Commercial Catalog Items

DLA Corporate Contracting Initiative

DLA Corporate Contracting Initiative. DLA has implemented a corporate contracting initiative without adequate management controls. In doing so, DLA placed greater emphasis on ease of use and on reducing infrastructure than on the prices to be paid by its customers. When it abandoned, or failed to take advantage of, the competitive breakout program previously employed by the Air

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Force under "Rights Guard," DLA also effectively inhibited the participation of small businesses in the acquisition process. In January 1997, DLA briefed the audit team on its corporate contracting program. In the briefing DLA defined corporate contracting and the benefits to its customers.

> DEFINITION.
>
> o Adopts commercial business practices,
>
> o May include a vendor's full product line, or may aggregate requirements of one or more DLA Inventory Control Point,
>
> o Accesses commercial delivery/distribution systems (Direct Vendor Delivery),
>
> o Incorporates electronic data interface (EDI) ordering capability
>
> CUSTOMER BENEFITS·
>
> o Lower product costs,
>
> o Ease of use,
>
> o Opportunity to reduce customer support infrastructure,
>
> o Improved delivery

Corporate Contracting Guidance. DISC provided adequate guidance on the proper use of Boeing corporate contracts to the other DLA supply centers. Of the three Boeing contracts reviewed, only contract 96-D-9501 was technically a corporate contract, although contract 92-G-0024 also was used to procure commercial catalog items from Boeing. The price negotiation memorandum for corporate contract 96-D-9501 described the contract type and estimated an annual value of $1 million, although DLA actually spent over $4 million on the contract in 1996.

> Negotiations were for a firm fixed price contract with economic price adjustment (EPA). The agreement is a long term indefinite quantity contract (IQC), with a contract term of five (5) years It **requires the direct fulfillment of military requisitions from existing off-the-shelf commercial inventory** It is a "direct vendor delivery (DVD)" contract. Orders will cite 10 days. However, delivery will "normally" occur within 4 hours for issue priority designator code (IPD) 01-03 requirements per the Government addendum.
>
> The contract covers items managed by other DLA procuring centers in addition to those items managed by DISC It is therefore a "corporate contract" under the DLA "Corporate Contracting Initiative" The

> items covered are cited in the Boeing Commercial Airplane Group (BCAG) Spare Parts Price & Standard Spare Parts Price catalogs The purpose of this document is to establish that the prices and general terms negotiated for the **noncompetitive, or sole source items** to be ordered by DLA under this contract represent the best value for the military consignee. Items for which competitive sources are cited in the Government description may be ordered under the contract, **however requirements for individual competition and pricing must be met by the ordering activity.** [emphasis added]

After the contract was awarded, DISC provided additional guidance to the other DLA supply centers on how the contract should be used.

> The contract authorizes us to procure spare parts directly from the Boeing Commercial Airplane Group (BCAG) for the first time utilizing the commercial practices of the airlines. This promises dramatic reductions in lead time, the prospect of automating our procurement process through the use of electronic commerce, and enhanced quality evidence to the military consignee. The short lead times enable the use of direct vendor delivery (DVD) procurement techniques
>
> The contract covers the entire catalog(s) referenced in the description of supplies, and authorizes the placement of non-competitive delivery orders for ***sole source*** Boeing part numbers through the Paperless Order Placement System (POPS) DISC has executed a justification for other than full and open competition (J&A) for the **DLA-managed *sole source* items** based on the data provided by your center prior to solicitation **The contract also allows the discretionary placement of orders for competitive items listed in the commercial catalogs, when determined to be the best value.** [emphasis added]

How DLA Used the Boeing Corporate Contract. DSCR and DISC used two different systems to procure commercial items on the Boeing corporate contract. DSCC had not implemented procedures to use the corporate contract. DSCR contracting officers placed orders through a direct interface with the Boeing SONIC system. DSCR contracting officers were instructed to use the Boeing corporate contract to its full extent and that all items listed in the commercial catalog should be purchased under the contract. The prices for the items were to be considered fair and reasonable based on commerciality. DSCR was also working to automate the system so that over 4,000 annual procurement requests would go directly to Boeing and not have to be worked by contracting officers. DISC was already using its POPS automated system to order items from Boeing. POPS issues delivery orders directly to Boeing for items in the commercial

catalog without reviews by contracting officers or item managers. Consequently, DSCR and DISC had implemented informal procedures to use the Boeing corporate contract to procure all items found in its commercial catalog on a sole-source basis. Although these procedures were easy to use and helped reduce the infrastructure needed to procure the items, the procedures also eliminated competition, inhibited the participation of small businesses in the Federal acquisition process, and significantly increased customer costs.

DLA Cost Recovery Rates

DLA Cost Recovery Rates. The DLA supply centers operate under a working capital fund concept and therefore charge their customers a cost recovery rate that is applied to the DLA acquisition cost of the items. The cost recovery rate includes costs to run the DLA supply centers and depots, overhead costs, and other material related costs such as inflation and transportation. The DLA cost recovery rate is then added to the DLA acquisition cost to establish the DLA sales price to DLA customers, generally the Military Departments.

Table 3 shows that the cost recovery rates charged by the three supply centers for the Boeing commercial items reviewed totaled about $2 million, or 28 percent of the DLA acquisition cost.

Table 3. DLA Cost Recovery Rates For Boeing Commercial Items

Contract	Buying Center	DLA Acquisition Cost	DLA Sales Price	Difference	Percent Difference
92-G-0024	DISC	170,195	248,850	78,655	46
	DSCC	750,102	981,886	231,784	31
	DSCR	3,525,602	4,589,100	1,063,498	30
96-D-9501	DISC	710,140	981,435	271,295	38
	DSCR	2,173,216	2,549,519	376,303	17
Total		**$7,329,255**	**$9,350,790**	**$2,021,535**	**28**

Although the DLA cost recovery rates may be appropriate for the manner in which DLA managed the commercial items, the rates are not appropriate for POPs orders of commercial items with direct vendor delivery. In comparison, the General Services Administration charges its customers a one percent industrial funding fee for all orders placed under multiple award schedule contracts. The one percent fee covers the spectrum of administrative costs to manage the program from market research, procurement planning, solicitation issuance, evaluation of proposals, negotiation and award, contract administration, marketing publications, etc.

Added Value. DLA provided little added value procuring, shipping, and stocking Boeing commercial items for the $2 million charged to its customers. Boeing's commercial customers either order parts through the SONIC system or from the Boeing "PART" page, the Web site for Boeing commercial spares customers. Basically, any commercial customer can go on-line with Boeing to order commercial catalog items. OC-ALC has a direct interface with the Boeing SONIC system and orders small quantities of commercial items for urgent (aircraft-on-the-ground) requirements. Consequently, the actual administrative costs to procure Boeing commercial catalog items are minimal. DLA supply centers were able to greatly reduce their administrative procurement costs by procuring the commercial catalog items sole-source from Boeing and not procuring the items competitively.

Boeing also manages and stocks commercial items in the Boeing spare parts distribution center. The distribution center houses all functions necessary to support 24-hour, 365 days a year spare parts distribution needs throughout the world. The Boeing spare parts distribution center issues approximately [redacted] million spare parts annually, of which [redacted] percent are for critical needs (aircraft-on-the-ground). Delivery is normally completed within [redacted] hours for critical needs. The Boeing spare parts distribution center is designed for direct vendor delivery which eliminates the need for customers to stock commercial items. However, DLA was procuring Boeing commercial items and stocking the items in DLA warehouses, which resulted in DLA customers paying duplicate stocking costs to Boeing as part of the catalog price, and to DLA as part of the cost recovery rate.

For example, in February 1996, DSCC procured 246 spoiler actuator sleeve units of NSN 1650-00-692-7488. The parts were scheduled to be shipped to three DLA depots, 107 units to the Defense Depot Susquehanna, PA; 105 units

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to the Defense Depot Columbus, OH; and 34 units the Defense Depot Ogden, UT. At the time the order was placed, Boeing had a total of 9 units in stock which were shipped [redacted] days from the date of the order, the remainder of the order was shipped between [redacted] and [redacted] days. As of August 15, 1997, over a year after the parts were received into inventory, the on-hand balance for the item at the Defense Depot Susquehanna was 181, Columbus was 188, and the data from the Ogden depot was not available because the facility is closing. The DLA cost recovery rate charged to this item was 31 percent or $30,027.

In June 1996, DISC procured 1,677 threaded pin-rivet units of NSN 5320-01-255-4649. The parts were shipped to the Defense Depot Susquehanna, 14 parts were shipped the day after the order was placed and the remaining 1,663 parts were shipped in September 1996, about 3 months later. The balance on-hand at the depot was 1,663 on April 29, 1997 and 732 on August 15, 1997. The DLA cost recovery rate for this item was 55 percent or $3,505 for an order where the parts only cost $6,373.

Included in the DLA cost recovery rate were shipping costs which DLA customers would also pay twice, first the items were shipped from Boeing to the DLA depot, then from the depot to the customer. If DoD wants to procure commercial items from Boeing, true commercial business practices should be adopted such as only procuring actual requirements and using direct vendor delivery. In addition, if DLA cannot provide added value to the acquisition of commercial items commensurate with the cost recovery rate being charged to its customers, then we believe that the customers should be authorized, in appropriate circumstances, to procure the items directly and avoid the DLA surcharge.

Local Purchase Alternatives. As reported in Inspector General, DoD, Report No. 96-090, "Local Procurement of Centrally Managed Items," March 29, 1996, DoD is attempting to increase local purchase authority of centrally managed items.

> Through various initiatives, DoD is attempting to inject business-like practices, market efficiencies, and a customer-oriented philosophy into the DoD business processes Towards that end, the Principal Assistant Deputy Under Secretary of Defense (Logistics) submitted and obtained approval on November 9, 1995, for a change to the Defense Federal Acquisition Regulation Supplement to increase local purchase authority for centrally managed items. DoD anticipates that the approved change will contribute to its initiatives to reduce inventories and the logistics

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> infrastructure by focusing the role of the central supply system on managing items where value is added (both cost economies and operational efficiencies).

Section 208.7003-1 of the Defense Federal Acquisition Regulation Supplement, "Assignments under integrated material management (IMM)," provides guidance on local purchase authority but does not clearly address local procurement of commercial items.

> (a) All items assigned for IMM must be acquired from the IMM manager except --
>
> (1) Items purchased under circumstances of unusual and compelling urgency as defined in FAR 6.302-2. After such a purchase is made, the requiring activity must send one copy of the contract and a statement of the emergency to the IMM manager,
>
> (2) Items for which the IMM manager assigns a supply system code for local purchase or otherwise grants authority to purchase locally; or
>
> (3) When purchase by the requiring activity is in the best interest of the Government in terms of the combination of quality, timeliness, and cost that best meets the requirement This exception does not apply to items--
>
> (i) Critical to the safe operation of a weapon system,
>
> (ii) With special security characteristics; or
>
> (iii) Which are dangerous (e g., explosives, munitions).

The Boeing commercial items reviewed appear to be items considered critical to the safe operation of a weapon system which would be excepted from local purchase authority when in the best interest of the Government. Consequently, the Under Secretary of Defense for Acquisition and Technology needs to determine whether Military Departments have the authority and flexibility under existing procurement regulations to use sources of supply for commercial items other than the integrated material manager, when other sources offer the best value. Allowing the Air Force to procure the commercial items directly from Boeing, as needed, would eliminate the need for DLA to manage and stock the items and also reduce Air Force costs by nearly 28 percent (DLA cost recovery surcharge minus minimal Air Force costs). If flexibility does not exist for the Military Departments to locally procure commercial items, the Under Secretary should propose such changes to procurement regulations. If flexibility does exist, the Under Secretary should inform the Military Departments of the

authority to locally purchase commercial items. To manage its own downsizing more efficiently and improve the overall value of its support to customers, DLA should divest itself of workload that the customers can perform themselves at less cost.

Management Actions During the Audit

The Office of the Under Secretary of Defense for Acquisition and Technology and DLA have been very responsive to the audit results. Accordingly, we limited the recommendations contained in this report. On June 9, 1997, the Deputy Director Material Management, DLA sent a memorandum "Action Items from DoD Inspector General (IG) Brief," to the Commanders at DISC, DSCC, and DSCR. The memorandum discussed tentative audit findings that had been briefed to DLA management and identified audit issues requiring command attention.

- DLA is identifying "Rights Guard" items (parts for which drawings are available under an Air Force contract with Boeing), obtaining manufacturing drawings necessary to solicit the items competitively, and competing future buys.

- DLA is determining whether the corporate contracts with Boeing were used as intended and whether the contracts were providing value to DLA customers. The review will include:

(i) <u>competitive items that historically were competed plus other items that may be bought competitively using Government-owned drawings or "Rights Guard" items;</u> Supply centers were tasked to obtain the necessary drawings, assure such items were coded competitive, block items from automated ordering (e.g., via the paperless order processing system [POPS], and compete items in the future).

(ii) <u>noncompetitive items that historically were, or may be, bought in volume and/or repetitively from Boeing;</u> (Supply centers were tasked to determine which items should bypass automated ordering and seek to negotiate volume price breaks from Boeing or a savings clause to cover future disparities that may arise. If necessary, a determination should be made whether to cancel orders for any unreasonably priced items and whether such cancellation would impose any financial liability of the Government. Supply centers were also

reminded to include a determination in the contract files that prices were not fair and reasonable when requirements cannot be foregone.)

(iii) any specific awards questioned in any subsequent audit report released by the IG.

- DLA is requesting a voluntary refund for any overpriced parts.

- DLA is using the DLA Method of Support Model or other business case analysis model suitable for planning major changes from stock management, before shifting to commercial business practices, such as a corporate contract.

- DLA is training managers and operations personnel in the proper use of corporate contracts, items/requirements that should be excluded, and data requests and evaluations of prices. DLA issued specific guidance in a policy letter, "Determinations of Commerciality and Price Reasonableness," dated June 10, 1997.

- DLA is developing automated system changes to preclude automatic order placement for:

(i) first time buys, to assure items are procured competitively; (This will establish a substantiated cost baseline for subsequent comparisons, e.g., comparing competitive prices to corporate contract price lists.)

(ii) subsequent requisitions for stock-numbered items for which the buy history indicates continued use of a corporate contract would likely result in a substantially higher material cost and/or an unacceptable delivery timeframe.

- DLA is continuing to make a concerted effort to develop long-term stable partnerships with competitive, as well as sole-source suppliers available on DLA's electronic shopping mall to enable their customers to select the most advantageous source to meet their needs.

Meanwhile, the Office of the Under Secretary of Defense for Acquisition and Technology opened a dialogue with Government and industry procurement experts to discuss the wider ramifications of the audit and to consider issues such as appropriate training initiatives to make the Government a better informed and more efficient buyer.

Summary

Congress enacted acquisition reform legislation to improve access to commercial technologies, reduce administrative overhead, and reverse the trend toward over regulation. However, Congress also expressed concern about the implementation of acquisition reform legislation (FASA), particularly the reliance on large businesses to supply goods and services, if implementation were not managed carefully (Senate Report No. 103-259, May 12, 1994).

> The committee has approached the legislation with the view that it must be implemented in a manner that makes the broadest use of the skills and resources of all segments of the business community, including small and small disadvantaged businesses. While the implementation of acquisition reform requires a substantial amount of flexibility, the committee notes that there may be a temptation on the part of both those who write regulations and those who manage programs to use that flexibility in a manner that simply relies on large, established businesses to supply goods and services Such an approach would be shortsighted, because it would deprive the Government of the advantages that accrue from stimulating and developing a large number of sources, as well as the innovation and creativity that resides in America's small businesses. The committee will work closely with the Committee on Small Business, as well as the Committee on Governmental Affairs, in the oversight of the legislation to ensure that it is implemented in a manner that enhances the ability of small disadvantaged businesses to participate in the federal acquisition process

As indicated by the results of this audit, DoD contracting officers and contractors are still learning how to establish equitable business relationships in the FASA/FARA environment. In this particular case, the DLA acquisition team had not been sufficiently effective in obtaining competition, paying fair and reasonable prices for commercial items, and using the corporate contracting initiative. DLA has reacted constructively and aggressively to the problems found by the audit; however, DLA must still demonstrate that it can competitively procure the spare parts in question using the Boeing "Rights Guard" program as effectively as the Air Force and provide added value to its customers to justify its surcharge. Otherwise, acquisition authority for many of these items should devolve to the Services. Due to management's proactive actions during the audit, we have limited the recommendations made in this report.

Management Comments on the Finding and Audit Response

Summaries of management comments on the finding and our audit response are found in Appendix E.

Recommendations, Management Comments, and Audit Response

1. We recommend that the Under Secretary of Defense for Acquisition and Technology:

a. Determine whether the Military Departments have the authority and flexibility under existing procurement regulations to use sources of supply for commercial items other then the integrated material manager, when other sources offer the best value.

b. If flexibility does not exist for the Military Departments to locally procure commercial items, the Under Secretary should propose such changes to procurement regulations. If flexibility does exist, the Under Secretary should inform the Military Departments of the authority to locally purchase commercial items.

Management Comments. The Under Secretary of Defense for Acquisition and Technology concurred, issuing a memorandum to the Military Departments reminding them that substantial authority already existed for DoD activities to purchase centrally managed items from other sources. The memorandum also asked for views from the Military Departments on whether additional flexibility in procurement regulations was required to allow DoD activities to procure some centrally managed items such as aircraft spare parts that are now available through commercial on-line ordering sources, which may be the "best value" source. After the views of the Military Departments are received, the Under Secretary will propose changes to procurement regulations, if determined necessary, to allow DoD activities to locally procure commercial items.

2. We recommend that the Director, Defense Logistics Agency require the Commanders, Defense Supply Center Columbus, Defense Supply Center Richmond, and the Defense Industrial Supply Center to review as part of their management control program self-evaluation, sole-source procurement, commercial item prices, and corporate contracting.

Management Comments. The Defense Logistics Agency concurred, stating that guidance was issued prescribing a standard format to assure that corporate contracts and other new business practice initiatives do not result in substantially higher material costs to customers. The guidance establishes headquarters review and approval mechanisms and specifies the metrics that will be used to assure the projected benefits are achieved during contract performance. The guidance also provides that price comparisons shall be made on the basis of total estimated costs to the customer and that the analysis shall be retained in the contract files to justify resulting support and purchase decisions providing added value to customers.

Part II - Additional Information

Appendix A. Audit Process

Scope

Work Performed. We reviewed DLA procedures and support contract documentation for delivery orders issued by DSCC, DSCR, and DISC to Boeing under contracts F34601-92-G-0024, F42600-94-G-7559, and SPO400/500-96-D-9501. The 1992 and 1996 contracts were used to purchase commercial catalog items (the 1996 contract was also a DLA corporate contract). The 1994 contract was used to purchase noncommercial military items. During CYs 1994 through 1996, DLA issued 162 delivery orders over $25,000 to Boeing on the contracts totaling $12,976,329. We reviewed 136 orders totaling $11,582,384. During the same period, DLA also issued 2,690 delivery orders under $25,000 to Boeing totaling $9,345,693. We reviewed 43 orders totaling $457,545 (all on the 1996 contract). We reviewed comparison buys of the same parts on competitive contracts and other Boeing contracts. We also reviewed Boeing sales information for commercial items for CYs 1994 through 1996.

Limitations to Audit Scope. We reviewed only a small number of orders under $25,000. For CY 1996, we reviewed 126 orders totaling $7,520,819, or only [redacted] of the [redacted] Boeing military replenishment spare part sales of [redacted]

Methodology

Use of Computer-Processed Data. To achieve the audit objectives we relied on computer-processed data from the DoD DD 350 database for contract actions over $25,000. The computer-processed data were determined reliable based upon the significant number of contract actions we reviewed and compared to the DD 350 output. Although we did not perform a formal reliability assessment of the computer-processed data, we determined that the contract delivery order numbers, award dates, and amounts generally agreed with the information in the computer-

Darkened areas (blank spaces) of this report represent data considered "Boeing Proprietary" which has been deleted.

processed data. We did not find errors that would preclude use of the computer-processed data to meet the audit objectives or that would change the conclusions in the report.

Universe and Sample. Tables 5, 6, and 7 summarize the DLA delivery orders reviewed on the Boeing Contracts.

Table 5. DLA Delivery Orders Reviewed on Boeing Contract F34601-92-G-0024

(Over $25,000)	Total Delivery Orders		Delivery Orders Reviewed	
CY	Number	Amount	Number	Amount
1994	12	$ 655,780	11	$ 623,414
1995	19	2,102,400	19	2,102,400
1996	29	1,958,016	27	1,834,763
Total	**60**	**$4,716,196**	**57**	**$4,560,577**
(Under $25,000)	Total Delivery Orders		Delivery Orders Reviewed	
CY	Number	Amount	Number	Amount
1994	336	$1,383,571	0	0
1995	303	1,546,768	0	0
1996	354	1,659,651	0	0
Total	**993**	**$4,589,990**	**0**	**0**

Table 6. DLA Delivery Orders Reviewed on Boeing Contract F42600-94-G-7559

(Over $25,000)	Total Delivery Orders		Delivery Orders Reviewed	
CY	Number	Amount	Number	Amount
1994	4	$291,056	4	$291,056
1995	22	1,691,582	19	1,502,240
1996	43	3,414,876	32	2,758,122
Total	**69**	**$5,397,514**	**55**	**$4,551,418**
(Under $25,000)	Total Delivery Orders		Delivery Orders Reviewed	
CY	Number	Amount	Number	Amount
1994	121	$626,144	0	0
1995	206	1,202,917	0	0
1996	315	1,685,848	0	0
Total	**642**	**$3,514,909**	**0**	**0**

Table 7. DLA Delivery Orders Reviewed on Boeing Contract SPO400/500-96-D-9501

(Over $25,000)	Total Delivery Orders		Delivery Orders Reviewed	
CY	Number	Amount	Number	Amount
1996	**33**	**$2,862,619**	**24**	**$2,470,389**
(Under $25,000)	Total Delivery Orders		Delivery Orders Reviewed	
CY	Number	Amount	Number	Amount
1996	**1,055**	**$1,240,797**	**43**	**$457,545**

Audit Type, Dates, and Standards. We performed this program audit from October 1996 through July 1997 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD Accordingly, we included tests of management controls considered necessary.

Contacts During the Audit. We visited or contacted individuals within the DoD and The Boeing Company. Further details are available on request.

Management Control Program

DoD Directive 5010.38, "Management Control 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 adequacy of the management controls at DSCC, DSCR, and DISC over procurement of spare parts. Specifically, we reviewed management controls regarding procuring items competitively, determining whether commercial item prices were fair and reasonable, and using corporate contracts. We reviewed management's self-evaluation applicable to those controls.

Adequacy of Management Controls. We identified material management control weaknesses for DSCC, DSCR, and DISC as defined by DoD Directive 5010.38. Management controls were not adequate at the three supply centers to ensure that DLA procured spare parts competitively, paid fair and reasonable prices for commercial items, and provided added value on using corporate contracts for commercial items. Actions already taken by DLA and Recommendation 2, if implemented, will improve procurement procedures at the supply centers and could result in potential monetary benefits of $13.3 million. A copy of the report will be provided to the senior official responsible for management controls at the Defense Logistics Agency.

Adequacy of Management's Self-Evaluation. DSCC, DSCR, and DISC had established management control processes, however, the processes did not adequately address obtaining competition, fair and reasonable prices for commercial items, and corporate contracting, and therefore, did not identify or report the material management control weaknesses identified by the audit.

Appendix B. Summary of Prior Coverage

General Accounting Office

General Accounting Office Report No. GAO/NSIAD-95-64 (OSD Case No. 9853), "Defense Inventory: Opportunities to Reduce Warehouse Space," May 24, 1995, indicates that there is substantial inventory that may never be used and a careful review of items most likely not to be used may reduce the number of items stored as well as storage space. About 84,000 of the items GAO reviewed had more than a 20-year supply and much of this inventory will likely never be used. Many items had deteriorated to the point that they were no longer usable. GAO recommended that the Secretary of Defense instruct inventory control points and program managers to focus their inventory reduction efforts on the material that occupies a great deal of storage space with more than a 20-year supply. Management generally agreed that inventories should be reduced and excess storage capacity should be eliminated.

General Accounting Office Report No. GAO/NSIAD-92-23 (OSD Case No. 8891), "Defense Procurement: Improvement Needed in Technical Data Management," February 25, 1992, indicates that the Military Departments and DLA repositories do not have historical logs or other records to measure how quickly they respond to requests for technical data. Nevertheless, repositories have Government internal control standards that require such documentation. The report also indicates that contractors reported having problems with the quality of the data they received. These problems included illegible drawings, obsolete data, and inaccurate or incomplete information and continued to inhibit contractors from competing for Government work or completing the work after a contract was awarded. The contractors were also unsatisfied with the help they received from repositories when trying to resolve problems with the data.

The report recommended that the Secretary of Defense direct the Military Department Secretaries and the Director, DLA to require technical data repository managers ensure compliance with the appropriate internal control documentation necessary to measure how quickly technical data requests are filled and to permit repository managers to determine the status of in-process requests. The report

recommended that the Military Department Secretaries and the Director, DLA reinforce their guidance to the organizations and entities charged with analyzing and accepting technical data for the DoD to ensure that technical data accepted during the acquisition process are as current, accurate, and complete as possible. The report also recommended that guidance be reinforced on the need to provide appropriate points-of-contact to resolve problems with data.

Although no official comments were provided, GAO concluded that DoD plans to automate its repository operations which should improve the system for managing technical data.

General Accounting Office Report No. GAO/NSIAD-91-53 (OSD Case No. 8531), "Defense Procurement: Not Providing Technical Data May Limit DLA Competition," January 30, 1991, indicates that the Defense General Supply Center did not identify the nature and extent of technical data available to the Government on spare parts being solicited. The report also states that the Defense General Supply Center procurement officials did not always receive access to all technical data reported to be available on spare parts when purchasing responsibility for the spare parts were transferred from the Military Departments to the Defense General Supply Center. As a result, opportunities for competition were missed.

The report recommended that the Commerce Business Daily notices for part-numbered solicitations at the Defense General Supply Center more clearly identify the nature and extent of technical data available to the Government and the extent to which potential offerors may have access to such data. The report also recommended that DoD require the Military Departments to ensure the completeness of the technical data transferred to DLA supply centers. DoD concurred with all of the recommendations in the report. DLA negotiated memorandums of agreement with the Army, Navy, and Air Force to govern the transfer of technical data from the Military Departments to DLA.

Inspector General, DoD

Report No. 98-064. Inspector General, DoD, Report No. 98-064, "Commercial and Noncommercial Sole-Source Items Procured on Contract N000383-93-G-M111," February 6, 1998, indicates that DLA paid (for sole-source commercial items) modestly discounted catalog prices that were significantly higher prices than the cost-based prices DLA previously paid for the items. As a result, DoD was not reaping the benefits anticipated when procuring commercial items. For CYs 1994 through 1996, DLA paid about [redacted] (in 1997 constant dollars) or an average of about [redacted] more than fair and reasonable prices for [redacted] of commercial items.

The report recommended that the Under Secretary of Defense for Acquisition and Technology provide additional guidance and training to the DoD acquisition community on purchasing commercial items from sole-source suppliers. The report recommended that the Director, Defense Logistics Agency require contracting officers to obtain uncertified cost or pricing data for commercial item procurements when needed to determine price reasonableness. The report also recommended that contracting officers procure economic order quantities, determine the reliability of data used for price analysis, and obtain certified cost and pricing data when required for noncommercial items. Management generally agreed with the recommendations, but presented a general theme that obtaining uncertified cost or pricing data to determine the reasonableness of contractor prices was an option that should be seldom used. The DoD is appropriately reacting to the issues raised in this report by developing additional training for the acquisition corps to operate more effectively in the post FASA/ FARA environment where commercial pricing and purchasing practices need to be better understood.

Report No. 97-207. Inspector General, DoD, Report No. 97-207, "Contracting Officer Price Analysis," August 26, 1997, indicates that management emphasis on the increased use of price analysis techniques contributed to improved compliance with regulations on price analysis performance. Procurement and contract administration offices had increased the use of price analysis after a 1993 audit (Report No. 94-004).

Darkened areas (blank spaces) of this report represent data considered "Boeing Proprietary" which has been deleted.

The report recommended that Service Acquisition Executives and the Director, DLA, issue policy guidance to their contracting organizations requiring contracting officers to perform and document price analyses as required. Management agreed to the recommendations.

Report No. 96-090. Inspector General, DoD, Report No. 96-090, "Local Procurement of Centrally Managed Items," March 29, 1996, indicates that DoD needs to address a variety of issues to successfully implement its initiatives to increase the use of local purchase authority and to focus the role of the central supply system on managing items where value is added. The audit was unable to determine the extent of local procurement of centrally managed items. However, procurement data provided by 13 organizations visited during the audit showed that only $7.2 million of $744 million (less than 1 percent) of the local procurements were for centrally managed items.

The report recommended that the Deputy Under Secretary of Defense (Logistics) develop procedures to have requisitioning organizations make greater use of local purchase authority for centrally managed items when local procurement is in the best interests of the Government; direct that requisitioning organizations develop procedures to determine the total cost or a local procurement; develop a detailed strategy to address the impact of the local purchase initiatives on centralized material management; and develop procedures addressing local procurement when inventory control points have excess stocks, reporting and recording of demand data for local procurements, and feedback on the progress and economies of local purchase initiatives. Management indicated that the audit results were already being put to use, concurred with the intent of all recommendations, and proposed alternate methods to meet the goals of the recommendations.

Report No. 94-071. Inspector General, DoD, Report No. 94-071, "Transfer of the Management of Consumable Items to the DLA," March 31, 1994, indicates that the Services inventory control points did not transfer essential logistics management data timely, or when transferred, the receiving DLA inventory control points did not always use the data. As a result, the logistics support expected from DLA inventory control points will probably be hampered.

The audit recommended that DoD prescribed criteria be followed in the communication and recording of essential logistics data for transferred items be improved and controls be implemented to ensure use of the data by DLA inventory managers. Management generally concurred with the recommendations and had taken actions to satisfy the intent of the recommendations.

Report No. 94-004. Inspector General, DoD, Report No. 94-004, "Contracting Officer Price Analysis," October 15, 1993, indicates that DoD contracting officers did not always perform and adequately document the use of price analysis on contractor proposal prices, resulting in inadequate assurance that fair and reasonable prices were obtained in negotiated contracts. The report recommended that the Military Departments and DLA issue written management control objectives and techniques to verify performance and documentation of price analyses by contracting officers. The report also recommended that the Deputy Under Secretary of Defense (Acquisition Reform) restructure training requirements to emphasize the performance and documentation of price analysis techniques.

The Air Force and DLA concurred with the recommendations but the Army and Navy believed that existing guidance on price and cost analysis was adequate.

Appendix C. NSN, Boeing Part Number, Item Description, and Contract

NSN	Boeing Part Number	Item Description[1]	Contract[2]
1560-00-019-9053	69-1941	Emergency Shaft	94
1560-00-065-8196	69-10806-1	Aircraft Structural Support Component	92
1560-00-213-4118	3-64728-2	IFR Boom Spring Centering Block	94
1560-00-331-4900	9-65409-3000	Structural Support	92
1560-00-419-6850	65-48140-4	Drain Assembly	94
1560-00-575-6510	5-97836	Telescoping Bracket	94
1560-00-603-7678	9-65808-2000	Emergency Hatch Stop	92
1560-00-606-5721	90-1417-16	Access Cover	94
1560-00-654-0744	5-97285-2	Stowage Latch Eye	94
1560-00-700-8897	65-5889	Crew Frame Assembly	94
1560-00-758-9374	65-11952-8	Nacelle Raceway Assembly	96
1560-00-798-7110	35-8623-501	Air Conditioning Duct Assembly	94
1560-00-803-2107	69-10999-3	Oil Breather Line Assembly	96
1560-00-822-7891	65-11720-14	Vane Segment Assembly	92
1560-00-862-2181	34-1432-516	Aircraft Skin	94
1560-00-873-4231	66-10241	Engine Mount Block	96
1560-00-886-8923	65-23879-23	Radiation Bracket	94
1560-00-910-9133	65-5009-1	Inboard Speed Drum	94
1560-00-910-9136	69-26238-1	Aircraft Structural Support Component	96
1560-00-927-3793	65-69413-5	Fan Reverser Installation Blocker Door	92
1560-00-972-6892	65-29634-14	Fan Reverser Vane Assembly	96
1560-01-006-0469	5-89537-3007	Quadrant Assembly	92
1560-01-009-4078	65-20852-4	Flap Gear Box Assembly	96
1560-01-014-7342	90-7821	Handle Sleeve	96
1560-01-015-6734	65-29994-6	Guide Arm Assembly	92
1560-01-019-0365	65-32244-7	Flap Torque Tube	92

Appendix C. NSN, Boeing Part Number, Item Description, and Contract

NSN	Boeing Part Number	Description[1]	Contract[2]
1560-01-019-1342	65-32220-4	Flap Hinge	96
1560-01-019-8146	65-31995-3	Structural Component Fitting	96
1560-01-020-0444	69-10063-9	Elevator Rudder Weight	92
1560-01-020-4027	69-9028-5	Wing Landing Flap	96
1560-01-021-4789	204-31042-2	Door Seal	94
1560-01-021-5501	65-32240-3	Flap Torque Tube	92
1560-01-021-5527	66-10360	Door Track Assembly	96
1560-01-026-3684	63-10265-1	Spring Stop	96
1560-01-027-6758	65-3283-17	Door Seal Assembly	92
1560-01-027-6811	69-4184-1	Wing Spar Pin	96
1560-01-027-6815	9-55629-3001	Wing Spar Pin	96
1560-01-028-7991	69-45903-1	Structural Support	96
1560-01-029-4374	204-70230-1	Structural Component Fitting	94
1560-01-035-2347	65-19198-3	Link Assembly	92
1560-01-039-3293	65-6414-19AW	Aircraft Structural Panel	92
1560-01-039-3299	69-4188-7	Aircraft Trim Assembly	96
1560-01-039-3305	65-18462-7	Aircraft Structural Fitting Component	96
1560-01-039-9150	65-18462-8	Fitting Assembly	96
1560-01-039-9179	64-1177-20	Aircraft Structural Panel	96
1560-01-039-9192	65-19169-3	Flap Door Acuator Fillet Arm & Plate Assembly	92
1560-01-040-1393	65-8435-3004	Structural Panel	96
1560-01-045-6800	5-88152-3033	VHF Navigation Antenna Assembly	92
1560-01-047-5792	69-11276-8	Rudder Rod Assembly	96
1560-01-052-8031	5-71761-501	Windshield	94
1560-01-052-8032	5-71761-502	Windshield	94
1560-01-063-9959	65-10606-31	Ring-Duct Support	92
1560-01-065-1352	204-11368-13	Radome Replacement Kit	94
1560-01-084-1436	5-83072-6	Aircraft Skin	94

Appendix C. NSN, Boeing Part Number, Item Description, and Contract

NSN	Boeing Part Number	Description[1]	Contract[2]
1560-01-095-9536	5-87169-3004	Housing Assembly	92
1560-01-106-3360	65-1378-19	Strip Assembly	92
1560-01-143-8537	65-27438-8	Throtl Cam Assembly	92
1560-01-145-0223	35-10701-36	Aircraft Skin	94
1560-01-163-1726	69-71211-5	Aircraft Structural Support Component	92
1560-01-165-5090	65-68624-2	Aircraft Structural Support	92
1560-01-176-5269	65-13169U19	Structural Support	92
1560-01-178-0995	65-16032-41	Seal Depressor Assembly	96
1560-01-178-1041	65-11882-10	Structural Support	92
1560-01-183-5138	65C18554-710	Upper Lip	94
1560-01-183-5139	65C18554-711	Upper Lip	94
1560-01-183-7265	458-50076-501	Air Conditioning Duct Assembly	94
1560-01-219-3242	65-95600-1100	Aircraft Skin	92
1560-01-219-4993	65-41416-16	Attach Ring	94
1560-01-273-4323	64-1072-3131	Structural Support	92
1560-01-273-4324	64-1072-3132	Structural Support	92
1560-01-273-9585	64-1068-3141	Structural Support	92
1560-01-273-9586	64-1068-3142	Structural Support	92
1560-01-290-5140	65C18614-626	Start Duct Assembly	94
1560-01-290-5141	65C18614-627	Start Duct Assembly	94
1560-01-290-5141	65C18614-627	Start Duct Assembly	92
1560-01-322-6850	65-6180-17	Floor Panel Trim	96
1560-01-329-7504	50-3750-2	Aircraft Panel	94
1560-01-341-7782	65-23417-7	Airfoil Rib	96
1560-01-343-1411	5-89875-3057	Structural Aircraft Panel	94
1560-01-343-1411	5-89875-3057	Structural Support Panel	92
1560-01-352-6531	50-9376	Structural Fitting Component	92
1560-01-352-6532	50-9375	Structural Fitting Component	92

Appendix C. NSN, Boeing Part Number, Item Description, and Contract

NSN	Boeing Part Number	Description[1]	Contract[2]
1560-01-372-1096	5-71770-4	Aircraft Window Frame	94
1560-01-372-1097	5-71770-3	Aircraft Window Frame	94
1560-01-372-8723	65-2937-12	Aircraft Structural Plate	96
1560-01-384-2359	9-64373-5	Structural Support	92
1560-01-385-6897	65-20993-3	Structural Fitting	96
1560-01-385-6897	65-20993-3	Structural Fitting	92
1560-01-385-7017	65-20993-4	Structural Fitting Component	96
1560-01-385-7017	65-20993-4	Structural Fitting Component	92
1560-01-386-1622	65-22227-2	Chord-Inboard Edge	96
1560-01-407-8308	50-9452	Access Door	94
1560-01-411-1322	65-22018-3	Roller Assembly Flap	96
1560-01-413-8389	65-18441-11	Structural Panel	92
1560-01-416-1742	65-20956-9	Structural Support	96
1560-01-420-2461	69-51536-1	Structural Support	92
1560-01-422-7105	9-63879-3001	Aircraft Trailing Edge	96
1560-01-434-1960	65-32220-4	Structural Fitting Component	96
1620-00-630-4244	69-4543-1	Cylinder Assembly (Bungee Assy)	92
1650-00-339-7279	60-1449	ABS Shock Ring Assembly	94
1650-00-534-5913	9-49698-1	Linear Actuating Cylinder Head	94
1650-00-692-7488	60-4962	Spoiler Actuator Sleeve	92
1650-01-012-6485	65-5646	Dampner Piston	92
1650-01-015-5037	50-7977	Actuating Cylinder	92
1650-01-187-4267	69-14928-7	Linear Actuating Cylinder Head	92
1680-00-343-4111	60-2299-1	Boom Sleeve Assembly	94
1680-00-716-3037	63-11029-2	Stowage Parts Kit	94
1680-01-027-3513	69-36754-12	Curtain Slide Assembly	96
1680-01-032-8912	69-28323-1	Harness Assembly	,96

Appendix C. NSN, Boeing Part Number, Item Description, and Contract

NSN	Boeing Part Number	Description[1]	Contract[2]
1680-01-038-3240	66-8796	Locking Hex Head Pin	96
1680-01-146-4987	204-40851-2	Survival Equipment Strap Assembly	94
1680-01-225-0705	204-40756-16	Panel Assembly	94
2915-01-338-0380	510-14060-1	Fuel Pressurizing & Drain Valve	94
3020-00-341-9436	9-66385	Bevel Gear	92
3020-00-534-3151	5-97226	Groove Pulley	94
3020-01-015-0909	65-19460-1	Bevel Gear	94
3040-00-233-1116	50-6237-3042	Counterbalance Weight	92
3040-00-525-3415	9-61709-4	Shouldered Shaft	92
3040-00-586-8631	90-2423-11	Rigid Connecting Link	92
3040-00-863-7314	65-10523	Remote Control Lever	92
3040-00-863-7315	65-10523-1	Remote Control Lever	92
3040-01-024-5190	65-19824-1	Bevel Gearshaft	94
3040-01-136-7222	66-4547-10	Rod Assembly	92
3040-01-136-7223	66-4547-11	Rod Assembly	92
3040-01-352-4172	DAA3116A422-009	Rigid Connecting Link	94
3110-00-925-8600	BACB10B315	Needle Bearing Cam Follower	92
3110-00-925-8601	BACB10B314	Needle Bearing Cam Follower	96
3110-01-016-2964	69-67049-1	Bearing Retainer	96
3120-00-662-7508	3-99453-1	Sleeve Bearing	92
3120-00-757-3832	66-17691-1	Sleeve Bushing	96
4030-01-025-0253	204-83087-1	Segment Coupling	94
4710-00-622-7416	5-97251	Fuel Tube Assembly	94
4710-01-323-1366	65-23827-1	Tube Assembly	94
4810-01-367-4932	5-63416-3	Valve Body	94
4820-01-044-2378	6522777-5	Butterfly Valve	94
5305-00-297-2846	6-73377	Setscrew	96
5305-00-973-2281	BACB30GD4-8S	Special Screw	96

Appendix C. NSN, Boeing Part Number, Item Description, and Contract

NSN	Boeing Part Number	Description[1]	Contract[2]
5306-00-652-7292	36-3064	Shoulder Bolt	94
5306-01-014-7744	66-3932-1	Internally Relieved Bolt	96
5306-01-371-5136	BACB30US14K40	Shear Bolt	96
5306-01-420-0875	66-4002-501	Machine Bolt	94
5306-01-436-4028	BACB30US16K40	Machine Bolt	96
5310-00-501-0432	66-10985	Plain Round Nut	96
5310-00-565-5342	66-1724	Landing Gear Nut	96
5310-00-574-9544	6-68024-1	Sleeve Nut	96
5310-00-574-9545	6-68024	Sleeve Nut	96
5310-00-637-3884	3-98746	Flat Washer	96
5310-00-895-6233	BACN10HC5	Self-Locking Barrel Nut	96
5310-00-895-6233	BACN10HC5	Self-locking Barrel Nut	92
5310-01-021-0619	66-20192-1	Flat Washer	96
5310-01-025-9992	BACN10HR18CD	Self-Locking Extended Washer Nut	96
5310-01-339-0788	63-12059	Flat Washer	96
5310-01-344-5944	63-8495-3002	Flat Washer	96
5315-01-019-1184	60-6548-1	Actuator Beam Pin	96
5320-01-019-6967	69-47090-8	Pin	96
5320-01-178-6248	BACB30FP10-7	Threaded Pin-Rivet	96
5320-01-255-4649	BACB30LW6-8	Threaded Pin-Rivet	96
5325-01-051-3094	BACS21AG4E13	Screw Thread Insert	96
5330-00-576-9075	29-5506-4	Gasket	94
5330-00-877-1820	66-10756	Nonmetallic Special Shaped Section Seal	96
5340-00-477-1078	3-14308	Handwheel	96
5340-00-625-6619	5-89393-4	Access Door Hinge	94
5340-01-044-7267	65-79137-18	Handle Assembly	96
5340-01-434-6568	69-36011-11	Butt Hinge Leaf	96

Appendix C. NSN, Boeing Part Number, Item Description, and Contract

NSN	Boeing Part Number	Description[1]	Contract[2]
5998-01-374-3105	4000-08155-03	Circuit Card Assembly	94
6150-00-458-3519	25-60433-2	Electrical Special Purpose Cable Assembly	94

[1]Item descriptions quoted from contract delivery order

[2]92 represents Contract No F34601-92-G-0024, 94 represents Contract No F42600-94-G-7559, and 96 represents SPO400-96-D-3501

Appendix D. Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts

NSN	Order	Total Price	Buying Activities Previous	Buying Activities Current	Acquisition Method Codes Previous	Acquisition Method Codes Current	✓ Correct X Incorrect	Technical Data Rights "Rights Guard"	Technical Data Rights DoD
1560-00-019-9053	TYJ1	$ 27,706	SA-ALC	DSCR	NA	NA		✓	
1560-00-065-8196	TYHF	44,980	OC-ALC	DSCR	2G	3H	X	✓	
1560-00-213-4118	TYT6	38,429	DSCR	DSCR	1G	1G	✓		✓
1560-00-331-4900	TYU5	41,340	SAC-ALC	DSCR	2G	3H	X	✓	
1560-00-419-6850	TYH3	36,756	SAC-ALC	DSCR	1G	1G	✓	✓	
1560-00-575-6510	TYL7	47,754	OC-ALC	DSCR	2G	3H	X	✓	
1560-00-603-7678	TYKC	45,270	SAC-ALC	DSCR	2G	3A	X	✓	
1560-00-606-5721	TYB3	31,600	OC-ALC	DSCR	2G	3A	X	✓	
1560-00-654-0744	TYL4	35,750	DSCR	DSCR	2G	1G	✓	✓	
1560-00-700-8897	TYR8	335,625	SA-ALC	DSCR	1G	3H	X	✓	
1560-00-700-8897	TYS8	430,272	SAC-ALC	DSCR	1G	3H	X	✓	
1560-00-758-9374	0048	37,260	OC-ALC	DSCR	2G	1H	X	✓	
1560-00-798-7110	TYQ8	52,416	OC-ALC	DSCR	1G	3H	X		✓
1560-00-803-2107	0044	43,690	OC-ALC	DSCR	1G	1G	✓	✓	
1560-00-822-7891	TYPK	29,134	SAC-ALC	DSCR	2C	3C		✓	
1560-00-862-2181	TYL5	383,672	OC-ALC	DSCR	2G	3H	X		✓
1560-00-873-4231	0052	27,962	OC-ALC	DSCR	1G	1G	✓	✓	
1560-00-886-8923	TYN3	25,460	SA-ALC	DSCR	2G	1G	✓	✓	
1560-00-910-9133	TYN1	40,480	SA-ALC	DSCR	1G	1G	✓	✓	
1560-00-910-9136	0056	36,093	DSCR	DSCR	2G	1G	✓	✓	
1560-00-927-3793	TYE8	100,350	DSCR	DSCR	1G	1G	✓	✓	
1560-00-927-3793	TYF2	38,133	DSCR	DSCR	1G	1G	✓	✓	
1560-00-972-6892	0005	305,991	DSCR	DSCR	5H	3Z		✓	

Appendix D. Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts

			Buying Activities		Acquisition Method Codes			Technical Data Rights	
NSN	Order	Total Price	Previous	Current	Previous	Current	✓ Correct X Incorrect	"Rights Guard"	DoD
1560-01-006-0469	TYP1	46,942	SAC-ALC	DSCR	3P	1G	✓	✓	
1560-01-006-0469	TYZ8	120,708	SAC-ALC	DSCR	3P	1G	✓	✓	
1560-01-009-4078	0007	199,420	OC-ALC	DSCR	2G	1G	✓	✓	
1560-01-009-4078	TYDF	39,884	OC-ALC	DSCR	2G	1G	✓	✓	
1560-01-014-7342	0014	3,724	OC-ALC	DSCR	NA	3Z		✓	
1560-01-015-6734	TYAQ	27,588	OC-ALC	DSCR	5P	3P		✓	
1560-01-019-0365	TYQK	233,610	SAC-ALC	DSCR	4P	3P		✓	
1560-01-019-1342	0067	99,940	SAC-ALC	DSCR	2G	3Z	X	✓	
1560-01-019-8146	0026	1,530	DSCR	DSCR	NA	3Z		✓	
1560-01-020-0444	TYAL	36,642	SAC-ALC	DSCR	NA	3H		✓	
1560-01-020-4027	0032	5,985	OC-ALC	DSCR	2A	3P		✓	
1560-01-021-4789	TY23	49,980	SAC-ALC	DSCR	NA	3H		✓	
1560-01-021-5501	TYQN	89,968	SAC-ALC	DSCR	1G	3H	X	✓	
1560-01-021-5527	0027	792	DSCR	DSCR	NA	3P		✓	
1560-01-026-3684	0011	18,091	SAC-ALC	DSCR	NA	3P		✓	
1560-01-027-6758	TYHK	23,544	SAC-ALC	DSCR	2G	1G	✓	✓	
1560-01-027-6811	0033	38,836	SAC-ALC	DSCR	2G	1G	✓	✓	
1560-01-027-6815	0003	168,300	OC-ALC	DSCR	2G	1C	X	✓	
1560-01-028-7991	0028	13,482	OC-ALC	DSCR	NA	3H		✓	
1560-01-029-4374	TYN5	29,880	SA-ALC	DSCR	2G	3H	X	✓	
1560-01-035-2347	TYPB	36,777	SAC-ALC	DSCR	1G	3Z	X	✓	
1560-01-039-3293	TYDC	39,000	DSCR	DSCR	1G	1G	✓	✓	
1560-01-039-3299	0016	1,137	OC-ALC	DSCR	NA	3Z		✓	
1560-01-039-3305	0004	153,630	OC-ALC	DSCR	NA	3Z		✓	
1560-01-039-9150	0006	93,885	SAC-ALC	DSCR	2G	1G	✓	✓	

Appendix D. Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts

			Buying Activities		Acquisition Method Codes			Technical Data Rights	
NSN	Order	Total Price	Previous	Current	Previous	Current	✓ Correct X Incorrect	"Rights Guard"	DoD
1560-01-039-9179	0018	18,650	SAC-ALC	DSCR	3P	3Z		✓	
1560-01-039-9192	TYBW	102,480	OC-ALC	DSCR	5A	3H		✓	
1560-01-040-1393	0061	44,804	SAC-ALC	DSCR	2G	3Z	X	✓	
1560-01-045-6800	TYHV	32,480	SAC-ALC	DSCR	5P	3P		✓	
1560-01-047-5792	0013	24,684	SAC-ALC	DSCR	4P	3Z		✓	
1560-01-052-8031	TY59	67,650	DSCR	DSCR	1G	1G	✓	✓	
1560-01-052-8032	TY50	110,460	SAC-ALC	DSCR	1G	3H	X	✓	
1560-01-063-9959	TYMK	23,120	OC-ALC	DSCR	2G	3H	X	✓	
1560-01-065-1352	TYG9	204,564	OC-ALC	DSCR	NA	3H		✓	
1560-01-084-1436	TYF2	74,673	OC-ALC	DSCR	2G	1G	✓	✓	
1560-01-095-9536	TYLE	27,972	SAC-ALC	DSCR	NA	3H		✓	
1560-01-095-9536	TYG8	45,150	SAC-ALC	DSCR	NA	3H		✓	
1560-01-106-3360	TYPZ	31,812	OC-ALC	DSCR	2G	3Z	X	✓	
1560-01-143-8537	TYGN	28,386	OC-ALC	DSCR	2G	3H	X	✓	
1560-01-145-0223	TY58	94,550	OC-ALC	DSCR	1G	3H	X	✓	
1560-01-163-1726	TYPN	38,912	DSCR	DSCR	5P	3P		✓	
1560-01-165-5090	TYNH	31,160	DSCR	DSCR	2G	1G	✓	✓	
1560-01-176-5269	TYQE	61,710	DSCR	DSCR	NA	3H		✓	
1560-01-178-0995	0025	5,460	DSCR	DSCR	NA	3P		✓	
1560-01-178-1041	TYZ4	38,796	DSCR	DSCR	NA	3H		✓	
1560-01-183-5138	TYF6	93,440	OC-ALC	DSCR	NA	3P		✓	
1560-01-183-5139	TYF5	181,040	OC-ALC	DSCR	NA	3P		✓	
1560-01-183-7265	TYP4	13,888	SAC-ALC	DSCR	5P	3P		✓	
1560-01-219-3242	TYJC	36,806	OC-ALC	DSCR	NA	3H		✓	
1560-01-219-4993	TYH7	31,591	OC-ALC	DSCR	NA	3H		✓	
1560-01-273-4323	TYFC	483,350	SAC-ALC	DSCR	NA	3H		✓	

Appendix D. Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts

			Buying Activities		Acquisition Method Codes			Technical Data Rights	
NSN	Order	Total Price	Previous	Current	Previous	Current	✓ Correct X Incorrect	"Rights Guard"	DoD
1560-01-273-4324	TYFD	483,350	SAC-ALC	DSCR	NA	3H		✓	
1560-01-273-9585	TYJE	202,826	SAC-ALC	DSCR	NA	3H		✓	
1560-01-273-9586	TYJF	202,826	SAC-ALC	DSCR	NA	3H		✓	
1560-01-290-5140	TYQ7	98,532	DSCR	DSCR	NA	3H		✓	
1560-01-290-5141	TYP3	29,510	DSCR	DSCR	NA	3H		✓	
1560-01-290-5141	TYAM	28,248	DSCR	DSCR	NA	3H		✓	
1560-01-322-6850	0020	140	DSCR	DSCR	NA	3Z		✓	
1560-01-329-7504	TYW1	53,214	DSCR	DSCR	NA	3H		✓	
1560-01-341-7782	0009	201,575	DSCR	DSCR	NA	3Z		✓	
1560-01-343-1411	TYO6	65,100	DSCR	DSCR	NA	3H		✓	
1560-01-343-1411	TYN6	44,145	DSCR	DSCR	NA	3H		✓	
1560-01-352-6531	TYFE	200,538	DESC	DSCR	NA	3H		✓	
1560-01-352-6532	TYFF	154,260	DSCR	DSCR	NA	3H		✓	
1560-01-372-1096	TYF9	30,696	DSCR	DSCR	NA	3H		✓	
1560-01-372-1097	TYF8	30,696	DSCR	DSCR	NA	3H		✓	
1560-01-372-8723	0024	4,402	DSCR	DSCR	NA	3Z		✓	
1560-01-384-2359	TYMM	102,200	DSCR	DSCR	NA	3H		✓	
1560-01-385-6897	0021	120,176	DSCR	DSCR	NA	3Z		✓	
1560-01-385-6897	TYEB	60,088	DSCR	DSCR	NA	3Z		✓	
1560-01-385-7017	0060	120,176	DSCR	DSCR	NA	3H		✓	
1560-01-385-7017	TYCC	90,132	DSCR	DSCR	NA	3H		✓	
1560-01-386-1622	0012	1,226	DSCR	DSCR	NA	3Z		✓	
1560-01-407-8308	TYU4	42,328	DSCR	DSCR	NA	3H		✓	
1560-01-411-1322	0036	4,896	DSCR	DSCR	NA	3Z		✓	
1560-01-413-8389	TYNV	66,460	DSCR	DSCR	NA	3Z		✓	
1560-01-416-1742	0019	2,443	DSCR	DSCR	NA	3Z		✓	

Appendix D. Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts

			Buying Activities		Acquisition Method Codes			Technical Data Rights	
NSN	Order	Total Price	Previous	Current	Previous	Current	✓ Correct X Incorrect	"Rights Guard"	DoD
1560-01-420-2461	TYHG	29,203	DSCR	DSCR	NA	3H		✓	
1560-01-422-7105	0008	289,345	DSCR	DSCR	NA	3Z		✓	
1560-01-434-1960	0068	55,230	DSCR	DSCR	NA	3H		✓	
1620-00-630-4244	UB2J	46,950	OC-ALC	DSCC	1G	3H	X	✓	
1650-00-339-7279	UB4Z	37,152	OC-ALC	DSCC	1G	3H	X	✓	
1650-00-534-5913	UB2D	29,998	SA-ALC	DSCC	1G	3H	X	✓	
1650-00-692-7488	UB6X	97,170	OC-ALC	DSCC	1G	3H	X	✓	
1650-01-012-6485	UB2G	33,670	OC-ALC	DSCC	1G	3H	X	✓	
1650-01-015-5037	UB3V	50,490	OC-ALC	DSCC	2G	2H	X	✓	
1650-01-187-4267	UBC1	26,961	OC-ALC	DSCC	1G	3H	X	✓	
1680-00-343-4111	TYN7	121,770	SA-ALC	DSCR	2C	3H		✓	
1680-00-716-3037	TY18	72,158	SA-ALC	DSCR	1G	3A	X	✓	
1680-00-716-3037	TYW4	90,300	SA-ALC	DSCR	1G	3P	X	✓	
1680-01-027-3513	0015	1,740	SAC-ALC	DSCR	NA	3Z		✓	
1680-01-032-8912	0058	41,124	SAC-ALC	DSCR	NA	3H		✓	
1680-01-038-3240	0017	5,382	SAC-ALC	DSCR	3L	3Z		✓	
1680-01-146-4987	TYU5	27,209	OC-ALC	DSCR	NA	3H		✓	
1680-01-225-0705	TYK2	53,423	DSCR	DSCR	NA	3H		✓	
2915-01-338-0380	TZ34	29,600	DISC	DISC	NA	3H			✓
3020-00-341-9436	UB77	65,535	DSCC	DSCC	NA	3D		✓	
3020-00-534-3151	UB88	115,024	DSCC	DSCC	2G	2G	✓	✓	
3020-01-015-0909	UBIM	42,699	DSCC	DSCC	NA	3C		✓	
3040-00-233-1116	UB6J	62,244	OC-ALC	DSCC	2G	3H	X	✓	
3040-00-525-3415	UB5Y	81,066	OC-ALC	DSCC	1G	3H	X	✓	
3040-00-586-8631	UB9A	60,316	OC-ALC	DSCC	1G	3H	X	✓	

Appendix D. Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts

			Buying Activities		Acquisition Method Codes			Technical Data Rights	
NSN	Order	Total Price	Previous	Current	Previous	Current	✓ Correct X Incorrect	"Rights Guard"	DoD
3040-00-863-7314	UB5J	29,568	OC-ALC	DSCC	1G	3H	X	✓	
3040-00-863-7315	UB3N	27,216	OC-ALC	DSCC	1G	2H	X	✓	
3040-01-024-5190	UBIN	39,700	DSCC	DSCC	NA	3H		✓	
3040-01-136-7222	UBC8	91,476	DSCC	DSCC	NA	3C		✓	
3040-01-136-7223	UBC7	40,960	DSCC	DSCC	NA	3C		✓	
3040-01-352-4172	UB4T	34,064	DSCC	DSCC	NA	NA			✓
3110-00-925-8600	TZ9R	87,000	DISC	DISC	NA	1B			✓
3110-00-925-8601	36	23,180	DISC	DISC	NA	1B			✓
3110-01-016-2964	675	10,620	DISC	DISC	NA	3P		✓	
3120-00-662-7508	TZ4Z	48,645	DISC	DISC	NA	3H		✓	
3120-00-757-3832	282	11,092	DISC	DISC	NA	1G	✓	✓	
4030-01-025-0253	TZ2U	186,250	SA-ALC	DISC	3C	3C		✓	
4030-01-025-0253	TZ59	43,620	SA-ALC	DISC	3C	3C		✓	
4710-00-622-7416	UB99	286,110	DSCC	DSCC	1G	1G	✓	✓	
4710-01-323-1366	UB4G	33,208	DSCC	DSCC	NA	1C		✓	
4810-01-367-4932	UB45	103,818	DSCC	DSCC	NA	3D		✓	
4810-01-367-4932	UB66	118,150	DSCC	DSCC	NA	3C		✓	
4820-01-044-2378	UB2P	29,734	DSCC	DSCC	NA	3H		✓	
5305-00-297-2846	658	11,706	DISC	DISC	NA	3H		✓	
5305-00-973-2281	232	37,967	DISC	DISC	NA	1C			✓
5306-00-652-7292	TZ3H	44,528	OC-ALC	DISC	NA	2G	✓		✓
5306-01-014-7744	254	18,500	DISC	DISC	NA	1G	✓	✓	
5306-01-371-5136	253	14,396	DISC	DISC	NA	1B			✓
5306-01-420-0875	TZ1V	27,075	DISC	DISC	NA	3H		✓	
5306-01-436-4028	127	13,928	DISC	DISC	NA	1B			✓

Appendix D. Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts

			Buying Activities		Acquisition Method Codes			Technical Data Rights	
NSN	Order	Total Price	Previous	Current	Previous	Current	✓ Correct X Incorrect	"Rights Guard"	DoD
5310-00-501-0432	555	8,370	DISC	DISC	NA	3H		✓	
5310-00-565-5342	8	112,665	DSCR	DISC	NA	2G	✓	✓	
5310-00-574-9544	47	41,500	OC-ALC	DISC	1G	3H	X	✓	
5310-00-574-9544	251	22,825	OC-ALC	DISC	1G	3H	X	✓	
5310-00-574-9545	233	136,120	OC-ALC	DISC	5L	3H		✓	
5310-00-637-3884	624	13,310	DISC	DISC	NA	3H		✓	
5310-00-895-6233	92	24,000	ATCOM	DISC	NA	1B			✓
5310-00-895-6233	TZ8T	34,000	ATCOM	DISC	NA	1B			✓
5310-01-021-0619	7	8,565	DSCR	DISC	3H	3H		✓	
5310-01-025-9992	125	9,649	DISC	DISC	NA	1C			✓
5310-01-339-0788	258	23,280	DISC	DISC	NA	3H		✓	
5310-01-339-0788	1153	10,864	DISC	DISC	NA	3H		✓	
5310-01-339-0788	46	19,400	DISC	DISC	NA	3H		✓	
5310-01-339-0788	1152	16,296	DISC	DISC	NA	3H		✓	
5310-01-344-5944	991	10,380	DISC	DISC	NA	3H		✓	
5315-01-019-1184	11	8,988	SA-ALC	DISC	3H	3H		✓	
5320-01-019-6967	256	31,500	SA-ALC	DISC	NA	3H		✓	
5320-01-178-6248	238	7,820	DISC	DISC	NA	1C			✓
5320-01-255-4649	247	12,160	DISC	DISC	NA	1C			✓
5325-01-051-3094	272	9,773	DISC	DISC	NA	3H			✓
5330-00-576-9075	TZ70	29,584	DISC	DISC	NA	3H			✓
5330-00-877-1820	271	11,544	SA-ALC	DISC	1G	2G	✓	✓	
5340-00-477-1078	292	5,061	OC-ALC	DISC	2G	3H	X	✓	
5340-00-625-6619	TZ4S	26,240	OC-ALC	DISC	NA	3H		✓	
5340-01-044-7267	295	9,911	DSCR	DISC	NA	3H		✓	
5340-01-044-7267	44	8,162	DSCR	DISC	NA	3H		✓	

Appendix D. Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts

			Buying Activities		Acquisition Method Codes`			Technical Data Rights	
NSN	Order	Total Price	Previous	Current	Previous	Current	✓ Correct X Incorrect	"Rights Guard"	DoD
5340-01-434-6568	288	33,200	DISC	DISC	NA	3H		✓	
5998-01-374-3105	UD46	26,268	DSCC	DSCC	NA	3C			✓
6150-00-458-3519	TYP8	110,984	DSCR	DSCR	NA	3B			✓
Total							28 Correct 38 Incorrect	159	20

ACQUISITION METHOD CODES DEFINITIONS

NA = Not Applicable

Acquisition Method Codes

1 = Suitable for competitive acquisition for the second or subsequent time

2 = Suitable for competition for the first time

3 = Acquire, for the second or subsequent time, directly from the actual manufacturer

Acquisition Method Suffix Code Defined

B = Source control drawing

C = Requires engineering source approval by the design control activity

D = Data not available

G = Fully competitive (complete data available)

H = Data insufficient

L = Part falls below screening threshold. However, part has been screened for additional sources.

P = Data proprietary

R = Data rights not owned by government, uneconomical to purchase data

Z = Commercial/off the shelf

Appendix E. Management Comments on the Finding and Audit Response

Management Comments on Causes of Higher Prices. DLA commented that the two specific causes for higher prices were the unavailability within DLA of the manufacturing drawings and associated technical data necessary to award the buys on a competitive basis and the unwillingness of Boeing to depart from its long-standing policy of selling commercial catalog spare parts only at list price, regardless of the customer, quantity, or other factors.

Audit Response. We agree that these are two of the proximate causes of higher prices, but believe that the root causes for the higher prices are those identified in the report.

Management Comments on Appropriate Acquisition Method Codes. DLA commented that its ICPs (Inventory Control Points) recoded items to a noncompetitive status when the customer's needs required the item delivery before a fully competitive technical data package could be updated and obtained. This temporary recoding is proper even though the ICP may eventually obtain a full and open competition data package (either Government-owned data or limited rights data under the Boeing "Rights Guard" licensing program.) When the data package is received and reviewed for completeness, the equipment specialist updates the coding to competitive status. Therefore, the term "incorrect" coding should not be used in the report.

Audit Response. Unfortunately, DLA was not taking any action to update and obtain competitive data packages for the spare parts that were reviewed, so the noncompetitive status coding assigned to spare parts by DLA was neither temporary nor correct.

Management Comments on Performing Price Analysis. DLA conceded that price analysis of some previous competitive buys could have been more thorough. However, due to the age of some of the comparison buys, availability of buy folders, and differences in circumstances when parts were procured by different military activities, use of comparative price analysis to these prior buys was generally not an option available to DLA contracting personnel for use in assessing price reasonableness.

Audit Response. We strongly disagree. Failure of DLA contracting officers to question the commercial catalog prices because of the age of some of the comparison buys, availability of buy folders, and differences in circumstances when parts were procured by different military organizations is understandable, but unfortunate. Even cursory review would have shown that the parts in question were not sole source and that other suppliers had provided the parts to DoD in the past, at substantially lower prices. Further, the significant price increases from both the current and older comparison buys from other manufacturers clearly showed that the Boeing commercial catalog prices were high. This realization should have led, in turn, to a realization that the benefits to be gained from using the corporate contract for these purchases either were not needed or were not worth the additional cost, so that alternatives would have been sought. They were not.

Management Comments on Accepting Commercial Catalog Prices as Fair and Reasonable. DLA commented that 2 separate orders, each for 25 structural supports (similar parts) valued at $483,350, were determined reasonable based on current catalog pricing. The requirement for both buys in question was urgent and compelling. The comparison buys used in the audit were from December 1983 for 5 and 10 items respectively. Consequently, the buyer had no way of knowing and making appropriate adjustments for different circumstances that very well may have existed previously and no way to confirm the reasonableness of the prices paid by the former Military activity responsible for managing the parts.

Audit Response. We do not agree with the DLA's assumption that the prices for sole-source commercial items can be determined reasonable based on current catalog pricing. The Boeing catalog unit price (in constant 1997 dollars) for the parts in question increased 1,105 percent since 1983 and the total quantity of parts purchased in December 1995 (50) was quite a bit higher than the total quantity of parts purchased back in December 1983 (15). Further, only [redacted] of the parts were delivered within [redacted] days and the remainder of the parts were delivered in over [redacted] days. Therefore, it was questionable if the requirements for all the parts was "urgent and compelling." Fortunately, price reasonableness for these parts can be determined in the competitive marketplace since both parts are covered under the Boeing "Rights Guard" agreement. Although the parts in question were included in our review, they were not included in our calculations of overpricing or potential cost avoidances because the parts had previously only been procured from Boeing and not competitively.

Darkened areas (blank spaces) of this report represent data considered "Boeing Proprietary" which has been deleted.

Management Comments on Vendor Stock Retention Model. DLA commented that the DISC Cost/Price Analysis Branch made a business case analysis using the DSCC-developed Vendor Stock Retention model, which assesses the alternative costs/benefits of changes from the current method of customer support. The analysis, which DISC reported supports a conclusion that Boeing's published catalog prices were cost-effective for direct vendor delivery procurements, was performed prior to opening of discussions with Boeing.

Audit Response. We reviewed the analysis performed by DISC used to conclude that Boeing's published catalog prices were cost-effective for direct vendor delivery procurements. Our interpretation of the data is that the DISC conclusion is seriously flawed and cannot be used to show savings associated with direct vendor delivery versus procuring economic order quantities and stocking the items.

DISC used a inappropriately small sample quantity of 40 NSNs without replacement Then, 16 NSNs were not used since they had no annual demand which was required to run the model and 10 additional NSNs were not used because safety level quantities exceeded 5 years. For the remaining 14 NSNs, the model showed cost savings associated with direct vendor delivery for 8 NSNs (4 NSNs actually showed lower unit prices for the catalog items than older comparative prices) and cost increases when direct vendor delivery was used instead of buying economic order quantities and stocking the parts for 6 NSNs. DISC excluded the NSN that showed the largest cost increase using direct vendor delivery ($132,639) versus procuring economic order quantities and stocking the part because it "biased the results." As a result, the model showed a total savings of $4,069 by using direct vendor delivery of the sample items (13 NSNs) and DISC concluded that Boeing's published catalog prices were cost-effective for direct vendor delivery.

Our Quantitative Methods Division provided the following comments on the DISC sample.

> A simple random sample of net size 24 items (40 items selected originally, with 16 items not used due to no annual demand) from a population of 999 items is insufficient to provide statistical dollar projections of usable precision at the 90 percent confidence level For the sample results presented, the range of uncertainty around such an

> estimate exceeds +/- 100 percent. Any attempt to use these results to project or infer population values, therefore, is meaningless Also, the exclusion of sample items may have biased the results
>
> Given the high variability of the sampled items and the use of simple random sampling, the minimum sample size needed to achieve, for example, relative precision of +/- 25 percent at the 90 percent confidence level is approximately 542 items A more complex statistical design, such as stratification, would reduce the sample size.

Direct vendor delivery arrangement certainly can be more cost effective in many instances than buying for wholesale inventory stock; however, the DLA study provided no credible indication that this was true for the parts purchased at Boeing catalog prices.

Management Comments on DISC Price Analysis. DLA commented that prior to award by DISC of the Boeing corporate contract, the DISC Cost/Price Analysis Branch reviewed previous price history and reported that the catalog prices were fair and reasonable.

Audit Response. We reviewed the price analysis performed by DISC used to conclude that Boeing's published catalog prices were fair and reasonable. We believe that the DISC conclusion is seriously flawed and cannot be used to support Boeing catalog prices as fair and reasonable.

DISC reviewed 24 NSNs from the spare parts catalog and compared the prices to previous prices paid by DISC for the same items since January 1994. For 14 of the NSNs, DISC compared the current and previous Boeing catalog prices, which showed no difference, since Boeing had not changed its catalog prices since 1994. For the remaining 10 NSNs, the Boeing catalog price was significantly higher than previous procurements from other suppliers. For 6 of the 10 NSNs the price increases ranged from 494 to 1,978 percent.

Management Comments on Boeing Corporate Contract Orders Placed Through Automated Systems. DLA commented that there is no requirement for further price analysis or a further price reasonableness determination when placing fixed price orders on a noncompetitive basis on indefinite quantity contracts because prices had previously been evaluated prior to award.

Audit Response. Unfortunately, as previously explained, the conclusions reached for the DISC analyses used to support direct vendor delivery and price reasonableness were seriously flawed. Our interpretation of the same limited data, would lead to the opposite conclusions that direct vendor delivery was not cost effective and that the catalog prices were not fair and reasonable.

Management Comments on Availability of Competitive Data Packages. DLA commented that because competitive data packages were not already available or readily attainable for use by contracting personnel and because of the customers urgent need for the items, no other alternative existed but to purchase the items at the Boeing catalog price, which was not negotiable. Therefore, the effectiveness of price analysis would not have altered the prices paid by DLA.

Audit Response. We strongly disagree. Had DLA (DISC) performed effective price analysis before awarding the corporate contract to Boeing, the contract may not have been awarded because it would have been obvious that the price differentials were out of all proportion to the benefits to be gained in the case of almost every part that had previously been procured from other sources. Further, effective price analysis by DLA contracting officers may have helped alert DLA management of the need to obtain competitive data packages before there was an immediate requirement for buying the parts. Better acquisition planning would have provided DLA an alternative to paying the Boeing catalog prices.

Management Comments on Assurances by DCMC Boeing that Commercial Prices Were Fair and Reasonable. DLA did not understand the basis for our conclusion that DCMC representatives never indicated DLA contracting officers should accept Boeing's commercial catalog prices as fair and reasonable.

Audit Response. The DCMC Boeing administrative contracting officer told us that DCMC never indicated DLA contracting officers should accept Boeing's commercial catalog prices as fair and reasonable. We found no indication that this was not factual.

Management Comments on Adequacy of Management Controls for Corporate Contracts. DLA did not agree that the corporate contracting initiative lacked adequate management controls. Also, the quality of controls does not alter the fact that in the absence of a competitive data package, awards were inevitably made at Boeing catalog prices for the sole-source parts.

Audit Response. We believe that the problems identified by the audit clearly show the need to improve management controls in this area. The DLA is, in fact, now taking measures to develop a better structural corporate contracting approach.

Management Comments on Implementing a Corporate Contracting Initiative that Emphasized Reducing Infrastructure Over Customer Prices. DLA did not agree that the corporate contracting initiative emphasized reducing infrastructure over customer prices. Reducing the delivered costs of supplies and services to the Armed Forces is a DLA goal and the corporate contract initiatives are a means of achieving this goal. DISC ran the Vendor Stock Retention model during the planning for the Boeing corporate contract.

Audit Response. The DLA corporate contract with Boeing was definitely not reducing costs of supplies and services to the Armed Forces. Other corporate contracts will need to be reviewed to determine the overall impact to DoD.

Management Comments on Reduced Costs from Competitive Procurements. DLA partially concurred with the potential cost avoidance calculation in the draft report ($13.3 million in the period FY 1998 through 2003), but noted that the resulting amounts were likely substantially overstated. The total increased material cost amounts should reflect offsets for differing terms and conditions, not just modest adjustments for inflation. Additionally, reductions in DLA's infrastructure costs, as well as those made at the Military activities that formerly managed these items, should also be recognized as further offsets to the audit-calculated total increase.

Audit Response. We believe the amount was a conservative calculation; however, after further analysis we have determined that there are too many variables to enable the potential monetary benefits to be calculated at this point. We will revisit the fiscal impact of implementing the agreed-upon corrective actions as part of the audit followup process.

Management Comments on Difficulties Obtaining "Rights Guard" Data. DLA commented that difficulties were historically experienced in obtaining "Rights Guard" data. This sometimes involved substantial Boeing charges due to the need for revisions for different reasons. These difficulties adversely affected the DLA's perceptions and usage of "Rights Guard" as a viable alternative.

Audit Response. We fail to understand why DLA would have such difficulty establishing an effective "Rights Guard" program when the Air Force (OC-ALC) has been so successful implementing its program. Hopefully, the workshop on the "Rights Guard" program hosted by OC-ALC and appropriate training to DLA personnel on how the program works will enable the DLA to overcome these difficulties and effectively implement a program to competitively procure the spare parts.

Management Comments on Infrastructure Cost Offsets. DLA commented that the report did not attempt to quantify any offsetting savings or other benefits of the corporate contracting initiative such as procurement administrative cost avoidance, procurement administrative lead time cost avoidance, and the value of reduced investment in safety level quantities. DLA analysis to date shows reduced safety level quantities of these stock-managed items of $6 million (from $175 million to $169 million).

Audit Response. As reported in the audit, a 172 percent average price increase for the commercial items procured on the corporate contract would be difficult to offset. If the current level of stock-managed parts ($169 million) is overpriced by 172 percent, DLA would need to offset $107 million dollars to justify the price. Once DLA awards its competitive long-term requirement type contracts for the parts, an effective analysis of any savings offset from the DLA corporate contracting initiative can be performed.

Management Comments on Cost Recovery Rate. DLA commented that its logistics mission is uniquely different from that of civilian agencies making a comparison to the lower industrial funding fee on GSA multiple award schedules invalid. The items covered on the GSA schedules are readily available "off-the-shelf" from the supplier's distribution system whereas the high volume readiness demands of Military customers generally have necessitated stockage in a Military warehouse system.

DLA also commented that its weighted average comparison of FY 1998 cost recovery rates for the items in question showed a favorable 32.9 percent rate for DLA versus a 83.3 percent rate for the Military Services.

Audit Response. The comparison to the GSA schedule is valid because the intent of the Boeing corporate contract was to use the Boeing commercial distribution system (available "off-the-shelf" items) so that DoD did not have to stock the parts. The GSA has the same kinds of arrangements with vendors and there is, in fact, direct competition between DLA and GSA to be the central purchaser for many common use items.

We found DLA's comparison of its cost recovery rate to the Military Services questionable. DLA obtained the following FY 1998 cost recovery rates from the Air Force, Air Logistics Centers: Oklahoma City (26.48 percent); San Antonio (25.99 percent); Warner Robins (26.1 percent); and Sacramento (132 percent). Only Sacramento, which was recommended for closure by the Base Realignment and Closure Commission and is now scheduled for privatization, had a higher cost recovery rate than DLA. Using DLA's commercial acquisition item costs, the cost of the items formerly managed by Sacramento represented 54 percent of the total costs (36 percent of the items). Consequently, when the Sacramento cost recovery rate of 132 percent was applied to 54 percent of the total costs, the resulting average cost recovery rate for the Military Services was 83.3 percent. With all the uncertainties involving Sacramento, it may be more appropriate to exclude their data, which results in an average cost recovery rate for the Military Services of 26.15 percent, compared to 34.58 percent for DLA to manage the items. However, a true comparison of cost recovery rates is difficult, because during the consumable item transfer, the Air Force maintained items classified as Depot Level Reparables (complex items repaired at maintenance depots) and repair of these items could significantly impact the Air Force cost recovery rates. DLA was charging the Services a cost recovery rate of 28 percent for doing nothing more than placing an order for them. The Services, through the internet, could have placed the same orders and eliminated the DLA surcharge.

Management Comments on Duplicate Stockage Charges. DLA comments that because they cannot rely on the Boeing commercial distribution system it makes sense for DLA to also stock items and this demonstrates the value added services available from paying DLA's duplicate stockage charges.

Audit Response. We agree it makes sense for DLA to stock items that Boeing cannot support through their commercial distribution system. However, it makes no sense to procure these items from Boeing at their commercial catalog price and pay duplicate stockage charges.

Management Comments on Logistical Reassignment of Item Management Responsibility. DLA commented that based on its comparison of cost recovery rates, a logistical reassignment of item management responsibility to the Military Departments would result in a higher cost, including increased procurement personnel resources.

Audit Response. A logistical reassignment of item management responsibility to the former purchasing organizations would be cost effective if DLA is unable to competitively procure the spare parts, but that decision should not be made until DLA has had a chance to implement its program to competitively procure the items.

Appendix F. Report Distribution

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  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*

Part III - Management Comments

The Under Secretary of Defense for Acquisition and Technology Comments

ACQUISITION AND TECHNOLOGY

OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON
WASHINGTON DC 20301-3000

23 DEC 1997

MEMORANDUM FOR INSPECTOR GENERAL OF THE DEPARMENT OF DEFENSE

SUBJECT: *Sole Source Prices for Commercial Catalog and Noncommercial Spare Parts*, Project No. 6CF-0068.01

Thank you for the opportunity to comment on the subject report. We also appreciate the opportunity you provided us to work with you in resolving this matter I know that you share our commitment to reforming our Acquisition System, so that we can be smarter, work faster and buy better and cheaper products which meet the warfighter's needs. We agree with the findings of your report and recommendations The Deputy Under Secretary of Defense (Logistics) has already undertaken the changes recommended A copy of the letter implementing this recommendation is attached for your information.

Thank you for providing us the opportunity to comment on the draft report

David A Drabkin
Acting Deputy Under Secretary of Defense
(Acquisition Reform)

Attachment
As Stated

24 OCT 1997

(L/MDM)

MEMORANDUM FOR ASSISTANT SECRETARY OF THE ARMY
(INSTALLATIONS, LOGISTICS, AND ENVIRONMENT)
ASSISTANT SECRETARY OF THE NAVY
(RESEARCH, DEVELOPMENT, AND ACQUISITION)
ASSISTANT SECRETARY OF THE AIR FORCE
(ACQUISITION)

SUBJECT: Authority to Purchase Centrally Managed Items From Other Sources

Recent findings by the Department of Defense Inspector General (DoDIG) indicate that: (1) DoD activities should be reminded of the substantial authority they have to purchase centrally managed items from other sources, and (2) the Military Departments should be asked for their views on whether additional local purchase authority is required

First, I request that you remind your activities that substantial authority and flexibility to purchase centrally managed items from other sources, when those sources provide the best value, is established in DoD FAR Supplement (DFARS) 208 7003-1 Attached for your reference is a December 11, 1995 memorandum on the most recent revision to this guidance

Second, I request that you provide me with your views on whether additional authority and flexibility is required. For example, the DoDIG findings note that some centrally managed items such as aircraft spare parts are now available through commercial on-line ordering sources, which may be the "best value" source in some cases (i.e., sole source items with commercial catalog pricing the best available) However, current guidance prohibits application of the "best value" justification for local purchase of a centrally managed item that is " Critical to the safe operation of a weapon system ", as cited in DFARS 208.7003-1(a)(3)(i). I would appreciate receiving by January 31, 1998, your views on whether additional flexibility is required to address this or other issues.

Should further information be required on these matters, Tom Carter may be reached on (703) 697-5216 Thank you for your assistance in this matter

s/ James B Emahiser
(for)
Roy R Willis
Acting Deputy Under Secretary
of Defense (Logistics)

Attachment

Defense Logistics Agency Comments

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

FEB 06 1998

IN REPLY REFER TO DDAI

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING, DEPARTMENT OF DEFENSE

SUBJECT: Draft Report on Sole-Source Prices for Commercial Catalog and Noncommercial Spare parts, 6CF-0068 01

Enclosed are our comments to your request of 15 October 1997 Should you have any questions or further tasking, please notify Sharon Entsminger, 767-6267

Encl

JEFFREY GOLDSTEIN
Chief (Acting), Internal Review Office

cc:
DLSC-PPB
DLSC-BO

Federal Recycling Program Printed on Recycled Paper

SUBJECT: Sole-Source Prices for Commercial Catalog and Noncommercial Spare Parts, 6CF-0068.01

FINDING: Sole-Source Prices for Spare Parts

The Defense Logistics Agency (DLA) purchased commercial catalog and noncommercial spare parts from the Boeing Company (Boeing) on a sole-source basis. The sole-source prices were significantly higher than the competitive prices DoD previously paid for the items. This occurred because DLA contracting personnel:

- failed to evaluate and implement procedures to effectively use the Boeing "Rights Guard" program established by the Air Force to breakout and compete Boeing spare parts by securing limited rights in Boeing's technical data and incorrectly coded items transferred from the Air Force to reflect that they were for noncompetitive acquisition when in fact those items had previously been competitively procured,

- failed to perform adequate price analysis of previous competitive buys to determine whether Boeing sole-source prices were fair and reasonable or whether the items should have been procured competitively;

- improperly accepted Boeing commercial catalog prices as fair and reasonable without adequate support for price reasonableness particularly when DoD was the "primary" customer and there was no competitive commercial market to ensure price integrity; and

- implemented a corporate contracting initiative, without adequate management controls, that emphasized reducing infrastructure over customer prices and inhibited the participation of small businesses in the Federal acquisition process

As a result, DLA paid an average of about 172 percent or $3 2 million (in 1997 constant dollars) more that previous competitive prices for the $5 million of sole-source spare parts purchased from Boeing during CYs 1994 through 1996. We calculate that DLA could reduce costs by at least $13 3 million during CYs 1998 through 2003 if competitive prices are paid for spare parts. DLA also charged its customers a cost recovery rate of about 28 percent ($2 million) for its services in procuring Boeing commercial catalog items. The DLA provided questionable value for those services and DoD was not reaping the benefits of the DLA corporate contracting initiative.

DLA COMMENTS: Partially concur.

1

GENERAL COMMENTS

On April 29, 1997, DLA issued a "heads up" memorandum to Commanders of DLA's "Hardware" Inventory Control Points (ICPs) (i.e., Defense Industrial Supply Center, Philadelphia, PA and Defense Supply Centers Columbus, OH and Richmond, VA) following an in-process audit status briefing given by the IG the previous day at the request of DLA's Senior Procurement Executive The memorandum made three principle points regarding the ongoing audit of DLA's procurement of Boeing spare parts:

i. We advised Commanders that, based on the preliminary IG efforts, it appeared that the Boeing corporate contract was being misused to buy higher value non-urgent requirements and competitive items, on a sole source basis, uses for which it was not intended, and much higher cost was resulting Formerly, the Air Force ICPs had been paying much less on competitive procurements using Boeing "Rights Guard" Program drawings

ii. We advised that the sole source coding of items formerly coded competitive while managed by the Air Force was being questioned; and

iii We advised of our understanding that the corporate contract delivery commitments were not being realized; thus, the value of the DLA corporate contract was being questioned

The memorandum specified local reviews and corrective action as appropriate. Following an update brief given by the IG to the DLA executive team, the DLA Deputy Director (Materiel Management) issued a comprehensive follow-on "action" memorandum to the ICP Commanders on June 9, 1997, requiring a status report concerning specific action items.

The Boeing corporate contract was designed to provide DoD the ability to purchase Boeing's commercial parts at catalog prices when it made business sense to do so The intent was basically to reduce overall costs to DoD (material costs plus infrastructure). It was also believed that by buying small quantities under the commercial catalog, delivery time would be substantially improved The contract was not appropriate for use when there was sufficient data and time to procure the items competitively. As Boeing refused to discount its catalog prices, the contract was not appropriate for stock or quantity buys unless Boeing was the sole source

As the draft report notes ***(see details of the aforementioned memorandum in the IG report section entitled* "DLA Actions During the Audit")***, DLA has taken aggressive action to respond to the issues raised by the IG. This comes at an increasingly challenging period as we continue simultaneously to assimilate the consolidation of inventory control points, the transfer of item management responsibility for consumable items from the Military Services to DLA, and the recent changes in the law regarding the acquisition of commercial items. To meet these challenges, DLA is continuously seeking more efficient and responsive logistics management solutions to meet the needs of the war fighter at the lowest possible costs for both the customer and the taxpayer.

We have now reviewed the resulting draft audit report, obtained ICP comments and conducted independent analyses of several issues. We have concluded that our ICPs paid higher prices to Boeing due to

(i) the unavailability within DLA, and thus to DLA contracting officers, of the manufacturing drawings and associated technical data necessary to award each of the buys in question on a competitive basis within the time frame needed to satisfy the needs of our customers (partly our failure to have procedures in place to assure timely availability of the data); and

(ii) Boeing's unwillingness to depart from its longstanding policy, from which we understand they have not deviated, of selling items contained in its commercial parts catalog (which include the items addressed in the audit) ***only*** at list price, regardless of customer, quantity, or other factors

We believe that the IG report should identify these two issues as the specific causes of the higher prices on the buys in question

DLA concurs that the prices charged by Boeing were significantly higher than the prices DoD previously paid when the items were procured competitively. The IG's willingness to share its tentative findings as they were being developed has enabled DLA and the Hardware ICPs to initiate and institutionalize corrective actions at the earliest possible date As a result, we should be able to realize savings resulting from the audit much earlier than would traditionally have been possible DLA's Hardware ICPs are now obtaining competitive data packages on the items in question and are streamlining processes for identifying needed data and acquiring it in time for the first Hardware ICP buy. This will enable DLA to fully achieve and pass on to Military customers, the opportunity savings that should result from competitive procurements of Boeing parts.

3

Our comments on each aspect of the finding are discussed in detail below:

DLA POSITION ON THE AUDIT FINDING

• **"DLA ...purchased commercial catalog and noncommercial spare parts from the Boeing Company (Boeing) on a sole-source basis..." that "...were significantly higher than the competitive prices DoD previously paid for the items...because DLA contracting personnel..."** ***(see the first paragraph of the finding (above)).*** **Concur.** We note this did **not** occur due to the failures or deficient practices of contracting officers in the performance of their mission.

•• DLA contracting officers have performed in accordance with laws and regulations during and following the mass logistical reassignment from the Services to DLA of item management responsibilities for millions of consumable items (which include most of the items addressed in the audit)

•• Instead of the two specific causes of increased prices paid by DLA identified in our General Comments above, the IG reports that it was due to other causes ***(see the four bulletized subparagraphs following the first paragraph of the finding (restated below))*** As we discuss in detail below, some of these factors, such as the limited participation of some of our Hardware ICPs in the Boeing "Rights Guard" Program, may have contributed secondarily to the higher material cost DLA paid during 1994 - 1996 for the items in question. In any event, we certainly agree that these factors represent opportunities to improve DLA's logistics support for our customers and have taken steps to effect these improvements

••• **"DLA contracting personnel failed to evaluate and implement procedures to effectively use the Boeing "Rights Guard" program established by the Air Force to break out and compete Boeing spare parts by securing limited rights in Boeing's technical data..."** ***(see the first bulletized subparagraph of the finding)*** **Concur.** DLA ICPs' Rights Guard processes did not result in effective use of the Boeing "Rights Guard" program. The lack of procedures to effectively use the "Rights Guard" program is not attributable to DLA contracting personnel The absence of technical data when needed to make the buys competitively led to higher prices.

•••• The "Rights Guard" program is a licensing arrangement provided under several Air Force contracts whereby Boeing technical data packages can be obtained by Government technical specialists for use by contracting personnel to enable

competitive solicitations.

●●●● Our Hardware ICPs have historically encountered difficulties in use of the "Rights Guard" program. However, as a result of actions initiated based on the IG's highlighting this problem to DLA management in April 1997 ***(see the first paragraph under the section entitled "*General Comments*" on page 2 of this response)***, the Hardware ICPs have been working aggressively to overcome these and other difficulties in having competitive data packages available when needed for competitive procurements.

●●●●● The DLA Hardware ICPs are streamlining local procedures to enable more timely access to, and use of, Boeing's technical data for competitive procurements.

●●●●● DLA arranged for representatives from each ICP to participate in a two day "hands-on" workshop hosted by the Oklahoma City Air Logistics Center (OC-ALC), October 22-23, 1997, to exchange information on lessons learned and techniques to maximize utility of the "Rights Guard" program

●●●●● Our Hardware ICPs have advised that they are reviewing all items covered by the audit ***(see IG report Appendix D, entitled* "Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts")***. Further, that various program and item-specific reviews and process audits have been initiated locally to enhance their "Rights Guard" processes and to identify other items for which "Rights Guard" data should be obtained. The objective is to acquire competitive data packages to enable subsequent procurements on a fully competitive basis where appropriate (e.g., quantity, time, best value)

●●●●● We are monitoring the ICPs' improvement initiatives and anticipate follow-on workshops, both internal and joint workshops with OC-ALC, in an effort to assure improved supply availability and prices that are commensurate with the level of logistics support we provide our customers.

●●●●● The success of these on-going initiatives will allow DLA to continue to minimize the total logistics costs to DoD and the taxpayer.

●●● **"DLA contracting personnel...incorrectly coded items transferred from the Air Force to reflect that they were for noncompetitive acquisition when in fact**

those items had previously been competitively procured;" *(see the first bulletized subparagraph of the finding).* **Partially concur.** Recoding of the items in question to a temporary noncompetitive status occurred and was proper This recoding was not a cause of the higher prices, but reflected the lack of data, which caused the higher prices.

●●●● The DLA ICPs recoded items to a noncompetitive status when the customer's needs required the item delivery before a fully competitive technical data package could be updated and obtained. This is in concert with DLA policy and DoD Federal Acquisition Regulation Supplement, Appendix E, "DoD Spare Parts Breakout Program," and is necessary to reflect the current availability of technical data to support procurement of the item competitively. This recoding is proper even though the ICP may eventually obtain a full and open competition data package (either Government-owned data or limited rights data under the Boeing "Rights Guard" licensing program).

●●●● When procurement is to be made of an item that is coded competitive (i e., using the Acquisition Method Code (AMC) and Acquisition Method Suffix Code (AMSC)), the technical specialist provides the necessary technical data package needed to manufacture the item If complete technical data is not available locally, it is necessary to obtain it from the cognizant Military Service's Technical Data Repository or its Engineering Support Activity responsible for design integrity. Depending on the customer's readiness requirement, the data package may not become available until after solicitation issuance Sometimes the urgency of the customer requirement for the part and/or a delay in obtaining a competitive data package from the Services precludes a competitive procurement using the data necessary to manufacture the item. Absent this technical data, we are unable to obtain competition from other potential manufacturers (except in the rare instance where an item had been reverse engineered and the alternate item offer can be qualified before award becomes necessary) In these situations, the AMC/AMSC for the item must be recoded (which is a technical, vice contracting, function requiring expertise in dealing with manufacturing drawings) to reflect the current competitive status for the instant procurement of the item, i e., the unavailability of a technical data package for use by potential offerors When the data package is received and reviewed for completeness, the equipment specialist updates the coding to competitive status.

●●●● We specifically requested our ICPs review the items cited as incorrectly coded in the audit report *(see the IG report Appendix D., entitled* **"Acquisition Method Codes and Technical Data Rights for Boeing Spare Parts").**

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Instances of temporary recoding in connection with the specific buys in question occurred but were proper and consistent with established regulations.

●●●● The IG report should explain that temporary recoding action in support of an individual buy where technical data cannot be obtained in time for a competitive procurement is both proper and necessary. Further, unless an item cited in Appendix D was found by the IG to have been improperly coded upon transfer to DLA

for item management or improperly recoded subsequently, the "incorrect" coding legends should be deleted from the Appendix

●●● "**DLA contracting personnel failed to perform adequate price analysis of previous competitive buys to determine whether Boeing sole-source prices were fair and reasonable...**" ***(see the second bulletized subparagraph of the finding)*** **Partially concur** that price analysis of some previous competitive buy prices could have been more thorough.

●●●● Normally, price analysis performed on repetitive buys involves reference to previous buy prices and pricing information utilized in making the prior buys.

●●●● Comparison to the price paid on the prior buy is the technique the IG used as the basis for reporting the fact that DLA paid more than previous competitive prices.

●●●● For reasons detailed below, this comparative price analysis technique has limited or no applicability when older buys are involved, which is the case in the majority of the instances in question:

●●●●● The buys in question were made in the 1994 - 1996 period and generally within a couple years following transfer of the item to DLA. The following data summarizes the age of the individual prior awards the IG used in calculating the price increases, and whether the ICP placing this prior award was the same DLA ICP or a different ICP (DLA or Military):

Calendar Year	Prior ICP Same DLA	Prior ICP Other DLA	Prior ICP Military	Percent
'92 - '96	47		18	44%
'87 - '91	2	2	28	22%
'82 - '86	4		34	26%
'78 - '81	0	_	11	8%
Total (146)	53	2	91	100%

●●●●● Most of these prior buy folders would not have been available for buyer review. The contract files for prior buys made by the same DLA ICP may be available for about three years. Conversely, at best, the only contract folders forwarded on logistic reassignment (most occurred beginning in 1992) of an item to a gaining DLA ICP are those for open contracts

●●●●● Even if a buy folder for a prior buy had been available, policy restrictions would likely have precluded use of this technique

●●●●●● Federal Acquisition Regulation, paragraph 15.805-2(b) authorizes the comparison of current prices to prior contract prices, **subject to** consideration of differences in specifications, quantities ordered, time for delivery, Government-furnished materials, etc. Further, it specifies that "Any comparison will not be valid unless the reasonableness of the prior price was established. [underlining added for emphasis]"

●●●●●● The only adjustment made by the IG in calculating price growth using this price comparison technique to prior buys was for inflation

●●●●●● There was no way for the DLA buyers of the large majority of the buys in question to: (i) have or acquire the knowledge necessary to adjust for different procurement/production circumstances that existed many years previously at a different (Military) activity, nor (ii) confirm that the prices paid on those prior awards made by the Military activities that had previously managed the parts had been determined reasonable.

●●●●● Therefore, use of comparative price analysis to these prior buys was thus generally not an option available to DLA contracting personnel for use in assessing price reasonableness.

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●●●● The requirements for price analysis vary depending on whether a competitive or a noncompetitive item is being purchased (e.g., under a Basic Ordering Agreement (BOA)) or ordered (e.g., under an existing indefinite delivery type contract (IDTC)), as discussed below:

●●●●● **Orders under the Air Force BOAs.**

●●●●●● Price analysis and a price reasonableness determination are required for orders placed under Basic Ordering Agreements, such as the two Air Force instruments under which DLA ICPs placed orders reviewed by the IG. This is because the orders themselves constitute individual contracts.

●●●●●● NSNs 1560-01-273-4323 & -4324. The IG points out *(see the IG report, second paragraph of the subsection entitled "***Accepting Commercial Catalog Prices as Fair and Reasonable***" under the section entitled "***Boeing Commercial Catalog Prices***")* that 25 of each structural support was purchased in December 1995 for total prices of $483,350 for each NSN (which is below the statutory threshold for which cost or pricing data is required, but regardless, would have been exempted from this requirement because these items meet the commercial definition). The requirement for both buys in question was urgent and compelling One firm was solicited under other than full and open competitive procedures and price was determined reasonable based on current catalog pricing

●●●●●● As the IG notes, the last DoD procurement of these parts was in 1983. In the recent buy, the buyer had no way of knowing and making appropriate adjustments for different circumstances that very well may have existed twelve years previously, and no way to confirm the reasonableness of the prices paid by the former Military activity (Oklahoma City Air Logistics Center) responsible for managing the parts. We note that the 1983 buy for both items had been included on a combined order. Knowledge of whether these were part of a much larger procurement is unavailable, as well as whether these parts were in production in support of aircraft production at that time. If the parts were in production at that time, the price of the 1983 buy should have avoided setup costs that undoubtedly were included in the DLA buy. Further, the prior savings for higher volume raw materials purchases and the former production efficiencies would not have been available at the time of the DLA buys. The inability to know, and to make price adjustments for prior circumstances, and to meet the FAR requirement of knowing whether the prior price was deemed fair and reasonable,

precluded reliance on comparative price analysis in this instance (and many other instances) as a means of analyzing the catalog price and determining price reasonableness for the instant buy.

●●●● **Orders under the DLA corporate contract:**

●●●●● The DISC Cost/Price Analysis Branch made a business case analysis using the DSCC-developed Vendor Stock Retention model, which assesses the alternative costs/benefits of changes from the current method of customer support. The analysis, which DISC reports supported a conclusion that Boeing's published prices were cost-effective for direct vendor delivery procurements, was performed prior to the opening of discussions with Boeing

●●●●● In addition, prior to award by DISC of the Boeing corporate contract (an indefinite quantity long-term contract (IQC)) , the DISC Cost/Price Analysis Branch reviewed previous price history, adjusted for inflation and quantity differences, and then compared these prices to the base year catalog prices for a statistical sample of catalog items. DISC reported that the catalog prices were fair and reasonable.

●●●●● From the inception of the Boeing corporate contract, buys of noncompetitive items covered by the contract were ordered through automated systems. There is no requirement for further price analysis or a further price reasonableness determination when placing fixed price orders on a noncompetitive basis under existing IQCs because prices had previously been evaluated prior to award When using the corporate contract price as a standing quote in a competitive procurement, however, price(s) must be analyzed and supported in a price reasonableness determination, before an order may be placed for a competitive item

●●●● Finally, we understand that Boeing has consistently sold commercial parts (i.e., those covered by the corporate contract) at the established catalog price to all customers, regardless of quantity required.

●●●● In conclusion:

●●●●● We note that the substantial price increases reported by the IG were calculated by comparison to prior, often very old buys, such as in the buys for

the NSNs addressed on page 8 of our response The only adjustment was for inflation. Such a comparison to prior buys made in different circumstances may provide some basis for comparison but it must be recognized that the order or magnitude of such results renders the result not fully credible.

●●●●● As use of this technique was, in effect, not sanctioned for contract pricing purposes involving the large majority of the buys in question, we believe it should not be relied on for IG audit reporting purposes.

●●●●● Because (i) competitive data packages were not already available or readily attainable for use by DLA contracting personnel at the time the items had to be ordered; (ii) further delay in meeting the customer's urgent need for the item was not an option; and because (iii) no other alternative existed but to purchase/order at Boeing's catalog price, which was not negotiable, we have concluded that the level of effectiveness of the price analysis would not have altered the prices of these DLA buys.

●●● **"DLA contracting personnel failed to perform adequate price analysis of previous competitive buys to determine whether ...the items should have been procured competitively;"** ***(see the second bulletized subparagraph of the finding).*** **Partially concur** that price analysis of previous competitive buy prices was not always adequate. Competitive-coded items and other items not blocked from automated ordering were routed to DLA contracting officers for procurements Local reviews of the buys folders confirmed that competition was sought. However, in most cases competition was not obtained. When an alternate offer was received, it could not be supported by technical data owned or licensed to the offeror. This inevitably led to placing an order with Boeing when customer needs for the item precluded further delay in the award. This situation should be reduced in the future with DLA's efforts to project future needs and obtain Government-owned drawings and "Rights Guard" program technical data.

●●● **"DLA contracting personnel improperly accepted Boeing commercial catalog prices as fair and reasonable without adequate support for price reasonableness particularly when DoD was the "primary" customer and there was no competitive commercial market to ensure price integrity."** ***(see the third bulletized subparagraph of the finding)*** **Partially concur** that price reasonableness determinations were not always adequate

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●●●● DLA agrees that this sometimes occurred, for the extenuating reasons addressed in the IG report ***(see the IG report subsection entitled* "Accepting Commercial Catalog Prices as Fair and Reasonable" *under the section entitled* "Boeing Commercial Catalog Prices")***.

●●●● Regardless, this did not result in higher prices for items bought using the Boeing catalog. DLA would like to receive reasonable volume discounts where appropriate, but Boeing steadfastly declined to offer or negotiate a quantity purchase or other discount from its catalog prices. We note that Boeing essentially confirmed this position to the IG during the audit ***(see the IG report subsection entitled* "Commercial Items Evaluated by Boeing" *under the section entitled* "Boeing Commercial Catalog Prices")***.

●●●● The IG report addressed the impact of DoD's unstable demand patterns ***(see IG report subsection entitled* "Importance of Recent Sales of Similar Quantities and Substantial Sales" *under the section entitled* "Boeing Commercial Catalog Prices)***. The report suggests that "...the large purchase of commercial items by DLA may not help to lower the Boeing catalog prices because of the infrequency of the purchases and difficulty for Boeing in forecasting requirements." However, it concludes that "Therefore, by procuring large infrequent quantities..., DLA was actually causing commercial catalog prices to increase " Appropriate revisions should be made, e g , by including the rationale for this conclusion in the report; otherwise, recommend the discussion of this matter be deleted

●●●● The IG noted some confusion as to why DLA contracting officers accepted Boeing commercial catalog prices as fair and reasonable ***(see the third paragraph of the IG report subsection entitled* "Accepting Commercial Catalog Prices as Fair and Reasonable" *under the section entitled* "Boeing Commercial Catalog Prices")***. However, the final sentence of this paragraph indicates the IG believes it has reached a conclusion through interviews as to whether assurances that these prices were fair and reasonable were given by DCMC Boeing representatives. Recommend this be omitted; otherwise, that it be expanded to explain the basis for the conclusion.

●●● "**DLA contracting personnel implemented a corporate contracting initiative, without adequate management controls...**" ***(see the fourth bulletized subparagraph of the finding)***. **Nonconcur** that the corporate contracting initiative

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lacked adequate management controls. DLSC and the ICPs have management control plans with objectives specifically targeted towards insuring adequate oversight and control over contracting and contract pricing. The controls to ensure that DLA procured spare parts competitively, paid fair and reasonable prices for commercial items, and provided added value on using corporate contracts for commercial items were apparently deemed inadequate at the three involved DLA ICPs ***(see the IG report Appendix A paragraph entitled* "Adequacy of Management Controls" *under the section entitled* "Management Control Program")*** because of the higher procurement prices DLA paid than paid by the Military prior to logistics reassignment The quality of the controls for these factors does not alter the fact that in the absence of a competitive data package, awards were inevitably made at Boeing catalog prices for these sole source parts.

••• **"DLA contracting personnel implemented a corporate contracting initiative...that emphasized reducing infrastructure over customer prices..."** ***(see the fourth bulletized subparagraph of the finding)***. **Nonconcur** that the corporate contracting initiative emphasized reducing infrastructure over customer prices. Reducing the delivered costs of supplies and services to the Armed Forces is a DLA goal. DLA's corporate contracting initiatives are a means of achieving this goal DLA is attempting to reduce its own logistics overhead (as well as that of its customers where possible), while at the same time reducing material unit costs by leveraging DLA's or DoD's buying power. As previously stated ***(see the first paragraph of our discussion under the caption* "Orders under the DLA corporate contract," *on page 9 above)***, DISC ran the Vendor Stock Retention model during planning for the Boeing corporate contract. The model assessed the overall cost impact (material prices plus infrastructure changes) of a switch in method of support to reliance on the Boeing commercial inventory/distribution system. The higher prices DLA is paying to Boeing is resulting in part because, absent a competitive data package, our contracting officers had no alternative but to order from Boeing at catalog prices for these sole source parts. And, as discussed earlier, DLA has been unsuccessful in achieving volume discounts from Boeing. Use of a different contractual vehicle would not have altered this outcome.

••• **"DLA contracting personnel implemented a corporate contracting initiative..." that "...inhibited the participation of small businesses in the Federal acquisition process."** ***(see the fourth bulletized subparagraph of the finding)***. **Partially concur** that the corporate contracting initiative did not continue the small business contracting opportunities afforded by the former Service ICPs for these parts. Since many of the corporate contract delivery orders were originally solicited competitively by the ICPs, small business participation was sought, although,

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unfortunately none was forthcoming, due to the absence of competitive data packages. This is being remedied by our efforts to fully utilize the Boeing "Right Guard" program Although orders were ultimately placed with Boeing, the corporation has implemented a Small and Small Disadvantaged Business Plan and has pledged to meet agreed upon small business subcontracting goals. Many Boeing parts supplied under the corporate contract are in fact supplied from small business manufacturers. Furthermore, the initiatives resulting from shortcomings the IG highlighted to DLA management last year will create competition and expand opportunities for small business participation as prime contractors. However, when these previous orders were placed, adequate technical data packages were not available to our contracting officers to enable competitive procurements. Therefore, they could not avoid sole source purchases at Boeing's catalog prices, regardless of the contracting instrument used to obtain the items.

• **"DLA paid an average of about 172 percent or $3.2 million (in 1997 constant dollars) more than previous competitive prices for $5 million of sole-source spare parts purchased from Boeing during CYs 1994 through 1996. We calculate that DLA could reduce costs by at least $13.3 million during CYs 1998 through during CYs 1998 through 2003 if competitive prices are paid for the commercial items."** ***(see the first two sentences, final paragraph of the finding)*** **Partially concur** in this IG conclusion; ***but*** **note** that the resulting amounts are likely substantially overstated. The total increased material cost amounts should reflect offsets for differing terms and conditions, not just a modest adjustment for inflation Additionally, reductions in DLA's infrastructure costs, as well as those made at the Military activities that formerly managed these item, should also be recognized as further offsets to the audit-calculated total increase

•• As noted above, the cost difference principally occurred because technical data packages owned by the Government for certain of the items had not been furnished by, or obtained from, the Military activities that previously procured the items competitively, nor was the data obtained under the Boeing "Rights Guard" program, in time to make these procurements on a competitive basis. Difficulties were historically experienced by the DLA ICPs in obtaining "Rights Guard" data. This sometimes involved substantial Boeing charges due to the need for revisions when production methods have changed and/or use of previous machinery is no longer cost-effective or possible (e.g., machine obsolescence)). These difficulties adversely affected the DLA ICPs' perceptions and usage of "Rights Guard" as a viable alternative.

•• Material cost offsets. As noted above *(see our discussion of NSNs 1560-01-273-4323 & -4324 on page 8 above)* there is a large time frame between the buys questioned by the IG and the year in which the prior buys were made, normally by a Military activity. Intuitively, we would expect that this would tend to result in overstated results. The inability to identify the differences, much less adequately adjust for them, may be why no attempt was made. However, we believe the existence of these unknowns and the potential for a large overstatement of the price disparity should be addressed in the report

•• Infrastructure cost offsets. The IG reported that informal procedures in use at DSCR and DISC helped reduce the infrastructure needed to procure the items *(see the IG report subsection entitled* **"How DLA Used the Boeing Corporate Contract"** *under the section entitled* **"DLA Corporate Contracting Initiative"***)*, but did not attempt to quantify any offsetting savings or other benefits of our corporate contracting initiative. Adjustments would be appropriate for such things as procurement administrative cost avoidance, procurement administrative lead time cost avoidance, and the value of reduced investment in safety level quantities. Based on a DLA analysis of orders to date under that contract, DLA ICPs reduced their investment in the Safety Level Quantity on these stock-managed items by $6 million (from $175 million to $169 million).

• "DLA also charged its customers a cost recovery rate of about 28 percent ($2 million) for its services in procuring Boeing commercial catalog items..." *(see the third sentence, final paragraph of the finding).* **Concur** in this IG conclusion.

•• Like other service organizations, DLA ICPs are required to recoup total costs of operations. For inventory control points, this includes total costs to manage and procure the items, transportation, price [inflation] stabilization, and may include depot costs, disposal costs, etc These costs and other factors, such as differences in the method of customer support and item management, result in differing cost recovery rates tailored to individual commodity groups.

•• DLA is a combat logistics agency, performing a complex mission of challenging dimensions in assuring unfailing, value added support to the war fighter around the clock around the world. DLA's logistics mission is uniquely different from that of civilian agencies. Making a comparison to the lower industrial funding fee on GSA multiple award schedules is invalid *(see the IG report, third paragraph of the subsection entitled* **"DLA Cost Recovery Rates"** *under the section of the same name)* because the items covered on those schedule contracts are readily available "off-the-shelf" from the supplier's distribution system (whereas the high volume readiness demands of Military

customers generally have necessitated stockage in a Military warehouse system) Recommend this comparison be deleted.

•• DLA's Military customers continue to operate activities that overhaul repairable items and purchase consumables in support of that function. DLA's streamlined operations enable customer support at rates that compare favorably with the cost recovery rates of the Military activities which formerly managed these Boeing parts:

••• The 28 percent was a composite average the IG calculated from orders under the earlier of the two BOAs it reviewed plus orders under the DLA corporate contract. We obtained the buy data the IG used in computing the 28 percent ***(see the IG report recap in* Table 3, "DLA Cost Recovery Rates For Boeing Commercial Items," *under the section entitled* "DLA Cost Recovery Rates")**, which we repriced using the actual FY 1998 cost recovery rates used by the current DLA ICPs for these individual items. We then recomputed the total cost recovery using the actual FY 1998 cost recovery rates that would have been applied for FY 1998 by the Military Services' individual ICPs that had responsibility for each item prior to item transfer to DLA. Weighted average results were **32.9 percent DLA** rate ***vice* 83.3 percent** cost recovery rate had the items in question not been transferred for DLA management.

••• In performing this analysis, we used IG report data (Appendix D), to determine the current and previous buying activities. In some instances where the previous activity is shown as DLA, we were able to identify from our procurement histories, the non-DLA activity that managed the items prior to transfer, i e., OC-ALC's former NSNs 1560,00-910-9136, 1560-00-927-3793, 1560-01-039-3293, 1560-01-163-1726, 1560-01-176-5269, 1560-01-178-0995, 3020-00-341-9436, and 3040-00-233-1116, OO-ALC's former NSNs 1560-01-014-7342, 1560-01-021-5527 and 5306-01-014-7744; SA-ALC's former NSNs 1560-01-019-8146 and 3040-00-586-8631; SM-ALC's former NSN 1560-01-165-5090; and WR-ALC's former NSN 3110-00-925-8601 We included the buys of these items in our calculations using the FY 1998 cost recovery rate for these Military activities. This made the results more reliable due to the increased number and dollar size of the portion of the IG's spreadsheet data that reflected a change from Military to DLA management.

• "**DLA provided questionable value for those services [i.e., meeting customer requirements for Boeing commercial parts] and DoD was not reaping the benefits of the DLA corporate contracting initiative**." ***(see the second sentence, final paragraph of the finding).*** **Partially concur** in this IG conclusion. The Boeing contract does not provide all the benefits we hope to achieve from corporate contracts because Boeing

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doesn't provide quantity discounts.

●● The IG report addresses a DLA briefing citing the benefits of DLA corporate contracts, i.e., lower product costs, ease of use, opportunity to reduce customer support infrastructure and improved delivery ***(see the IG report paragraph entitled "DLA Corporate Contracting Initiative," under the section with this same title).*** This reports the IG's agreement that the Boeing corporate contract is easy to use and provides an opportunity to reduce infrastructure. Further, the IG agrees that it has improved deliveries for small (but not larger) quantities of parts; however, it reports that "customer product costs increased significantly."

●● Our brief provided an overview of the benefits of corporate contracts, but we want to underscore that **each** corporate contract is unique and all of these benefits are not obtainable in every instance. In the case of Boeing, the primary benefit was to be very substantial reductions in total logistics support time frames, i e., (i) reducing the Government's procurement administrative lead time by having a contract in place from which orders for direct vendor delivery could be ordered in one day by DLA's automated Paperless Order Processing System (POPS), plus (ii) eliminating the production lead time historically required in procurements through Boeing's Military Aircraft Company, by providing the "off-the-shelf" 0-10 day order/ship time frame that is available via access to Boeing's commercial parts system These reductions would be of substantial benefit for urgently needed items and for all lower valued orders.

●● As a result of the in-process IG briefs last Spring, DLA learned that the anticipated delivery benefit had not yet been substantially achieved, based on the IG's review of parts shipped under the contract from inception (December 1995) through (March 21, 1997) ***(see the IG report subsection entitled "Commercial Item Delivery," under the section entitled "Boeing Corporate Contract Prices").*** As a result, we promptly referred this matter for ICP command attention The ICPs using the corporate contract (DISC and DSCR) have confirmed that larger quantity stock replenishment requirements were being ordered. This substantially exceeded Boeing's traditional stockage levels needed to support its commercial customers, resulting in back orders

●● We expect that the full benefits of this contract will be realized when the ICPs acquire the competitive data packages and compete future buys among actual manufacturers and other potential sources. This should reduce the average order quantities placed on a periodic basis for Boeing direct delivery to our customers. Once our demand pattern for these items becomes predictable, Boeing should be able to supply our customers' needs within the normal time frames of its commercial

inventory/distribution system.

•• The report goes on to state ***(see the second and fifth paragraphs, respectively, of the IG report subsection entitled* "DLA Added Value Procuring, Shipping, and Stocking Boeing Commercial Items," *under the section entitled* "DLA Cost Recovery Rates")*** that:

••• "DLA was procuring Boeing commercial items and stocking the items in DLA warehouses, which resulted in DLA customers paying duplicate stocking costs to Boeing as part of the catalog price, and to DLA as part of the cost recovery rate." DLA notes this is not "duplicate" stocking but rather equates to the two-tier commercial distribution system commonly employed throughout the general economy

••• "Included in the DLA cost recovery rate were shipping costs which DLA customers would also pay twice, first the items were shipped from Boeing to the DLA depot, then from the depot to the customer." DLA notes this is not duplicative but consistent with two-tier Original Equipment Manufacturer (OEM)-to-distributor-to-customer distribution systems, which to date has not been seriously challenged in many business segments by efforts to adopt direct, OEM-to-consumer models.

••• "If DoD wants to procure commercial items from Boeing, true commercial business practices should be adopted such as only procuring actual requirements and using direct vendor delivery." DLA notes that for many Boeing parts, this has shown to be economically infeasible and unacceptable for maintaining ample Military readiness, across the spectrum of different Military scenarios

•• In referring to the 28 percent composite cost recovery rate, the IG reports ***(see the IG report recap in* Table 3, "DLA Cost Recovery Rates For Boeing Commercial Items," *under the section entitled* "DLA Cost Recovery Rates"),*** "the rates are not appropriate for POPS orders of commercial for direct vendor delivery." We agree. As can be seen in reviewing Table 3, the majority of the total value of award the IG used in calculating this composite are under the 1992 Air Force BOAs Orders thereunder constitute individual contracts POPS is a technique for the automated ordering (without buyer involvement) under existing contracts of items coded noncompetitive. A number of the items ultimately ordered under the corporate contract initially were referred for buyer action because the items were coded competitive. Even though these were ultimately ordered under the corporate contract, the customers were charged the normal cost recovery rate vice the lower, POPs rate, because these were not POPS orders We note that the that the cost recovery rates at our Hardware ICPs range from about 7 to 19 percent for FY 1998, depending on the ICP and method of support

●● We believe that DLA is providing value for customer logistics support as demonstrated by the examples the IG cited ***(see the third and fourth paragraphs, respectively, of this same subsection)*** to make the points in the preceding three bulletized quotations cited in the preceding page of this response :

●●● NSN 1650-00-692-7488. The IG points out that at the time of a DLA ICP stock replenishment order (February 1996) for 246 of these spoiler actuator sleeve units, Boeing had 9 units in stock. These were shipped [redacted] days later (April 1996), with the remainder shipped betwee[redacted] and [redacted] days after order (August 1996). We note that because we stocked this item, Defense Depot Susquehanna, PA was able to immediately meet a customer's requirement by shipping 101 units in July 1996. Our inability to obtain sufficient quantities to support Military requirements of this item from Boeing's commercial distribution center is typical and demonstrates the value added services available from paying DLA's "duplicate stockage" charges for sole source items

●●● NSN 5320-01-255-4649. The IG points out that, for a DLA ICP stock replenishment order (June 1996) for 1,677 [actually 3,200] of t[redacted] units, Boeing shippe[redacted] units the next day and the remaining [redacted] further, that the DLA cost recovery rate was 55 percent [dropped to 44.2 percent for FY 1998] o[redacted] [actually [redacted]] for an order where the parts only cost [redacted] actually [redacted]] We, instead, note that this is yet another example why DoD cannot totally rely on supply availability under Boeing's commercial distribution system.

●● The IG expressed the opinion that "...it would be most efficient to authorize the Air Force to purchase commercial items if competitive procurement is infeasible. This would reduce Air Force costs by the 28 percent DLA surcharge."

●●● We note that authorization already exists to purchase its requirements of these items (DFARS 208.7003). The threshold for file documentation required to justify local purchase of an item assigned for integrated materiel management was recently increased to the micro-purchase threshold ($2,500) and the threshold at which a waiver is required was increased to the simplified acquisition threshold ($100,000).

●●● DLA is taking steps to enable competitive procurements of these items in the future.

●●● As previously pointed out in the FY 1998 cost recovery rate comparison ***(see page 15 of this response)***, a logistical reassignment of item management responsibility to the former Military activities would result in a higher cost (not to

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Darkened areas (blank spaces) of this report represent data considered "Boeing Proprietary" which has been deleted.

mention the issue of necessitating additional procurement personnel resourcing). If instead, individual Military customers were to assume direct purchase responsibility, some increase in procurement administrative costs should likewise be anticipated, which would at least partially offset the potential avoidance of the 7 to 19 percent current POPS rates DLA ICPs apply for FY 1998

•• Based on a study of orders to date under the Boeing corporate contract, we determined that the DLA "Hardware" ICPs were able to raise supply availability on NSNs covered thereunder from a pre-contract average of 69.8% in the FYs 1994/1995 time frame, to 73.2 percent during the FYs 1996/1997 period (under the contract).

•• In conclusion, we believe the above detailed discussion demonstrates that DLA is providing value added logistical support to the Services. And, as DLA obtains the needed competitive technical data packages and other on-going initiatives stemming from the IG's in-process briefings are institutionalized, DoD will realize the full potential benefits of DLA's corporate contracting and more advanced logistics support initiatives.

RECOMMENDATION 1: We recommend that the Under Secretary for Acquisition and Technology.

a Determine whether the Military Departments have the authority and flexibility under existing procurement regulations to use sources of supply for commercial items other than the integrated material manager, when other sources offer the best value.

b. If flexibility does not exist for the Military Departments to locally procure commercial items, the Under Secretary should propose such changes to procurement regulations If flexibility does exist, the Under Secretary should inform the Military Departments of the authority to locally purchase commercial items

DLA COMMENTS: Defer to OSD inasmuch as this recommendation is directed thereto vice DLA.

DISPOSITION: CONSIDERED COMPLETE

RECOMMENDATION 2: Recommend that the Director, Defense Logistics Agency require the Commanders, Defense Supply Center Columbus, Defense Supply Center Richmond and the Defense Industrial Supply Center to review as part of their management control program self-evaluation, sole-source procurement, commercial items prices, and corporate contracting.

DLA COMMENTS: Concur. The ICPs have management control plans with objectives **generally** targeted towards insuring adequate oversight and control over contracting and contract pricing. DLA annually evaluates the system of internal control of the procurement function in support of the annual statement of assurance required under the Federal Managers' Financial Integrity Act of 1982 The DLA plan for FY 1997 identified "Pricing Oversight" as one of eleven key areas of oversight necessary to ensure operations are relatively free of fraud, waste, abuse, and/or mismanagement. Various surveillance techniques are used, including resolution of problems identified through IG audits. The plan cited spare parts overpricing as a specific area of focus and spelled out the corrective action that was being taken to overcome spare parts overpricing identified in an earlier IG audit that was ongoing at that time of our annual statement of assurance for 1997 (September 1997)

In an effort to assure full understanding of this recommendation, we held several follow-up discussions with the IG. The project manager for this audit advised on February 2, 1998, that the objective of this recommendation is that DLA have a process to assure that corporate contracts and other new business practices initiatives do not result in substantially higher material costs to the customer. We advised that DLA had recognized management's need for a structured approach, which led to development and issuance of a comprehensive management policy providing appropriate internal controls. The policy (cited below): prescribes a standard format for reporting the results of a Business Case Analysis (BCA) in support of proposed new initiatives, establishes headquarters review and approval mechanisms, and states that metrics in the BCA will be used to assure the projected benefits are achieved during contract performance

In supplemental guidance included in Revision 4 to our Defense Logistics Acquisition Directive (DLAD 4105.1), we added a paragraph at 7-102 (b) specifying that.

"A Business Case Analysis, in accordance with MM Memorandum dated May 15, 1997, subject: DLA Materiel Management (MM) Initiative Management Policy, shall be accomplished coincident with planning for a Shift to Commercial Practices The price comparison shall be made on the basis of total estimated costs to the customer, i.e., materiel purchase cost plus the cost recovery markup for logistics support costs charged by DLA, plus an estimate of the customers' own logistics costs (storage, delivery, forecasting, requisitioning or buying, etc.). The analysis, which shall be retained in the resulting contract file, shall demonstrate that the support decision and the resulting purchase decisions will provide added value to our customers (e.g , lower overall costs inclusive of their logistics costs, improved deliveries, and/or enhanced supplier support, etc.) "

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The IG correctly points out the need to **specifically** review sole-source procurements, commercial item prices and corporate contracting Commanders should specifically review all innovative business practices to determine if they are operating in a manner consistent with the best interests of our customers.

DISPOSITION: ONGOING. ECD: 30 Sep 98

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