



DEPARTMENT OF THE NAVY
OFFICE OF THE ASSISTANT SECRETARY
(RESEARCH, DEVELOPMENT AND ACQUISITION)
1000 NAVY PENTAGON
WASHINGTON DC 20350-1000

SEP 28 2010

MEMORANDUM FOR DISTRIBUTION

SUBJECT: DoDIG Contracting Action Areas of Concern, "Purchases Made With Earmarks (Project No. D2008-D000CF-0013.000)"

The attached Director, Defense Procurement and Acquisition Policy (DPAP) memorandum of August 10, 2010 is forwarded for your information and action, as appropriate. It follows an audit by the DoD Office of Inspector General (DoDIG) of contracts awarded using earmarked funds for fiscal year 2005. DoDIG reported issues related to market research, competition, and fair and reasonable price determinations. DPAP reminds the DoD acquisition community that contract actions associated with earmarks require special attention, and recommends consultation with counsel on all statutory earmarks.

Please ensure this guidance is provided to all appropriate contracting and acquisition personnel. Please also review your processes to ensure you avoid the kinds of deficiencies found by DODIG. My point of contact is Mr. Clarence Belton, clarence.belton@navy.mil, 703-693-4006.

A handwritten signature in black ink, appearing to read "Bruce A. Sharp".

Bruce A. Sharp
Director, Program Analysis and
Business Transformation
Deputy Assistant Secretary of the Navy
(Acquisition & Logistics Management)

Attachment:
As stated

Distribution:
See next page

SUBJECT: DoDIG Contracting Action Areas of Concern, "Purchases Made With Earmarks (Project No. D2008-D000CF-0013.000)"

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ACQUISITION,
TECHNOLOGY
AND LOGISTICS

OFFICE OF THE UNDER SECRETARY OF DEFENSE
3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000

AUG 10 2010

MEMORANDUM FOR COMMANDER, UNITED STATES SPECIAL OPERATIONS
COMMAND (ATTN: ACQUISITION EXECUTIVE)
COMMANDER, UNITED STATES TRANSPORTATION
COMMAND (ATTN: ACQUISITION EXECUTIVE)
DEPUTY ASSISTANT SECRETARY OF THE ARMY
(PROCUREMENT)
DEPUTY ASSISTANT SECRETARY OF THE NAVY
(ACQUISITION & LOGISTICS MANAGEMENT)
DEPUTY ASSISTANT SECRETARY OF THE AIR FORCE
(CONTRACTING)
DIRECTORS, DEFENSE AGENCIES
DIRECTORS, DOD FIELD ACTIVITIES

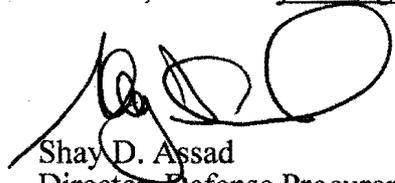
SUBJECT: DoDIG Contracting Action Areas of Concern, "Purchases Made With
Earmarks (Project No. D2008-DOOOCF-0013.000)"

The DoDIG conducted an audit to determine whether DoD activities awarded contracts using funds earmarked in the FY 2005 DoD budget in accordance with the Federal Acquisition Regulation (FAR) and DoD procurement regulations. By the memorandum of June 30, 2010 (attached), the DoDIG requested OUSD(AT&L) to issue its own memorandum emphasizing specified areas of concern.

The DoDIG reviewed 26 contract actions and identified 8 as having concerns relating to market research, competition, and fair and reasonable price determinations. I want to emphasize that contract actions associated with earmarks, unless otherwise noted in supplemental guidance, must comply with the FAR, DFARS, and in the case of all statutory earmarks, you should consult with legal counsel concerning what actions are required. In addition, DoD Components must comply with the memorandum dated June 7, 2010, signed by the USD(AT&L) and USD(C) concerning competition requirements under section 8121 of the FY2010 Appropriations Act.

I would ask that you review the attached audit report and ensure that individual and organizational procurement procedures relating to earmark contract awards are consistent with governing law and regulation.

Please contact Mr. Jeff Grover, 703-697-9352, or email jeffrey.grover@osd.mil if additional information is required.


Shay D. Assad
Director, Defense Procurement
and Acquisition Policy

Attachment:
As stated



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

June 30, 2010

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION,
TECHNOLOGY, AND LOGISTICS
UNDER SECRETARY OF DEFENSE
(COMPTROLLER)/CHIEF FINANCIAL OFFICER
ASSISTANT SECRETARY OF THE AIR FORCE
(FINANCIAL MANAGEMENT AND COMPTROLLER)

SUBJECT: Purchases Made With Earmarks (Project No. D2008-D000CF-0013.000)

We are providing this memorandum for information and use. We announced the subject audit in October 2007. Our audit objective was to determine whether DOD activities awarded contracts using funds earmarked in the FY 2005 DOD budget in accordance with the Federal Acquisition Regulation (FAR) and DOD procurement regulations. We do not require comments on this memorandum.

Background

We conducted this audit because of the national attention and high visibility of congressional earmarks. The Office of Management and Budget (OMB) defines an earmark as unrequested funding in an appropriation act in which Congress 1) circumvents a merit-based or competitive allocation process, 2) specifies the location or recipient, or 3) otherwise curtails the ability of the Government to control critical aspects of the fund's allocation. A congressional earmark is a provision of law, a directive, or a report accompanying a bill that specifies the identity of an entity or project for which funds are authorized or made available in a conference report or bill that was not requested by the President in a budget submission to Congress.

Legislative language may explicitly designate any portion of a lump-sum amount for particular purposes. In addition, instructions for targeted spending are more commonly found in appropriations committee reports accompanying appropriations bills. Although committee reports and managers' statements lack the force of law, these documents help explain congressional intent and affect budget decisions because agency heads must annually defend their allocations and could be penalized if they ignored lawmakers' directives. All 17 earmarks we examined originated in appropriations committee reports. None were statutorily specified in the FY 2005 Defense Appropriation Act signed by the President.

Congressional Add-Ons. Of the 17 earmarks reviewed, 14 earmarks were congressional add-ons to existing programs. Twenty-six contract actions with a total value of \$75.5 million related to these 14 earmarks. The programs funded by these earmarks were the following:

- Combat Vehicle Research,
- Bradley Integrated Modernization,
- Construction Equipment Service Life Extension Program,
- Earth Moving Equipment - United States Navy Construction Units,

- SEABEE Construction Equipment,
- Halvorsen Loaders,
- Insensitive Munitions Production - Holston Army Ammunition Plant,
- Holston Army Ammunition Plant RDX and HDX Production,
- Cost-Effective Targeting System,
- Maintenance Analysis Safety and Training,
- P-3C Digital Autopilot for Additional Aircraft Upgrades,
- Bacchus Naval Industrial Plant,
- New England Manufacturing Supply Chain, and
- Defense Supply Chain Technology.

DOD officials stated that they treated these earmarks as supplemental funding to their respective programs because the earmark portion was comingled with the budgeted amounts. We determined that these programs were pre-existing requirements that provided value to DOD.

Work Performed

DOD activities used FY 2005 earmarks to procure an assortment of equipment, supplies, and services. We judgmentally selected 17 earmarks from the FY 2005 OMB database, valued at \$125.3 million. For the 17 earmarks selected, we identified 29 contract actions composed of task orders and modifications valued at about \$77.1 million. Specifically, for 14 earmarks we examined 26 contract actions for market research, competition, and fair and reasonable pricing. In addition, the remaining three earmarks related to the Air Force's Distinguished Visitor (DV) airlift mission at Scott Air Force Base; the 3 earmarks also funded the staffing and administrative functions of Air Force personnel performing the mission. We reviewed 3 contract actions related to the DV airlift mission. Although all earmarks reviewed were received in FY 2005, several involved ongoing programs initiated in earlier fiscal years. We reviewed documentation maintained by the contracting organizations to support procuring services, equipment, and supplies. The purchase documents we reviewed were military interdepartmental purchase requests and acceptances, statements of work, cost proposals, sole-source letters, contract award documents, determination and findings, task orders, price negotiation memoranda, task order modifications, requests for proposals, orders for supplies and services, and miscellaneous correspondence. We interviewed program managers, finance officials, resource managers, analysts, directors, resource advisors, and contracting officer's technical representatives about purchase requirements and acquisition, types of funds used, market research, competition, and fair and reasonable pricing.

Results

DOD activities generally used FY 2005 DOD earmarks to fund legitimate DOD requirements and missions. However, we determined from our review of 26 contract actions that DOD activities did not always comply with the Federal Acquisition Regulation (FAR) and DOD procurement regulations when procuring services. For 8 of 26 contract actions related to 3 of the 14 earmarks, we identified concerns about market research, competition, and fair and reasonable pricing determinations. These conditions occurred because language in the appropriation committee report gave DOD little or no latitude in how to use the funding. Because many of the earmarks related to existing programs, DOD officials generally awarded contract actions to the incumbent vendors without considering whether competition between vendors for the products

or services was viable. As a result, DOD did not conduct adequate market research that may have resulted in increased competition, and DOD may have paid more than it should have if competition occurred or if price reasonableness was properly documented.

Market Research and Competition. Two contract actions, valued at \$4.7 million, related to one earmark did not have adequate market research or demonstrate competition. FAR Subpart 7.102(b), "Policy," states that agencies must perform acquisition planning and conduct market research for all acquisitions to provide for acquiring commercial items suitable to meet the agency's needs and to promote full and open competition. FAR Part 10, "Market Research," prescribes the policies and procedures for conducting market research to determine the most suitable approach to acquiring, distributing, and supporting supplies and services. FAR part 10 requires that agencies use the results of market research to determine the sources capable of satisfying the agency's requirements. Market research can help ensure that the Government gets the best product for the best price. Officials can use a variety of market research techniques to identify potential sources including reviewing recent market research for similar products, submitting requests for information, querying Government databases, viewing Web sites, obtaining source lists, reviewing catalogs, and holding pre-solicitation conferences.

FAR subpart 6.101(a) and (b) states that the contracting officer must promote and provide for full and open competition in soliciting offers and awarding Government contracts. FAR subpart 6.101 further states that the contracting officer must use the most appropriate form of competition to meet the needs of the Government. The New England Manufacturing Supply project reported an earmark for \$5.6 million but inadequate market research by Defense Logistics Agency officials may have limited the services being obtained from another source to fulfill Phase III of the project. The contractor would be performing a small portion of the contract's scope of work and opportunity may have existed for a subcontractor or other contractor to have competed. Defense Logistics Agency officials' lack of market research limited their ability to seek competition that may have resulted in better value from another source.

Fair and Reasonable Pricing. Six contract actions, valued at \$6.4 million, related to two earmarks did not have adequate support to show that DOD officials performed a determination of fair and reasonable pricing. FAR Subpart 15.402, "Pricing Policy," states that contracting officers must determine price reasonableness, and FAR Subpart 15.406-3, "Documenting the Negotiation," states that contracting officers must document that the price is fair and reasonable in the price negotiation memorandum. FAR Subpart 15.403, "Obtaining Cost or Pricing Data," states that contracting officers are responsible for obtaining adequate information to evaluate price reasonableness. For sole-source contracts, officials should ensure that pricing data are available to support price reasonableness and ensure that the Government achieves the best value. For example, a DOD activity used earmark funding for work related to the combat vehicle research project, but it is unlikely that DOD officials awarded contract W56HZV-06-C-0459 based on a fair and reasonable price determination. The contract was for developing stir weldings in support of combat vehicle mobility. An Independent Government Cost Estimate, price negotiation memorandum, or historical costs were not available to assess and determine price reasonableness.

Distinguished Visitor Mission Earmarks. We examined three earmarks on which we selected three contract actions. The three earmarks funded the site activation expenses, personnel cost, and other administrative expenses associated with the DV airlift mission of the 932nd Airlift Wing (AW) at Scott Air Force Base, Illinois. In addition, we reviewed the requirement for the DV mission at Scott Air Force Base. In conjunction with the 89th AW and the 201st Airlift Squadron, the 932nd AW provides worldwide airlift service for DVs to locations in the United States and other parts of the world. The DVs include congressional members and delegations, Executive branch and DOD officials and other high-ranking dignitaries.

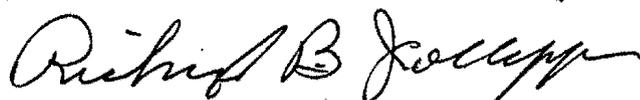
We determined that the DV passengers transported by the six aircraft that the 932nd AW used for DVs were picked up at and later returned to Andrews Air Force Base, Maryland. However, all six aircraft were based at Scott Air Force Base, Illinois, a roundtrip distance of 1,214 miles. With the exception of crews, the aircraft contained no passengers on the flight to and from Scott Air Force Base. No cost-benefit analysis of the logistics and potential for savings has been performed on the 932nd AW's DV mission to determine whether the mission is viable at Scott Air Force base, the mission should be transferred to an alternative unit or location, or alternative aircraft configurations would be more efficient and more cost-effective.

Suggested Actions

We suggest that the Under Secretary of Defense (Comptroller)/Chief Financial Officer include language, when apportioning congressionally directed funds to DOD recipients, that requires adherence to the Federal Acquisition Regulation and DOD procurement regulations related to market research, competition, and fair and reasonable pricing. We also suggest that the Under Secretary of Defense for Acquisition, Technology, and Logistics issue a memorandum to the Services and Defense agencies stating that market research, competition, and fair and reasonable pricing must occur to the maximum extent possible when awarding contracts funded with earmarks.

We suggest that the Commander, Air Mobility Command, in conjunction with the Commander, Air Force Reserve Command, perform a comprehensive cost-benefit analysis of the 932nd AW's DV transport mission to determine whether the mission is cost-effective and logistically viable or whether the mission should be performed by the 89th Airlift Wing and the 201st Air Squadron at Andrews Air Force Base.

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 604-9201 (DSN 664-9201).



Richard B. Jolliffe
Assistant Inspector General
Acquisition and Contract Management