

Audit



Report

PROCURING FUEL AND GROUND HANDLING SERVICES
AT COMMERCIAL AIRPORTS

Report Number 98-189

August 18, 1998

Office of the Inspector General
Department of Defense

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Acronyms

AIR
DESC
FBO

Aviation Into-Plane Reimbursement
Defense Energy Support Center
Fixed-Base Operator



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

August 18, 1998

MEMORANDUM FOR DIRECTOR, DEFENSE LOGISTICS AGENCY
ASSISTANT DEPUTY UNDER SECRETARY OF DEFENSE
(MATERIEL AND DISTRIBUTION MANAGEMENT)

SUBJECT: Audit Report on Procuring Fuel and Ground Handling Services at
Commercial Airports (Report No. 98-189)

We are providing this report for your information and use. This is the second in a series of reports on DoD management of fuels. This audit was requested by the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management).

We considered management comments on a draft of this report in preparing the final report. The comments conformed to the requirements of DoD Directive 7650.3 and left no unresolved issues. Therefore, no additional comments are required.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Ms. Evelyn R. Klemstine at (703) 604-9172 (DSN 664-9172), e-mail eklemstine@dodig.osd.mil, or Mr. John Yonaitis at (703) 604-9632 (DSN 664-9632), e-mail jyonaitis@dodig.osd.mil. See Appendix D for the report distribution. The audit team members are listed inside the back cover.

A handwritten signature in black ink that reads "Robert J. Lieberman".

Robert J. Lieberman
Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. 98-189
(Project No. 7LG-5030.01)

August 18, 1998

Procuring Fuel and Ground Handling Services at Commercial Airports

Executive Summary

Introduction. This report is the second in a series of reports on DoD management of fuels. This audit was requested by the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management). DoD pilots usually obtain fuel and ground handling services at military installations; however, mission requirements sometime dictate landing at commercial airports. On those occasions, DoD pilots purchase fuel from fixed-base operators at commercial airports using into-plane contracts, the aviation into-plane reimbursement card, or local purchase procedures. DoD also uses the aviation into-plane reimbursement card and local purchase procedures to obtain ground handling services at commercial airports. DoD used the aviation into-plane reimbursement card to procure \$10.5 million of fuel from May 1, 1997, through April 30, 1998.

Audit Objectives. The overall audit objective was to evaluate the management of and processes used to procure, store, and account for fuels to meet U.S. European Command requirements for regional contingencies. The specific objective for this segment of the audit was to determine the most cost-effective acquisition strategy for procuring aviation fuel and to determine whether prices for ground handling services were reasonable at commercial airports. Specifically, the Assistant Deputy Under Secretary of Defense (Material and Distribution Management) had requested that we determine whether cost-effective commercial alternatives existed for into-plane contracting and whether fixed-base operators with into-plane contracts were increasing prices charged for ground handling services to compensate for the lower fuel prices negotiated in into-plane contracts. We also reviewed the management control program as it related to the audit objective.

Inspector General, DoD, Report No. 98-114, "Fuel War Reserves for the European Theater," April 16, 1998, discusses the requirements determination process for fuel war reserves. A subsequent audit will cover implementation of the role specialist nation concept for the supply of fuel to multinational forces in the European theater.

Audit Results. The prices in into-plane contracts were generally lower than the prices available through the use of the aviation into-plane reimbursement card and significantly lower than commercial prices at commercial airports. However, the actual cost-effectiveness of into-plane contracts over commercial alternatives could not be determined because the Defense Energy Support Center had not evaluated the prime vendor strategy for procuring fuel at commercial airports. As a result, the Defense Energy Support Center cannot be assured that the acquisition strategy for procuring fuel at commercial airports provides the best value to DoD (Finding A).

Based on our review of the 30 fixed-base operators, we found no indication that fixed-base operators increased prices for ground handling services as a means to compensate for lower fuel prices negotiated in into-plane contracts. Although the 30 fixed-base operators contacted had different methodologies for determining prices for ground handling services, those methodologies did not result in price increases to DoD (Finding B).

Management controls were adequate as they applied to the audit objectives (Appendix A).

Summary of Recommendations. We recommend that the Defense Energy Support Center issue a request for information to potential prime vendors to identify their abilities for providing fixed-base operator support at commercial airports and to determine the feasibility of using the prime vendor strategy for providing fixed-base operator support at commercial airports.

Management Comments. The Defense Energy Support Center concurred with the findings and the recommendations. A discussion of management comments is in Part I and the complete text is in Part III.

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Part I - Audit Results

Audit Background

DoD pilots usually obtain fuel and ground handling services at military installations; however, mission requirements sometimes dictate that they land at commercial airports. Commercial airports have on-site commercial businesses that provide fuel and ground handling services. The businesses are referred to as fixed-base operators (FBOs). DoD pilots purchase fuel from the FBOs at commercial airports using into-plane contracts, the aviation into-plane reimbursement (AIR) card, or local purchase procedures. DoD pilots also use the AIR card and local purchase procedures to obtain ground handling services at commercial airports.

Into-Plane Contracts. Into-plane contracts are multi-year agreements between the Defense Energy Support Center (DESC) and FBOs for the purchase of fuel with additives¹ at commercial airports. DESC establishes into-plane contracts at commercial airports where DoD anticipates fuel requirements of at least 15,000 gallons per year. Into-plane contracts include military standards for fuel quality, but do not guarantee that DoD will purchase minimum or maximum fuel quantities. As of October 1, 1997, DESC had awarded 337 into-plane contracts for 507 airports worldwide, comprising 308 contracts for 338 airports in the continental United States and 29 contracts for 169 airports in Alaska, Hawaii, and 88 countries. During FY 1997, about \$167 million of fuel was purchased under those 337 contracts. In addition, DESC employed 19 personnel to manage into-plane contracts at an estimated \$1 million in annual operating expenses.

AIR Card Contract. In January 1997, DESC awarded the first AIR card contract to Kropp Holdings, Inc., a commercial credit card processing company. The AIR card was developed to improve local purchase procedures by providing visibility over fuel and ground handling services purchased at FBOs not having into-plane contracts and affording DoD lower than commercial fuel prices through contractor discounts. From May 1, 1997, through April 30, 1998, the AIR card contractor processed over 13,000 transactions for over 5.7 million gallons of fuel, valued at about \$10.5 million. Eventually, DESC plans to use the AIR card for all purchases of fuel and ground handling services, including procurements at FBOs with into-plane contracts. Future procedures will enable pilots to use the AIR card in place of the aircraft identa-plate² to purchase fuel at into-plane contract prices. Those procedures will be implemented as soon as an automated link between DESC and the Defense Finance and Accounting Service is implemented. See Appendix B for additional information on the AIR card.

¹Additives consist of fuel system icing inhibitor and corrosion inhibitors.

²The identa-plate is an aircraft identification card (DD Form 1896 for jet fuel and DD Form 1897 for aviation gasoline).

Local Purchase Procedures. Local purchase procedures are used for procuring fuel and ground handling services at airports where DESC did not establish into-plane contracts and FBOs do not accept the AIR card. Using local purchase procedures, DoD pilots purchase fuel and ground handling services at commercial prices using either Standard Form 44 "Purchase-Order-Invoice-Voucher" or Air Force Forms 15/315 "United States Air Force Invoice/United States Air Force Avfuels Invoice." Centralized data identifying the purchaser, the quantities purchased, date of transaction, and cost per gallon or service was not available at DESC or the AIR card contractor because they are not involved in the local purchase process. The FBOs send the invoices directly to the home station or base of the pilot making the purchase.

Audit Objectives

This report is the second in a series of reports on DoD management of fuels. This audit was requested by the Assistant Deputy Under Secretary of Defense (Material and Distribution Management). The overall audit objective was to evaluate the management of and processes used to procure, store, and account for fuels to meet U.S. European Command requirements for regional contingencies. The specific objective for this segment of the audit was to determine the most cost-effective acquisition strategy for procuring aviation fuel and to determine whether prices for ground handling services were reasonable at commercial airports. Specifically, the Assistant Deputy Under Secretary of Defense (Material and Distribution Management) had requested that we determine whether cost-effective commercial alternatives existed for into-plane contracting and whether FBOs with into-plane contracts were increasing prices charged for ground handling services to compensate for the lower fuel prices negotiated in into-plane contracts. We also reviewed the management control program as it related to the audit objective.

Inspector General, DoD, Report No. 98-114, "Fuel War Reserves for the European Theater," April 16, 1998, discusses the requirements determination process for fuel war reserves. A subsequent audit will cover implementation of the role specialist nation concept for the supply of fuel to multinational forces in the European theater. See Appendix A for a discussion of the audit scope and methodology and our review of the management control program and for a summary of prior coverage related to the audit objectives.

Finding A. Procuring Fuel at Commercial Airports

The prices in into-plane contracts were generally lower than the prices available through the use of the AIR card and significantly lower than commercial prices at commercial airports. However, the actual cost-effectiveness of into-plane contracts over commercial alternatives could not be determined because DESC had not evaluated the prime vendor strategy for procuring fuel at commercial airports. As a result, DESC cannot be assured that its acquisition strategy used for procuring fuel at commercial airports provides the best value to DoD.

Policy and Contract Provisions

Comptroller Memorandum on Prime Vendor Contracting. An Under Secretary of Defense (Comptroller) memorandum, "Management Reform Memorandum No. 12--Expanding the use of Prime Vendor Contract Instruments," June 17, 1997, discusses the use of prime vendor contracts that permit DoD customers to procure items directly from commercial suppliers, thereby avoiding the cost of building warehouses and maintaining inventories. The memorandum further states that the Defense Logistics Agency had already extended the prime vendor innovation for facilities maintenance and concludes that, although prime vendor contracts are in the prototype stage, the technique has the potential for considerable cost savings to DoD.

AIR Card Contract Provisions. The AIR card contract specifies the responsibilities of the contractor in the processing of DoD purchases using the AIR card. The AIR card contract requires the contractor to provide detailed transaction data to DoD to ensure timely and accurate billings to the Services responsible for the aircraft.³ In addition, the AIR card contract provisions require the contractor to make payments to the FBOs. The contract contains neither provisions requiring the AIR card contractor to sell fuel or ground handling services to DoD nor provisions that discuss the prices DoD would be charged for fuel or ground handling services. Thus, the AIR card contractor could increase the fuel price at any time, up to the FBOs commercial price, and still be in compliance with the terms and conditions of the AIR card contract.

³DoD aircraft include fighters, helicopters, patrol craft, and transports.

Comparing Existing Fuel Purchasing Alternatives

The prices in into-plane contracts were generally lower than the prices available through the use of the AIR card and significantly lower than commercial prices at commercial airports. DoD pilots purchased fuel using into-plane contracts, the AIR card, or local purchase procedures. Into-plane contract fuel prices were adjusted up or down weekly using an independent reference index such as *Platt's Oilgram Price Report*.⁴ AIR card fuel prices are adjusted whenever market prices dictate a change or the FBO notifies the AIR card contractor of an increase or decrease in fuel prices. FBOs adjust commercial fuel prices at any time, based on fuel market conditions.

Fuel Price Comparison. As of October 1, 1997, DESC had a worldwide universe of 507 airports using into-plane contracts. Of the 507 airports, 107 (63 in the continental United States and 44 overseas) had fuel pricing data available to compare the into-plane contract, the AIR card contract, and commercial prices. We compared those prices to determine whether any significant differences existed. For the comparison, we selected airports where at least one FBO had an active into-plane contract, at least one FBO accepted the AIR card, and commercial prices were available. The prices compared were per gallon prices plus taxes and fees in effect during September and October 1997. We used the most favorable AIR card contractor prices, based on volume discounts, that the FBO offered at those locations. See Appendix C for a list of the 107 FBOs and the into-plane, AIR card, and commercial prices in our sample.

Lower Into-Plane Prices. The comparison of into-plane contract, AIR card contract, and commercial fuel prices showed that into-plane contracts provided the lowest price to DoD. The average fuel price at the 107 airports was \$1.10 per gallon for into-plane contracts, \$1.63 for the AIR card contract, and \$1.90 at the commercial price. As a result, the into-plane price averaged \$.53 per gallon less than the AIR card price, and \$.80 per gallon less than the commercial price. In contrast, the AIR card price averaged only \$.27 per gallon less than the commercial price at the 107 FBOs offering discounts. In addition, the into-plane contract advantage over the AIR card contract averaged \$.70 less per gallon in the continental United States, whereas the into-plane contract averaged only \$.27 per gallon less overseas.⁵ Based on our review of into-plane prices; AIR card prices; and commercial prices for fuel, DoD pilots can obtain the lowest prices available when using FBOs having into-plane contracts to purchase fuel.

Commercial Prime Vendors

Although the fuel costs per gallon for into-plane contracts were lower, DESC could not determine the cost-effectiveness of into-plane contracts over all commercial alternatives because DESC had not fully evaluated the costs and benefits of consolidating fuel procurements at commercial airports through one or

⁴*Platt's Oilgram Price Report* is a newsletter published daily by McGraw-Hill providing information on worldwide prices for petroleum products.

⁵Total fuel cost savings are dependent on the volume of fuel purchased at each location.

Finding A. Procuring Fuel at Commercial Airports

more prime vendors. The prime vendor strategy is a concept of support whereby a single distributor serves as the major provider of a product to various Federal and state customers within a geographical region or zone. The Defense Logistics Agency has successfully used prime vendor contracts for other commodities in an attempt to mirror commercial business practices and to eliminate unneeded costs.

Prime Vendor Strategy. The Defense Logistics Agency used the prime vendor strategy to leverage private sector capabilities and streamline acquisition for construction, food and beverage, and medical supplies. For example, regional contracts that provide for payment to a few prime vendors for medical supplies have replaced the use of multiple payments to many medical supply contractors. Benefits of prime vendor contracts include reduced inventory costs, reduced prices, and improved service, with reduced inventory costs cited as the primary benefit. Although the use of prime vendors for procuring fuel at commercial airports would represent a new application of the concept, potential benefits include lower fuel and lower contract administration costs and improved service.

DESC Actions. The DESC had not pursued a prime vendor acquisition strategy for procuring fuel at commercial airports, although a potential prime vendor had submitted a proposal to DESC. In the December 1996 proposal, the contractor would negotiate and manage fuel acquisitions at into-plane contract locations and at commercial airports that did not have into-plane contracts, including AIR card purchases. DESC determined that the unsolicited proposal was actually a late response to the specific solicitation for a Government credit card processor; thus, the proposal could not be considered. Although the contractor submitted the proposal after the solicitation closing date, DESC could have surveyed the commercial market to determine whether the contractor's claims concerning the capabilities of the commercial market were valid. In addition, DESC could have issued a request for information soliciting the cost data needed to compare the contractor costs and DoD costs for managing into-plane contracts and the AIR card program. The proposal received from the potential prime vendor did not include any cost data, and as of May 1998, DESC had not taken any action to evaluate the costs and benefits of pursuing a prime vendor strategy for into-plane contracts for procuring fuel at commercial airports.

Potential Benefits from Prime Vendor Strategy. The DESC could obtain benefits when procuring fuel at commercial airports that were not traditionally associated with the prime vendor strategy. However, DESC did not take action to pursue the prime vendor strategy because DESC officials believed that they had already realized the main benefit obtainable through a prime vendor strategy, reduced inventory costs. DESC further believed that because into-plane contracts did not result in DoD fuel inventories and the contracting officer dealt directly with the commercial supplier, then no further benefits would be obtained by a prime vendor strategy. Although reduced inventory costs are the main benefit cited for past uses of the prime vendor strategy, the basic concept of replacing multiple suppliers with one or several prime vendors could provide the following benefits for future contracts.

- o Contract management costs could be reduced if DESC is responsible for managing at least one prime vendor contract instead of over 300 into-plane contracts.

Finding A. Procuring Fuel at Commercial Airports

- o DoD processing costs could be reduced if only one or more prime vendors were reimbursed for all into-plane transactions.

- o Fuel prices available through prime vendor commercial sources could be lower than into-plane prices because the prime vendors could negotiate with FBOs using the leverage provided by the purchase volume of into-plane contracts plus the leverage already provided by existing agreements between the prime vendor and FBOs.

To determine the feasibility of a prime vendor strategy, DESC should identify potential prime vendors in the commercial sector and evaluate the costs and benefits of using any available sources for procuring fuel at commercial airports. The evaluation should include the costs of DoD management of into-plane and AIR card contracts versus the cost of managing one or more prime vendor contracts. The evaluation would also need to include the benefits, if any, that could result from using commercial sources with the additional negotiating leverage provided by DoD purchase volume. Finally, the evaluation would need to include any quality and safety risks that using a prime vendor strategy could pose.

Potential Prime Vendors. Because DESC had not obtained potential prime vendor cost and pricing data, we could not determine the cost and benefits of using a prime vendor for procuring fuel at commercial airports. However, we did identify existing commercial sources that perform functions similar to those that a prime vendor might perform. To identify potential prime vendors, we surveyed four commercial aviation credit card companies or fuel suppliers to determine the services they provide to their corporate or general aviation customers. The four companies contacted were Multi-Service Corporation, British Petroleum, Universal Air, and Air Routing International. Each company had established agreements with FBOs to provide fuel to their customers at discounted or commercial prices. Officials from the four companies stated that they had agreements with from 600 to 3,800 locations worldwide and that commercial airlines, major corporations, and thousands of general aviation pilots used one or more of the companies to obtain fuel at commercial airports. The companies also stated that they will occasionally establish agreements, of varying lengths, at specific locations on behalf of customers. Two of the four companies guaranteed fuel quality or included fuel quality in agreements with FBOs. One company official also stated that the company occasionally performed or coordinated fuel quality reviews.

Additional Information Needed for Ensuring Best Value

Further information and additional analysis are needed to fully analyze the feasibility, costs, and benefits of using commercial companies as a prime vendor. We were able to obtain general information from the commercial companies we contacted, but were limited to the specific information we could obtain concerning their capabilities and costs. Only the DESC contracting officers can issue requests for information asking commercial companies to demonstrate their ability to provide fixed-based operator support at commercial airports and to provide cost estimates. On June 2, 1998, we agreed to work with DESC to analyze the feasibility of using the prime vendor strategy for providing fixed-base operator support at commercial airports. Specifically, we would work together to

Finding A. Procuring Fuel at Commercial Airports

determine whether a prime vendor market exists that would respond to a solicitation for FBO support at commercial airports; the costs involved; and whether DoD could realize potential monetary benefits. Without obtaining and evaluating information concerning prime vendors, DESC cannot be assured that the acquisition strategy used for procuring fuel at commercial airports provides the best value to DoD.

Recommendations and Management Comments

A. We recommend that the Commander, Defense Energy Support Center:

1. Issue a request for information to potential prime vendors to identify their ability to provide fixed-base operator support at commercial airports.

2. Determine the feasibility of using the prime vendor strategy for providing fixed-base operator support at commercial airports.

Management Comments. The Defense Energy Support Center concurred with the recommendations, stating that all actions will be completed by September 30, 1998.

Finding B. Procuring Ground Handling Services

Based on our review of the 30 FBOs, we found no evidence that FBOs increased prices for ground handling services as a means to compensate for lower fuel prices negotiated under into-plane contracts. Although the 30 FBOs contacted had different methodologies for determining prices for ground handling services, those methodologies did not result in price increases to DoD.

Ground Handling Services

Types of Ground Handling Services. Ground handling services are the care and servicing of an aircraft and its crew that FBOs provide at commercial airports. In addition, FBOs collect fees and taxes that an airport authority assesses when an aircraft lands. Ground handling services include baggage handling, deicing, engine starts, general handling, hangar rental, lavatory servicing, and parking. Fees and taxes include airport fees, airport head tax, departure tax, Drug Enforcement Administration fees, immigration fees, landing fees, and sales tax. Not all ground handling services are required and not all fees and taxes are applicable each time an aircraft lands at a commercial airport. Also, an FBO, at its discretion, can choose to provide ground handling services for DoD aircraft and crew even when fuel is not purchased.

Guidance for Ground Handling Services. Ground handling services are not procured under contracts because contracts are not required for purchases of \$2,500 or less. The Services procure ground handling services with either the AIR card or local purchase procedures. DoD had not issued guidance for using the AIR card to procure ground handling services because DESC did not approve the AIR card for DoD-wide use until October 1997. In addition, DoD had not issued specific guidance for procuring ground handling services; however, the Federal Acquisition Regulation contains guidance on local purchase procedures, which the Army and Navy used when procuring ground handling services. The Federal Acquisition Regulation states that local purchase procedures can be used for on-the-spot, over-the-counter purchases of supplies and nonpersonal services (such as ground handling services) of \$2,500 or less. In contrast to the Army and the Navy, the Air Force issued Air Force Instruction 23-202, "Buying Petroleum Products, and Other Supplies and Services Off-Station," July 19, 1994, which states that the Air Force is authorized to procure ground handling services using local purchase procedures when an official mission or trip is made to an area where Air Force, other DoD, or contract services are not available.

Pricing of Ground Handling Services

Based on our review of the 30 FBOs, the FBOs did not increase prices for ground handling services to compensate for low fuel prices negotiated under into-plane contracts. Although the 30 FBOs contacted had different methodologies for determining prices for ground handling services, those methodologies did not result in price increases to DoD.

Review of FBOs with Into-Plane Contracts. As of October 1, 1997, DESC had 308 into-plane contracts in the continental United States. We judgmentally contacted 30 (10 percent) FBOs that had into-plane contracts in FY 1997 to determine the rationale they used to price ground handling services. In FY 1997, 10,663 aircraft landed at those 30 FBOs and procured over 13.5 million gallons of fuel using into-plane contracts. However, we were unable to determine the volume or costs of ground handling services procured from those 30 FBOs because the Services did not maintain a data base for accumulating ground handling service expenditures.

Methodology for Determining Prices for Ground Handling Services. Each of the 30 FBOs contacted had developed its own unique pricing structure for ground handling services. Some of the variables that the 30 FBOs considered when determining prices for ground handling services consisted of size of the aircraft, whether fuel was purchased and the number of gallons, whether the pilot was a regular customer, and the number of services provided. In addition, the FBOs considered the length of time the aircraft stayed at the FBO, whether equipment had to be rented from a major airline or another FBO, fees and taxes set by the airport authority, and the prices of their competitors. Of the 30 FBOs contacted:

- o 12 did not charge DoD pilots for any ground handling services;
- o 7 always charged DoD pilots for ground handling services at the commercial prices;
- o 5 would either reduce or waive charges for ground handling services if DoD pilots procured fuel at the same time the ground services were provided, regardless of the method DoD pilots used to procure the fuel;
- o 5 sometimes reduced or waived ground handling service charges for DoD pilots regardless of whether fuel was procured; and
- o 1 charged DoD a flat rate regardless of the number of ground handling services provided.

Finding B. Procuring Ground Handling Services

Prices Charged DoD and Commercial Customers. The DoD pilots paid prices for ground handling services that were either the same or less than the prices that FBOs charged commercial customers. In addition, procuring ground handling services from FBOs with into-plane contracts did not result in higher costs to DoD. For the 18 FBOs that sometimes or always charged DoD pilots for ground handling services, there was a wide range of prices for those services. For example, Mercury Air Center Los Angeles charged from \$94 to \$380 for use of its ramp parking area, based on the size of the aircraft, and separately priced all other services that it provided. Its prices for ground handling services were not based on whether the DoD pilot used an into-plane contract to procure fuel. In contrast, Bangor International Airport charged DoD a flat \$215 handling fee regardless of the size of the aircraft, which covered all ground handling services including clearing customs, deicing, engine starts, and lavatory servicing. Personnel at Bangor Airport stated that a commercial customer would be charged from \$500 to \$2,000 for ground handling services, based on the aircraft size and the services needed. Overall, the 18 FBOs did not charge DoD pilots prices for ground handling services that exceeded prices charged to commercial customers and often charged DoD pilots less than commercial customers.

Based on the results of our review, we concluded that FBOs were not increasing prices for ground handling services to compensate for low fuel prices negotiated under into-plane contracts. It was standard business practice for the 30 FBOs to either waive charges for ground handling services provided to DoD pilots or to charge prices that were lower than or equivalent to prices that those FBOs charged their commercial customers. In addition, no relationship existed between fuel prices negotiated under into-plane contracts and prices charged for ground handling services. As a result, we are not making any recommendations on ground handling services in this report.

Part II - Additional Information

Appendix A. Audit Process

Scope and Methodology

We reviewed DoD policies on local purchase procedures, DESC policies and procedures for managing the into-plane contracts and DESC methodology for soliciting and awarding the contract for the AIR card. In addition, we reviewed DESC frequency reports for FYs 1996 and 1997 that summarized the volume of fuel purchased under into-plane contracts, transactions processed by the AIR card contractor from May 1, 1997, through April 30, 1998, and FY 1998 documentation from FBOs on pricing ground handling services.

To determine whether prices charged for fuel under into-plane contracts were lower than prices the AIR card contractor and FBOs charged, we compared into-plane contract prices with the prices available through a commercial discount fuel program that the AIR card contractor operated and the commercial prices FBOs set. To determine whether DESC had evaluated the prime vendor concept, we identified the missions and functions integral to the into-plane program, examined DoD policy and practices on the use of the prime vendor strategy, and contacted four private sector companies in the aviation fuel business to obtain information on the services they typically provide to their customers. To determine whether FBOs were increasing prices for ground handling services they provided to DoD to compensate for low fuel prices negotiated under into-plane contracts, we contacted 30 of the 308 FBOs that had into-plane contracts in FY 1997 and obtained pricing information and discussed the variables affecting the pricing of ground handling services for commercial and DoD aircraft.

DoD-wide Corporate Level Goals. In response to the Government Performance and Results Act, DoD established 6 DoD-wide corporate level performance objectives and 14 goals for meeting those objectives. This report pertains to the achievement of the performance objective to fundamentally reengineer DoD and to achieve a 21st century infrastructure. The goal of that objective is to reduce costs while maintaining required military capabilities across all DoD mission areas. (DoD-6)

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

Use of Computer-Processed Data. We relied on computer-processed data from the DESC Defense Fuels Automated Management System and the Accounting System of the AIR card contractor. We did not test general and application controls to confirm the reliability of the systems because we only relied on the information to determine the magnitude of into-plane contracts and purchases made with the AIR card and to compare prices for fuel. Not testing the controls did not affect the results of the audit.

Audit Type, Dates, and Standards. This economy and efficiency audit was conducted from February through May 1998. The audit was conducted in accordance with auditing standards issued by the Comptroller General of the United States, and accordingly, included such tests of management controls as were considered necessary.

Contacts During the Audit. We visited or contacted individuals and organizations within DoD, commercial contractors, and commercial trade organizations. Further details are available upon 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 Controls. We reviewed the adequacy of management controls over the into-plane contracting process. We did not review the Services' management controls over procuring ground handling services because we did not identify any problems at the FBOs. We did not assess the adequacy of management's self-evaluation because we did not identify a material weakness.

Adequacy of Management Controls. The DESC management controls over into-plane contracts were adequate. We identified no material management control weaknesses in those areas reviewed.

Summary of Prior Coverage

General Accounting Office Report No. GAO/NSIAD-96-188 (OSD Case No. 1189), "Information on Selected Aspects of DoD's Jet Fuel Programs," July 31, 1996.

Appendix B. Additional Background Information on the AIR Card

The Government AIR card is a commercially accepted credit card that DoD uses to purchase fuel, fuel related supplies, and ground handling services at commercial airports. Kropp Holdings, Inc. (the contractor), is the credit card processor under contract for the AIR card. The AIR card is used in place of local purchase procedures and provides fuel discounts from the commercial price. When the AIR card is used, the AIR card contractor pays the FBO and DoD reimburses the AIR card contractor. DESC is responsible for negotiating and managing the AIR card contract and for implementing any future changes to transaction processing procedures.

Background. The AIR card initially was developed by the Air Force in 1994, as a replacement for Air Force local purchases. In a December 23, 1994, memorandum, the Air Force notified the Defense Logistics Agency that the credit card the Air Force was using provided an improved accounting and payment process as well as other favorable advantages, including access to lower fuel prices from discounts available only to card holders; greater acceptability by foreign vendors; and better visibility of flying hour costs. In addition, the Air Force offered its assistance to the Defense Logistics Agency in implementing a similar aviation fuel credit card for use throughout DoD. DESC reviewed the Air Force credit card process and initiated procurement procedures to implement the AIR card concept. It issued a solicitation for the Government AIR card contract in October 1996.

Issuance of Credit Card. On January 23, 1997, DESC awarded an AIR card contract to Kropp Holdings, Inc., for an 8-month test period, ending September 30, 1997, with 2 succeeding option years. During the test period, the contractor was responsible for issuing credit cards to participating military units, providing computer systems training, and processing AIR card transactions. On September 29, 1997, DESC exercised option year 1 that extended the contract period to September 30, 1998. Option year 1 called for expanding the AIR card use to all DoD organizations and interfacing with the DESC Fuels Automated System for purchases and invoicing of other than into-plane transactions. In addition, option year 2 of the contract, due to be exercised October 1, 1998, would provide credit cards to all Federal civilian agencies while providing the same transaction processing services as prior years. During the contract test period, the contractor issued approximately 500 AIR cards to selected military units to be used for purchasing ground handling services and fuel at noninto-plane FBOs. The number of AIR cards distributed throughout DoD increased to 15,000 during option year 1. The number of credit cards issued will increase substantially to accommodate all Federal civilian agencies under option year 2.

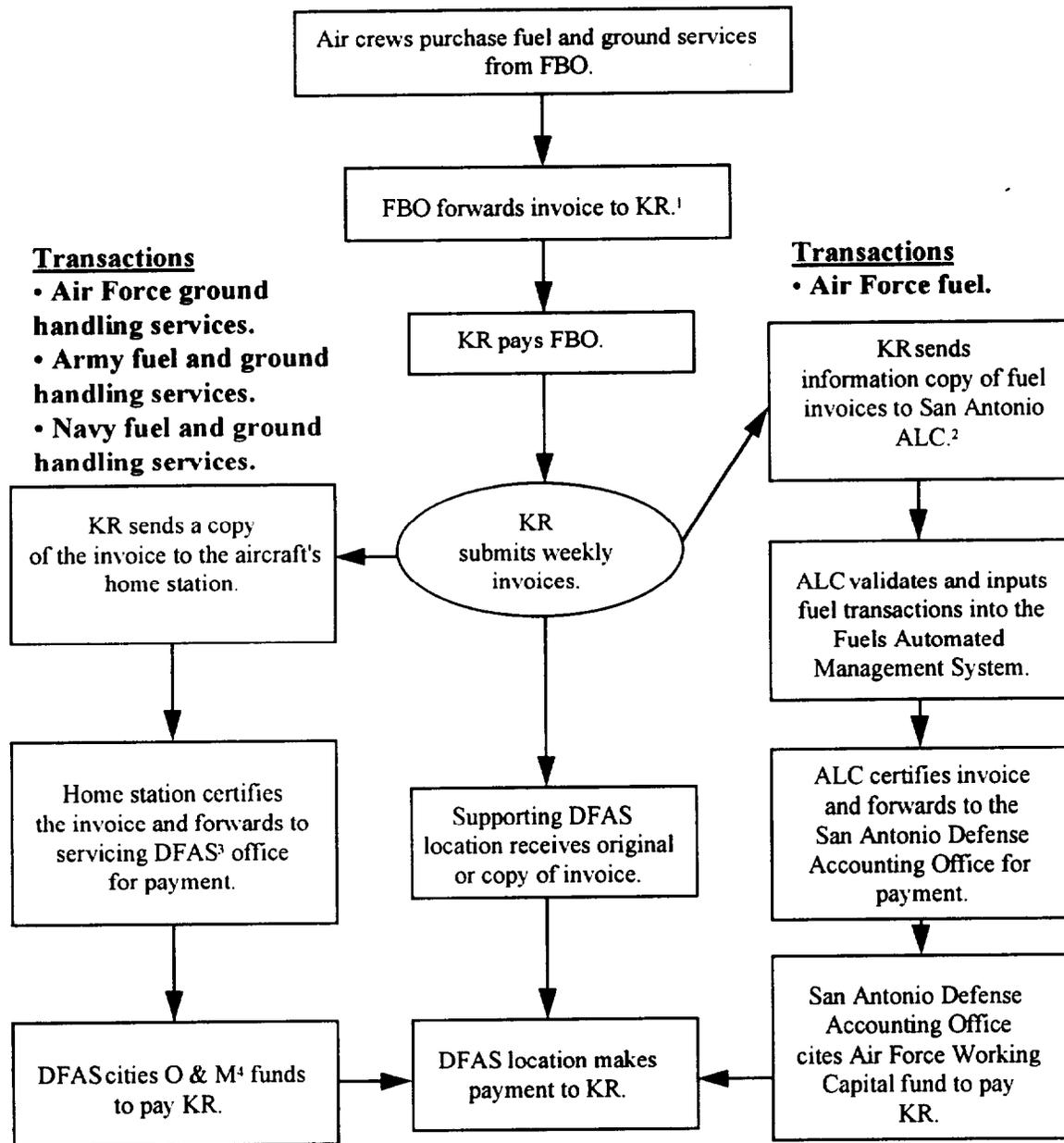
Appendix B. Additional Background Information on the Air Card

Contractor Transactions Using the AIR Card. The contractor uses two types of transactions for the purchase of fuel and ground handling services. The first is a typical credit card transaction whereby the FBO pays the contractor a processing fee of between 1.5 percent and 4 percent for accepting the credit card. In return, the FBO receives payment from the contractor within an agreed-upon period, usually 7 to 10 days. Those credit card transactions apply to fuel and ground handling services. The second type of transaction is a resale fuel transaction in which the contractor purchases fuel from an FBO, a fuel wholesaler, or the commodities market and resells it at a profit to its customers, including DoD, for a price known as the "OASIS discount." For those transactions, the AIR card serves as an identification card informing the vendor that the holder of the card is eligible for the OASIS discount. The resale transaction does not require the FBO to pay the contractor the processing fee and does not guarantee faster payments to the FBO.

Payment Processes. The payment processes for the AIR card vary according to whether fuel or ground handling services are purchased and which Service is involved. DoD pilots or a member of their crew present the AIR card to the FBO that provides the fuel or ground handling services. The FBO submits the purchase invoices to the contractor by electronic transmission, facsimile, or mail. The contractor pays the FBO according to the conditions agreed upon by the contractor and the FBO. Once a week, the contractor invoices the Services' home stations or fuel offices, depending on payment procedures and whether fuel or ground services are purchased. The Defense Finance and Accounting Service reimburses the contractor citing the Services' Working Capital fund or Operation and Maintenance fund.

The AIR card has met the initial intended purposes of the program. As implemented, the AIR card has replaced local purchase methods at those FBOs accepting the AIR card and provides greater visibility over purchases at those locations. The following figure shows the billing and payment procedures for each Service.

Appendix B. Additional Background Information on the AIR Card



Transactions

- Air Force ground handling services.
- Army fuel and ground handling services.
- Navy fuel and ground handling services.

Transactions

- Air Force fuel.

¹ KR Contractor.
² ALC Air Logistics Command.
³ DFAS Defense Finance and Accounting Service.
⁴ O & M Operation and Maintenance.

AIR Card Billing and Payment Process at Noninto-Plane Locations

Appendix C. Details on Fuel Price Comparison

We compared prices at airports to determine whether fuel prices negotiated under into-plane contracts were more economical than prices offered through the AIR card contractor and commercial prices set by FBOs. We selected the airports for our comparison from the universe of 507 airports around the world, at which DESC had established into-plane contracts as of October 1, 1997.

Methodology for Selecting Airports for Review. From the universe of 507 airports, we selected airports for review if:

- o we could obtain the into-plane price, the AIR card price, and the commercial price in effect during September and October 1997;
- o at least one FBO had an active into-plane contract; and
- o at least one FBO accepted the AIR card.

Of the 507 airports, only 107 airports met all three criteria, 63 in the continental United States and 44 overseas. We performed a price comparison at all 107 airports.

Adjustments to Fuel Per Gallon Price. To standardize the per gallon fuel prices, we included fees and taxes in our comparison of the into-plane price, AIR card price, and commercial price. Fees and taxes include airport fees, airport tax, customs supervision fee, Federal excise tax, hydrant fee, and value added tax. We included fees and taxes in the per gallon price although DoD may be exempt from paying fees and taxes at certain airports or may be eligible for a refund of taxes paid. In addition, we adjusted the data obtained from the AIR card contractor for airports outside the continental United States to include fees and taxes equivalent to those charged for into-plane sales at the same location and assumed that any volume discounts available were taken.

Tables C-1 and C-2 show the price comparison for fuel at the 107 airports. The into-plane prices at 33 of the 63 airports in the continental United States include the cost for a fuel additive that inhibits icing. The price for fuel with the additive is slightly higher than the price for fuel without the additive.

Appendix C. Details on Fuel Price Comparison

Table C-1. Fuel Prices at Airports in the Continental United States

<u>Airport Name, City, State or Country</u>	<u>Into-Plane Price</u>	<u>AIR Card Price</u>	<u>Commercial Price</u>
Abilene Regional Airport, Abilene, Texas	\$1.38	\$1.87	\$2.12
Adams Field, Little Rock, Arkansas	0.82	1.34	1.69
Akron Canton Regional Airport, Canton, Ohio	1.26	1.99	2.09
Albuquerque International Airport, Albuquerque, New Mexico	1.11	1.64	1.84
Alexandria International Airport, Alexandria, Louisiana	1.00	1.78	1.98
Bangor International Airport, Bangor, Maine	1.18	1.53	1.92
Billings/Logan International Airport, Billings, Montana	1.28	1.91	2.15
Boeing Field/King County, Seattle, Washington	0.94	1.93	2.38
Boise Air Terminal, Boise, Idaho	1.11	1.78	2.18
Brown Field Municipal Airport, San Diego, California	1.41	1.90	2.20
Brownsville South Padre Island International Airport, South Padre, Texas	1.01	2.00	2.15
Burke Lake Front Airport, Cleveland, Ohio	1.14	2.10	2.30
Capital City Airport, Lansing, Michigan	1.36	2.11	2.31
Carl Spaatz Field, Reading Regional Airport, Reading, Pennsylvania	1.24	1.92	2.22
Central Nebraska Regional Airport, Grand Island, Nebraska	1.21	1.55	1.85
Columbia Municipal Airport, W. Columbia, South Carolina	1.07	1.58	1.63
Dallas Love Field, Dallas, Texas	0.93	2.16	2.26
Daugherty Field, Long Beach, California	1.01	1.70	2.27
DeKalb-Peach-Tree Airport, Atlanta, Georgia	1.15	1.99	2.24
Easton Municipal Airport, Easton, Maryland	1.44	1.63	1.69
El Paso International Airport, El Paso, Texas	1.26	2.01	2.17
Falcon Field, Mesa, Arizona	1.26	1.94	2.36
Ft. Lauderdale Hollywood International Airport, Fort Lauderdale, Florida	0.95	1.54	2.24
Garden City Regional Airport, Garden City, Kansas	1.26	1.70	1.95
Grand Strand Airport, N. Myrtle Beach, South Carolina	1.19	1.62	1.92
Great Falls International Airport, Great Falls, Montana	1.52	1.85	2.15
Greater Rockford Airport, Rockford, Illinois	1.16	1.48	2.28
Hancock International Airport, Syracuse, New York	0.98	1.84	2.14
Hector Field, Fargo, North Dakota	1.32	1.56	2.00
Helena Regional Airport, Helena, Montana	1.24	1.70	2.10
Houston International Airport, Houston, Texas	1.13	1.85	2.10
Hulman Field, Terre Haute, Indiana	1.44	2.06	2.31
L.G. Hanscom Field, Bedford, Massachusetts	1.08	2.01	2.29
Lakefront Airport, New Orleans, Louisiana	1.06	2.23	2.33

*Into-plane price includes fuel system icing inhibitor.

Appendix C. Details on Fuel Price Comparison

<u>Airport Name, City, State or Country</u>	<u>Into-Plane Price</u>	<u>AIR Card Price</u>	<u>Commercial Price</u>
Laredo International Airport, Laredo, Texas*	1.19	1.80	1.90
Lea County Airport Hobbs Service, Hobbs, New Mexico	1.25	1.95	2.05
Lincoln Municipal Airport, Lincoln, Nebraska*	1.21	1.35	1.65
Lubbock International Airport, Lubbock, Texas*	1.27	1.87	2.12
Manassas Regional Airport, Manassas, Virginia	0.95	1.99	2.09
McCarron International Airport, Las Vegas, Nevada	1.32	1.91	2.19
Miami International Airport, Miami, Florida	1.31	2.03	2.19
Missoula International Airport, Missoula, Montana	1.25	1.86	1.99
Mobile Downtown Airport, Mobile, Alabama	1.01	1.67	2.07
Monroe Regional Airport, Monroe, Louisiana*	1.24	1.88	2.20
Natrona International Airport, Casper, Wyoming	1.40	1.94	2.04
New Hanover International Airport, Wilmington, North Carolina	0.93	2.05	2.18
New Orleans International Airport, New Orleans, Louisiana	0.76	2.31	2.45
Panama City/Bay County Airport, Panama City, Florida	0.99	2.15	2.24
Portland International Jetport, Portland, Maine	0.95	1.94	2.07
Reynolds Field, Jackson Co. Airport, Jackson, Michigan*	1.43	1.70	1.85
Richmond International Airport, Richmond, Virginia	0.87	2.03	2.13
Salt Lake City International Airport, Salt Lake City, Utah	1.22	2.17	2.27
San Antonio International Airport, San Antonio, Texas*	1.08	2.16	2.30
Santa Maria Public Airport, Santa Maria, California*	1.34	1.45	1.70
Sarasota-Bradenton Airport, Sarasota, Florida*	1.28	1.89	1.99
Sky Harbor International Airport, Phoenix, Arizona*	0.85	1.59	1.69
St. Louis Regional Airport, Alton, Illinois*	1.11	1.85	2.10
Stockton Metro Airport, Stockton, California	0.95	1.65	2.25
Van Nuys Airport, Van Nuys, California	1.04	1.79	1.99
W.K. Kellogg Regional Airport, Battle Creek, Michigan*	1.00	1.72	1.90
Walker Field, Grand Junction, Colorado	1.45	1.90	2.00
Wichita Mid-Continental Airport, Wichita, Kansas	1.15	2.17	2.27
Yakima Air Terminal, Yakima, Washington	<u>0.93</u>	<u>2.26</u>	<u>2.36</u>
Average Fuel Prices	\$1.15	\$1.85	\$2.10

*Into-plane price includes fuel system icing inhibitor.

Appendix C. Details on Fuel Price Comparison

Table C-2. Fuel Prices at Airports in Alaska and Overseas

<u>Airport Name, City, State or Country</u>	<u>Into-Plane Price</u>	<u>AIR Card Price</u>	<u>Commercial Price</u>
Alice Springs, Northeastern Territory, Australia	\$1.14	\$1.91	\$2.09
Anchorage International Airport, Anchorage, Alaska	1.07	1.74	2.04
Antalya International Airport, Antalya, Turkey	0.65	0.87	1.26
Ataturk International Airport, Istanbul, Turkey	0.66	0.85	1.15
Bahrain International Airport, Maharraq, Bahrain	0.76	1.00	1.23
Bangkok International Airport, Bangkok, Thailand	0.71	0.91	1.13
Bermuda International Airport, Saint Georges, Bermuda	1.12	1.49	1.59
Brussels National Airport, Brussels, Belgium	0.70	0.93	1.78
Cairo International Airport, Cairo, Egypt	0.71	0.84	1.01
Cyril E King International Airport, St. Thomas, Virgin Islands	1.23	1.44	1.60
Dakar/Yoff International Airport, Dakar, Senegal	0.82	0.96	1.16
Dalaman Field, Dalaman, Turkey	0.68	0.86	1.35
Dhahran International Airport, Dhahran, Saudi Arabia	0.77	0.97	1.47
Djibouti International Airport, Ambouli, Djibouti	1.02	1.23	1.40
El Salvador International Airport, San Salvador, El Salvador	0.98	1.37	1.72
El Trompillo Airport, Santa Cruz, Bolivia	1.50	2.02	2.02
Entebbe International Airport, Entebbe, Uganda	1.21	1.70	1.98
Ezeiza Buenos Aires, Buenos Aires, Argentina	1.04	1.16	1.23
Faro International Airport, Faro, Portugal	0.69	1.10	1.37
Freetown International Airport, Freetown, Sierra Leone	1.39	1.56	2.32
Gardermoen International Airport, Oslo, Norway	0.75	0.89	1.52
Harare International Airport, Harare, Zimbabwe	0.98	1.01	1.01
Johan Pengel International Airport, Paramaribo, Suriname	0.98	1.24	1.68
Jorge Arauz Airport, Trinidad, Bolivia	1.50	1.91	2.02
King Khalid International Airport, Riyadh, Saudi Arabia	0.86	0.97	1.39
Larnaca International Airport, Larnaca, Cyprus	0.74	0.94	1.40
Leon' M ba International Airport, Libreville, Gabon	0.86	0.93	1.06
Murtala Mhamd International Airport, Lagos, Nigeria	0.86	1.50	1.50
Nassau International Airport, Nassau, Bahamas	1.10	1.69	1.79
Niamey International Airport, Niamey, Niger	1.59	1.66	2.16
Nouakchott International Airport, Nouakchott, Mauritania	1.36	1.56	1.82
Nsimalen International Airport, Yaounde, Cameroon	1.67	1.98	2.18
Orly International Airport, Paris, France	0.70	0.82	1.76
Port Au Prince International Airport, Port Au Prince, Haiti	1.57	1.71	2.20
Prague International Airport, Prague, Czech Republic	0.90	1.28	1.40
Rhine Main International Airport, Frankfurt, Germany	0.66	0.93	1.40
Seeb International Airport, Muscat, Oman	1.44	0.98	1.57
Silvia Pettrosi International Airport, Asuncion, Paraguay	1.55	1.40	1.90
Sir Segosagr Rmgolm, Mahebourg, Mauritius	0.81	1.09	1.34
Stuttgart International Airport, Echterdingen, Germany	0.94	1.72	1.88

Appendix C. Details on Fuel Price Comparison

<u>Airport Name, City, State or Country</u>	<u>Into-Plane Price</u>	<u>AIR Card Price</u>	<u>Commercial Price</u>
Taif International Airport, Taif, Saudi Arabia	1.27	1.70	2.05
Thessalonika International Airport, Thessalonika, Greece	0.74	1.12	1.28
ViruViru International Airport, Santa Cruz, Bolivia	1.50	2.02	2.02
Wien Schwechat, Vienna, Austria	<u>0.93</u>	<u>1.23</u>	<u>1.77</u>
Average Fuel Prices	\$1.03	\$1.30	\$1.61
Average Worldwide Fuel Prices	\$1.10	\$1.63	\$1.90

Appendix D. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition and Technology
Deputy Under Secretary of Defense (Acquisition Reform)
Deputy Under Secretary of Defense (Logistics)
Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management)
Director, Defense Logistics Studies Information Exchange
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Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
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House Committee on Appropriations
House Subcommittee on National Security, Committee on Appropriations
House Committee on Government Reform and Oversight
House Subcommittee on Government Management, Information, and Technology,
Committee on Government Reform and Oversight
House Subcommittee on National Security, International Affairs, and Criminal
Justice, Committee on Government Reform and Oversight
House Committee on National Security

Part III - Management Comments

Defense Energy Support Center Comments



DEFENSE LOGISTICS AGENCY
HEADQUARTERS
8725 JOHN J. KINGMAN ROAD, SUITE 2533
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IN REPLY
REFER TO

21 JUL 1998

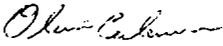
DDAI

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING,
DEPARTMENT OF DEFENSE

SUBJECT: Procuring Fuel and Ground Handling Services at Commercial Airports,
7LG-5030.01

Enclosed are our comments to your request of 12 June 1998. Should you have any questions,
please notify Annell Williams, 767-6274.

Encl

F.R. 
JEFFREY GOLDSTEIN
Chief (Acting), Internal Review Office

cc:
DLSC-BO
DESC-P
DESC-DI

Subject: Procuring Fuel and Ground Handling Services at Commercial Airports

Finding A: The prices in into-plane contracts were generally lower than the prices available through the use of the AIR card and significantly lower than commercial prices at commercial airports. However, the actual cost-effectiveness of into-plane contracts over commercial alternatives could not be determined because DESC had not evaluated the prime vendor strategy for procuring fuel at commercial airports. As a result, DESC cannot be assured that its acquisition strategy used for procuring fuel at commercial airports provides the best value to DoD.

DLA Comments: Concur. We agree that further information and additional analysis are needed to fully analyze the feasibility, costs and benefits of using commercial companies as prime vendors.

Finding B: Based on our review of the 30 FBOs, we found no evidence that FBOs increased prices for ground handling services as a means to compensate for lower fuel prices negotiated under into-plane contracts. Although the 30 FBOs contacted had different methodologies for determining prices for ground handling services, those methodologies did not result in price increases to DoD.

DLA Comments: Concur.

Recommendations:

DoD IG recommends that the Commander, Defense Energy Support Center:

1. Issue a request for information to potential prime vendors to identify their ability to provide fixed-base operator support at commercial airports.
2. Determine the feasibility of using the prime vendor strategy for providing fixed-base operator support at commercial airports.

DLA Comments: Concur.

Disposition: Action is ongoing. ECD for Recommendation 1 - July 31, 1998
ECD for Recommendation 2 - September 30, 1998

Action Officer: Shelby J. Yeakley, DESC-P, (703) 767-8501

Review: Richard R. Sninsky, DESC-DI, (703) 767-9671

Approval: David P. Keller, RADM, SC, USN, Commander, DI.SC

Coordination: Annel W. Williams, DDAI

DLA Approval:



JUL 20 1998

Audit Team Members

This report was prepared by the Readiness and Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, DoD.

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