



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

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NATIONAL SECURITY AND
INTERNATIONAL AFFAIRS DIVISION

JUNE 1, 1983

B-208191

The Honorable Verne Orr
The Secretary of the Air Force



121528

Dear Mr. Secretary:

Subject: Air Force Breakout Efforts
Are Ineffective (GAO/PLRD-83-82)

We have reviewed the effectiveness of efforts at the Oklahoma City Air Logistics Center (OC-ALC) to implement the Air Force High Dollar Spare Parts Breakout Program. We plan, during future audits, to assess this program in other Department of Defense (DOD) organizations.

Both DOD and certain congressional committees are concerned about the continuing and worsening trend in noncompetitive procurement of spare parts. During fiscal year 1981, the Air Force Logistics Command (AFLC) procured over \$1 billion in engine spare parts with only about 11 percent of the procurements awarded competitively.

On April 19, 1983, the Subcommittee on Legislation and National Security, House Committee on Government Operations, held hearings on breakout. At these hearings, DOD stated that it was aware that the breakout program had "wandered" and "there was mounting concern that DOD was losing cost-saving opportunities." DOD also stated that (1) it will publish revised guidance on the breakout program, (2) it directed its components to review and to initiate steps to improve the procurement status of certain parts by the end of fiscal year 1984, and (3) on March 15, 1983, the Deputy Secretary of Defense directed the military departments and defense agencies to take steps to overcome factors inhibiting breakout of replenishment spare parts.

In addition, the Air Force testified that our report findings were generally valid and that data problems and a lack of personnel were inhibiting breakout.

In summary, we believe the Air Force is not breaking out, to the maximum practicable extent for competition or direct purchase, the high dollar value aircraft engine replenishment spare parts supplied by a large prime contractor. Breakout efforts at ALCs have been limited because of a lack of information on the actual manufacturers of the parts and uncertainty about the Government's rights to use technical data prepared by the prime contractor.

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The Air Force has attempted to increase its breakouts through more aggressive negotiations with the prime contractor (United Technologies Corporation, Pratt & Whitney Aircraft) who is the major supplier of high dollar value spare parts. But we believe the Air Force needs to develop better ways of identifying actual manufacturers of high dollar value parts so that purchases can be made directly from them. These parts account for only about 7.5 percent of the spare parts that ALCs buy from the prime contractor, but account for about 76.6 percent of the procurement dollars. By avoiding the prime contractor's markup and reducing production leadtime by direct purchase of a portion of these relatively few parts, ALCs can maximize savings.

DOD'S BREAKOUT PROGRAM

DOD issued the joint regulation "High Dollar Spare Parts Breakout Program" (Air Force Regulation (AFR) 57-6) in 1969. The objective of this program is the earliest possible screening of spare parts to determine the optimum procurement methods, particularly the potential for breakout for competition or direct purchase.

ALCs designate screening results by assigning (1) procurement method codes (PMCs) to denote the procurement status of spare parts and (2) suffix codes to indicate why the PMC was selected.

- PMC 1 denotes the part is already competitive.
- PMC 2 denotes the part is suitable for competition for the first time.
- PMC 3 denotes the part is procured directly from the actual manufacturer.
- PMC 4 denotes the part is suitable for direct purchase from the actual manufacturer rather than the original prime for the first time.
- PMC 5 denotes that the part is not suitable for competitive procurement or direct purchase. Therefore, the part continues to be procured from a prime contractor who is not the actual manufacturer.

Suffix codes fall into three broad categories: technical, data, and economic evaluations. Technical evaluations are concerned with the manufacturing, quality, and reliability of parts. Data evaluations discuss the adequacy and legality of using available technical data for procurement and economic evaluations involve the cost effectiveness of breaking out individual parts.

OBJECTIVES, SCOPE, AND METHODOLOGY

We initiated this review because of concern expressed by DOD and the Congress concerning the limited success of DOD's breakout program. Our objectives were to identify the actual manufacturers of high dollar value replenishment spare parts purchased from the prime engine contractor and to determine the potential for buying parts not actually manufactured by the prime either competitively or direct from the actual manufacturer.

We limited our review to (1) aircraft engine replenishment spare parts because they represent a large portion of the Air Force's parts procurements and (2) parts purchased from a prime contractor (Pratt & Whitney) who furnishes about 55 to 60 percent of the aircraft engine spare parts requirements.

We developed a universe of consumable parts bought from the prime contractor in fiscal year 1981, along with the annual demand for each part. From this universe we selected for review all 73 parts with annual demands over \$100,000 each. We identified the actual manufacturers (1) using vendor identification numbers stamped on the parts or (2) with the assistance of the Air Force plant representative at the prime contractor's plant. We interviewed the actual manufacturers to determine their contribution to the production and quality control of the sample parts. We also interviewed OC-ALC officials and reviewed regulations, records, and reports concerning the breakout program to identify issues barring breakout and potential solutions.

The universe contained about 3,705 parts with a combined annual demand of about \$40 million. The total annual demand for the 73 parts we selected was \$19.3 million. Hence, our sample included about 2 percent of the items, but about 48 percent of the annual demand dollars. Thus, we deliberately biased the sample to test the feasibility of identifying actual manufacturers of high dollar value parts. As a result, our sample results cannot be projected to the universe.

We considered sample parts manufactured by subcontractors and shipped as finished products to the prime contractor as likely breakout candidates for direct or competitive purchase. Testing and inspections required to assure requisite quality and reliability were not considered an impediment to breakout unless there were indications that the prime had special test and inspection facilities and/or procedures at its plants for "over-inspections" after receiving finished parts from its subcontractors. We considered that any of the prime contractor's quality control inspections at the vendor's plant could be accomplished by the Government after breakout.

Our work was performed during fiscal years 1981 and 1982 at the OC-ALC, which is primarily responsible for procuring spare parts for the prime contractor's engines. We also visited the prime's manufacturing plant in East Hartford, Connecticut, and various subcontractors.

This review was performed in accordance with generally accepted government auditing standards.

GROSS SAVINGS FROM COMPETITION OR DIRECT PURCHASE
OF HIGH DOLLAR VALUE PARTS ARE SUBSTANTIAL

Direct procurements from actual spare part manufacturers can result in gross savings to the Government by (1) eliminating the prime's markup and/or profits and (2) reducing stock requirements caused by production leadtime. Furthermore, the prime contractor frequently has more than one supplier for each spare part; thus, competition and associated price reductions may be feasible. We call the change in price alone "gross savings" because other factors must be considered, such as the cost to the Government for (1) administering the breakout program, (2) qualifying new contractors, (3) competing the procurement, and (4) providing engineering, quality control, and other necessary activities carried out by the prime contractor before breakout.^{1/} In addition, the price may vary because of quantity discounts and escalation. Examples of the gross savings that resulted from breakout and procurement from other than the prime contractor follow.

| Sample part | Sole-source buys before breakout | | Competitive or direct buys after breakout | | Gross savings | | |
|-------------|----------------------------------|------------|---|------------|---------------|---------------|--------------------|
| | Quantity | Unit price | Quantity | Unit price | Unit price | Unit Per-cent | Total |
| #1 baffle | 61 | \$3,433 | 85 | \$1,377 | \$2,056 | 60 | \$174,760 |
| #15 support | 26 | 14,960 | 36 | 8,450 | 6,510 | 44 | 234,360 |
| #15 support | 26 | 14,960 | 61 | 7,240 | 7,720 | 52 | 470,920 |
| #58 seal | 382 | 2,020 | 164 | 647 | 1,373 | 68 | <u>225,172</u> |
| Total | | | | | | | <u>\$1,105,212</u> |

Prior to breakout, the last procurement of these parts was made on a sole-source basis from the prime contractor. All three

^{1/}Such costs are to be evaluated under AFR 57-6 by DOD activities to determine the economies of breaking out individual parts. We did not cover these evaluations as part of our review.

parts had an assigned PMC of 3, indicating the prime was the actual manufacturer. Assigned suffix codes restricted breakout because they indicated that only the prime contractor had the unique manufacturing processes or tooling required to produce the baffles and supports and that only the prime could assure quality of the seals if they were manufactured by other sources. However, after breakout four sources other than the prime bid on the baffles, five other sources bid on the supports, and two other sources (both subcontractors of the prime) bid on the seals. In each case, the prime's subcontractors received the contracts, with unit price reductions ranging from 44 to 68 percent.

Direct purchase from actual part manufacturers can also reduce Air Force investment in inventories and storage costs since the subcontractors' production leadtimes to the prime are substantially less than the prime's leadtime to the Air Force. Leadtime is the time between the date of the contract or purchase order and the receipt of the first significant delivery quantity (under normal delivery conditions). For example, the latest scheduled production leadtime from the prime for one of our sample parts, a blade, was 588 days. However, the subcontractor said its leadtime to ship these blades to the prime was only 270 days, which would be its leadtime for selling direct to the OC-ALC.

We identified two factors that account for most of this leadtime variance of 318 days. First, the prime took almost 9 months from the date of the OC-ALC's purchase order to place an order with its supplier. 1/ Second, subcontractors shipped their finished products to the prime's plant for sample inspections and/or repackaging before delivery to the OC-ALC.

Based on the vendors' and subcontractors' production leadtime for 29 of the sample parts shipped as finished products to the prime, we estimate that direct buying from the actual manufacturers would reduce Air Force inventory requirements by \$3.5 million, stock safety levels by \$366,000, and annual holding costs by \$59,000. These savings may be reduced to some degree if the Air Force's present administrative costs and leadtime are increased by purchasing direct or competitively rather than by using basic ordering agreements to buy sole source from the prime when it is not the actual manufacturer.

1/We did not attempt to determine the reason for the delay.

LACK OF ACCURATE INFORMATION ABOUT INDIVIDUAL
PART MANUFACTURERS OBSTRUCTS BREAKOUT

Subcontractors manufactured and shipped 47 of the 73 sample parts to the prime as finished products. The OC-ALC has not developed similar information, however, because it has not established effective procedures to identify the actual manufacturers of individual parts. Because the OC-ALC did not know who the actual manufacturers were, it:

--Coded parts with a PMC of 3 to indicate that the prime is the manufacturer although the parts were actually made by its subcontractors.

--Coded parts with suffix codes to indicate that manufacturing and quality control requirements justify continued buying from the prime although the manufacturing and quality of the part was controlled by its subcontractors.

Such coding inaccuracies conceal the fact that these are sole-source procurements from the prime who is not the actual manufacturer and preclude further breakout efforts. We found similar problems at other ALCs in previous reviews.

Air Force lacks reliable data
on actual manufacturers

Reliable data on actual part manufacturers are not available for breakout purposes throughout the Air Force. In a recent report (GAO/PLRD-82-104, August 2, 1982), we concluded that the Small Business Administration's (SBA's) breakout efforts at four ALCs were impeded because such information was not available from the Air Force. As a result, SBA had to establish its own program to identify and qualify part manufacturers for breakout to small business concerns. We recommended that the Administrator of SBA assign additional resources to the breakout efforts at ALCs.

Sole-source purchases from a prime contractor
who is not the actual manufacturer are understated

The PMCs for about 60 percent of our sample items were erroneous. Parts were coded as direct purchases (PMC 3 or 4) when they were really sole-source procurements from sources other than the actual manufacturers (PMC 5). Subcontractors manufactured 47 of our 73 sample parts and shipped them as finished products to the prime. Although the prime was not the actual manufacturer, 44 were coded as purchased direct from the actual manufacturers.

OC-ALC officials estimate that subcontractors make 80 percent of the spare parts they buy from the prime. Yet the OC-ALC codes them as direct purchases because it does not know who manufactures the parts. This is because (1) the prime is not required by procurement regulations or contracts to provide data to the OC-ALC concerning the source of individual parts for which the prime is the design control activity and (2) the Air Force has not developed the information by other means.

OC-ALC's fiscal year 1981 replenishment spare parts procurement report showed 5,519 parts costing \$339 million as direct purchases (sole source from the actual manufacturer) and only 160 parts costing \$4.3 million as sole source from the prime contractor who was not the actual manufacturer. On the basis of our sample analysis, we believe (1) direct purchases (PMC 3) could be significantly overstated and (2) sole-source procurements from the prime contractor who is not the actual manufacturer (PMC 5) could be significantly understated. Because of these overstatements and understatements, Air Force resources may not be directed to breaking out parts.

Suffix codes incorrect

The suffix codes assigned by the OC-ALC to justify purchasing from the prime were frequently inaccurate. The OC-ALC cited inaccurate technical reasons (suffix codes) for buying 23 of the 47 sample parts from the prime. For example, one subcontractor manufactured nine parts having an annual demand of about \$1.9 million or about 10 percent of our sample parts. The OC-ALC said it bought three of these parts from the prime contractor to maintain quality of the part and to restrict procurement to sources either (1) having the unique capability to produce the parts or (2) having the master or coordinated tooling needed for production. We found, however, that the subcontractor, not the prime contractor, developed and implemented the quality control procedures, developed the manufacturing process, and owned the tooling and equipment used to produce the parts. Thus, the reasons stated for buying parts from the prime were inaccurate.

We believe the OC-ALC coded these parts inaccurately because the technical evaluators were unaware of the prime's contribution to the manufacture and reliability of the individual parts.

BREAKOUT EFFORTS NOT DIRECTED
TO HIGH DOLLAR VALUE PARTS

The SBA program, see page 6, which the Air Force is supporting, has been relatively successful but is not directed to high dollar value spare parts. These parts are the relatively few that make up a preponderance of the annual procurement dollars. For example, 279, or about 7.5 percent of

our universe of 3,705 consumable parts bought from the prime in 1981, accounted for about \$31 million or about 76.6 percent of the annual procurement dollars.

Although the OC-ALC has been relatively successful in breaking out selected parts under various special projects initiated since 1979, it has not directed its efforts to high dollar value parts. For example, the OC-ALC improved the procurement status of 42 parts as a result of contracting with the prime contractor to rescreen 100 parts. Only 12 of the 73 high dollar parts in our sample, however, were included in this effort.

The following chart shows the results of special breakout efforts on some of our 73 sample parts.

| <u>Breakout effort</u> | <u>No.</u> |
|--|------------|
| Not included in any breakout efforts | 31 |
| Included in breakout efforts but no improvement | 25 |
| Broken out and coded direct from prime's vendors | 7 |
| Broken out and coded for competition | <u>10</u> |
| | <u>73</u> |

The 10 items broken out for competition occurred primarily, however, as a result of vendors actively seeking to qualify for direct sales rather than the OC-ALC seeking to identify and qualify them as new sources.

UNIQUE DATA RESTRICTIONS IMPEDING
BREAKOUT NEED TO BE RESOLVED

The OC-ALC has not made a concerted effort to identify and remove restrictions that may no longer apply on the use of technical data for procurement of replacement spare parts. As a result, competition or direct purchase from the actual part manufacturers who are technically able and willing to sell direct to the OC-ALC has been hindered.

Unique data restrictions imposed by provisions of the initial engine contracts prevent the OC-ALC from breaking out many of the sample parts that were manufactured by the prime's subcontractors. For example, one subcontractor manufactured and shipped nine of our sample parts as finished products to the prime. Upon learning of the subcontractor's technical ability and willingness to sell direct, the OC-ALC contacted the subcontractor and found the subcontractor's only stipulation for selling direct was assurance from the OC-ALC that the technical data in its possession could be used without infringing on the prime's data rights. Because of uncertainty over data restrictions the OC-ALC

was not able to make such a certification or to furnish its own certification or to furnish its own drawings; therefore, no breakout occurred. Thus, restricted data is the primary issue obstructing the OC-ALC from breaking out many of the sample parts that we found were manufactured by the prime's subcontractors.

Data use restricted by contract provisions

The problem of data restriction facing the OC-ALC stems from an agreement negotiated by the Navy and the prime contractor involving engine acquisition contracts from fiscal years 1962 to 1968. The agreement provides that data relating to parts designated "engineering critical" would be considered proprietary and bear a restrictive legend precluding the Government from using the data for reprourement purposes.

Data relating to parts that presented no significant manufacturing problem or that experienced only ordinary risks in an engine environment were to be designated "not engineering critical." The Government would be able to procure such parts from any qualified source without consideration of, or restriction by, whatever data rights the prime might have.

The agreement was considered necessary at the time because engine development costs had been financed partially by both the prime contractor and the Government. The procurement regulations state that the ownership of rights in data is determined by who funded the development of the data. Therefore, an intermixing of funds made the determination of rights in data virtually impossible to establish.

Methodology for resolving data restrictions

The OC-ALC Judge Advocate believes the "engineering critical" criteria equate to an engineering determination that certain items demand continuing control of the manufacturing process by the design activity (prime contractor) to assure the requisite quality and reliability of those items, but where such continuing control by the prime is not required, the items are not "engineering critical" within the meaning of the contract. He believes that questionable designations can be changed with the concurrence of the prime or can be challenged and resolved under the disputes clause of the contract.

Many of our sample parts were manufactured by the prime's subcontractors. For many of these parts, the prime does not exercise continuing control of the manufacturing process to assure requisite quality and reliability. Consequently, in our opinion, these parts are likely candidates for challenging the "engineering critical" designations under the criteria expressed by the Judge Advocate. But the OC-ALC has taken no action to resolve the data restrictions impeding breakout of these parts.

The OC-ALC is not in a position to identify and challenge other high dollar value parts with questionable "engineering critical" designations because it lacks reliable information on the actual manufacturer of individual parts. In our opinion, this information is an essential prerequisite for determining who exercises continuing control over the manufacturing process of individual parts. According to the Judge Advocate, this information is needed to establish the legitimacy of "engineering critical" designations and related data restrictions.

PROPRIETARY DATA CONSTRAINTS TO BREAKOUT APPEAR WIDESPREAD

Although data restrictions involving our sample parts were unique because of contract provisions, data issues apparently have an Air Force-wide impact on constraining breakout from other prime contractors.

We found that various ALCs are encountering breakout problems that they attribute to poor planning and management in the acquisition of data. ALCs reported that data furnished by the prime contractors were frequently not usable for procurement as a result of unsupported proprietary claims or the absence of critical drawings and tolerances.

CONCLUSIONS

Replenishment spare parts purchased from the prime contractor are frequently manufactured by subcontractors and shipped as finished products to the prime. Such information is essential during the breakout screening process to identify parts having breakout potential for competition or direct purchase. However, the Air Force does not have accurate data concerning the actual manufacturers of individual parts because it has not been successful in identifying subcontractors producing finished parts for the prime.

Data restrictions have also prevented the OC-ALC from breaking out parts designated "engineering critical" by the prime under provisions of the initial contracts. Although the OC-ALC Judge Advocate has established criteria for removing these restrictions, the OC-ALC has been unable to challenge the designations and to test the adequacy of the criteria because it lacks accurate information as to the prime's contribution to the manufacturing control of the individual parts.

Many of the parts we reviewed were manufactured by subcontractors and shipped as finished products to the prime. In our opinion, these parts are prime candidates for testing the adequacy of the Judge Advocate's criteria and setting precedence for subsequent breakout efforts. But the OC-ALC has not attempted to remove the data restrictions from these parts.

We believe the Air Force needs to develop a program for determining the actual manufacturer of individual parts. Such a program would identify the parts that have the potential for direct or competitive purchase and accumulate the required production control data needed to remove inappropriate restrictions constraining breakout. In our opinion, potential breakout savings can be maximized by concentrating such program efforts on the relatively few high dollar value parts being bought from the prime.

RECOMMENDATIONS

We recommend that the Secretary of the Air Force improve the effectiveness of the High Dollar Spare Parts Breakout Program by directing:

- All appropriate Air Force units to rescreen all spare parts with PMCs of 3, 4, and 5, initially concentrating on procurements due to occur in the near future, that come under the definition of high dollar value replenishment spare parts in the breakout regulation, and establish procedures for identifying actual manufacturers of such parts scheduled for sole-source procurement from the prime contractor. Actual manufacturers, other than the prime contractor, should be contacted and a determination made as to their capabilities for supplying the part(s) direct to the Air Force.
- All appropriate Air Force units to include in all future aircraft engine contracts or contracts for major components where high dollar value spare parts are likely to be purchased, a clause that requires (1) the identification of part manufacturers and suppliers at the time of the initial acquisition, (2) notification of changes in manufacturers and suppliers during the life of the contract, and (3) if the prime contractor fails to make a good faith effort to meet the requirements of (1) and (2), any limited rights markings on technical data related to the parts may be canceled or ignored by the contracting officer.
- The Commanding Officer of the OC-ALC to establish the identity of the actual manufacturer of an engineering critical high dollar value replenishment spare part. If there is doubt as to the propriety of the "engineering critical" designation (that is, the prime contractor is no longer actively involved and is not controlling the manufacturing process to assure requisite quality and reliability of the part), the Commanding Officer should ask the prime contractor to justify the designation. If the

prime refuses or fails to substantiate the claim, the Commanding Officer should initiate action to remove the restrictive markings.

AGENCY COMMENTS AND OUR EVALUATION

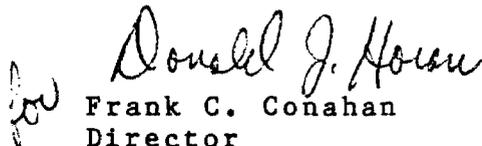
A draft of this report was forwarded to you for comment on March 30, 1983. Since we did not receive a reply within the time prescribed by law, we are issuing the report without official comments.

We requested and received comments from Pratt & Whitney (see app. I). Pratt & Whitney stated (1) it had cooperated with the Air Force and breakouts had increased recently, (2) our extrapolating OC-ALC results to other ALCs was inappropriate, (3) we had overlooked some breakout program costs to the Government, and (4) our use of "questionable restrictions" was inappropriate. (See app. II for our rebuttal to these comments.) Generally, we believe our findings are still valid. However, we did delete "questionable restrictions" and substitute "restrictions that may no longer apply".

This report contains recommendations to you on page 11. As you know, 31 U.S.C. § 720 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Chairmen of the above-named committees; the Director, Office of Management and Budget; the Secretary of Defense; and the Administrator of the Small Business Administration. We will also make copies available to others on request.

Sincerely yours,


Frank C. Conahan
Director

Enclosures - 2



P. O. Box 2691
West Palm Beach, Florida 33402
305/840-2000

8 April 1983

Government Products Division

Frank W. McAbee, Jr.
President

Mr. Donald J. Horan
Director Procurement, Logistics and
Readiness Division
United States General Accounting Office
Washington, D. C. 20548

Dear Mr. Horan:

We appreciate the opportunity to review and comment on the GAO draft report on Spare Parts Breakout (Code 950648). We are unable to provide specific comments relative to the analysis without the benefit of the part numbers involved in the study. We do, however, have some general comments relative to this report and would like to offer the following:

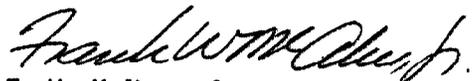
- o The use of the FY'81 data (October 1980 - September 1981) to portray the current Breakout environment is misleading in light of the fact that Pratt & Whitney provided to the Oklahoma City Air Logistics Center (OC-ALC) 5469 part numbers as breakout candidates during FY'82. We provided the current record vendor name, and we are continuing to assist OC-ALC in identifying vendors for the 5469 candidate breakout parts. Therefore, we believe that if a similar analysis were performed today, it would show that significant breakout has been achieved.
- o Extrapolating the results of the OC-ALC analysis to identify problems inhibiting breakout at other Logistics Centers is not appropriate. In the case of the F100 engine at the San Antonio Air Logistics Center (SA-ALC) the Air Force generally has unlimited rights in the data, and they were successful in FY'82 in breaking out a large portion of the procurements placed. We have assisted SA-ALC by providing vendor names and addresses for approximately 1400 part numbers during FY'82.
- o The net savings identified in the draft report as accruing to the U.S. Government through breakout did not recognize certain increased costs associated with: 1) configuration management related to maintenance of drawings, data and records to insure currency with Engineering changes and other technical information; 2) maintaining and operating an expanded procurement organization which schedules, expedites and administers thousands of Purchase Orders issued to hundreds of vendors by several government procurement organizations; 3) additional quality personnel and equipment required to monitor and inspect the supplier quality system; 4) additional quality personnel required to identify and reject nonconforming parts; 5) additional engineering personnel

Mr. Donald J. Horan
8 April 1983
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required to resolve quality problems associated with these rejected parts and quality problems identified in the field; 6) inability to combine individual spare parts requirements for the same part numbers to attain maximum quantity price breaks; 7) loss of flexibility for diverting parts terminated for convenience; 8) certain necessary fixed costs which are not volume related which would have to be absorbed by the remaining military and commercial business base. Most of these costs are identified as 'standard' breakout costs per AFR 57-6: High Dollar Spare Parts Breakout Program. These costs must be quantified and added to the breakout parts price in order to make a valid cost effectiveness comparison.

- o Relative to removing impediments for breakout, we believe that the inference to 'questionable restrictions' in the use of technical data is inappropriate. This term suggests that Pratt & Whitney has wrongfully marked the data delivered. We firmly believe that the 'limited rights' legends were properly applied under the provisions of the contract under which this data was generated.

Again, we appreciate the opportunity to review and comment on the draft report. If we may be of further assistance, please do not hesitate to call on us.


F. W. McAbee, Jr.

GAO RESPONSES TOPRATT & WHITNEY GENERAL COMMENTSPRATT & WHITNEY COMMENT

"The use of the FY'81 data (October 1980 - September 1981) to portray the current Breakout environment is misleading in light of the fact that Pratt & Whitney provided to the Oklahoma City Air Logistics Center (OC-ALC) 5,469 part numbers as breakout candidates during FY'82. We provided the current record vendor name, and we are continuing to assist OC-ALC in identifying vendors for the 5,469 candidate breakout parts. Therefore, we believe that if a similar analysis were performed today, it would show that significant breakout has been achieved.

GAO response

Our reported position is that Air Force breakout efforts should be directed to high dollar value spare parts as defined in the breakout regulation. We state that the OC-ALC has initiated various special breakout projects since 1979. One such program involved the above effort mentioned by Pratt & Whitney. Only one of our 73 high dollar value sample parts was included in the 5,469 parts. Thus, we believe the report is not misleading because it recognizes that breakout efforts have not been directed to high dollar value parts.

PRATT & WHITNEY COMMENT

"Extrapolating the results of the OC-ALC analysis to identify problems inhibiting breakout at other Logistics Centers is not appropriate. In the case of the F100 engine at the San Antonio Air Logistics Center (SA-ALC) the Air Force generally has unlimited rights in the data, and they were successful in FY'82 in breaking out a large portion of the procurements placed. We have assisted SA-ALC by providing vendor names and addresses for approximately 1,400 part numbers during FY'82."

GAO response

We generally agree with Pratt & Whitney's comments that data issues may not be a problem with replenishment spare parts for Pratt & Whitney's F-100 engines at the San Antonio ALC. However, we did find indications that technical data issues were a problem at centers other than the OC-ALC with respect to engines and end-items furnished by prime contractors other than Pratt & Whitney. A recent DOD Inspector General's report further supports the reported statement that data problems exist throughout the Air Force, not just at the OC-ALC. We incorporated a new section, entitled "Proprietary Data Constraints to Breakout Appear Widespread," before the conclusion section in our report to demonstrate that data problems are Air Force-wide.

PRATT & WHITNEY COMMENT

"The net savings identified in the draft report as accruing to the U.S. Government through breakout did not recognize certain increased costs associated with: 1) configuration management related to maintenance of drawings, data and records to insure currency with Engineering changes and other technical information; 2) maintaining and operating an expanded procurement organization which schedules, expedites and administers thousands of Purchase Orders issued to hundreds of vendors by several government procurement organizations; 3) additional quality personnel and equipment required to monitor and inspect the supplier quality system; 4) additional quality personnel required to identify and reject nonconforming parts; 5) additional engineering personnel required to resolve quality problems associated with these rejected parts and quality problems identified in the field; 6) inability to combine individual spare parts requirements for the same part numbers to attain maximum quantity price breaks; 7) loss of flexibility for diverting parts terminated for convenience; 8) certain necessary fixed costs which are not volume related which would have to be absorbed by the remaining military and commercial business base. Most of these costs are identified as 'standard' breakout costs per AFR 57-6: High Dollar Spare Parts Breakout Program. These costs must be quantified and added to the breakout parts price in order to make a valid cost effectiveness comparison."

GAO response

As stated by Pratt & Whitney, most of the costs referred to above are identified as standard breakout costs in AFR 57-6. The High Dollar Spare Parts Breakout Program recognizes that such costs will be incurred to some degree either by the prime or directly by the Government after breakout. For this reason, the program calls for an economic evaluation concerning the cost effectiveness of breaking out individual items (see p. 2).

Which of the costs referred to by Pratt & Whitney will be incurred by the Government after breakout and how much will be incurred varies with individual parts. For example, vendors we visited said that many of our sample parts had not been redesigned during the many years they manufactured them. The Government's configuration control costs for these parts would then be nominal or non-existent. Also, Defense Contract Administrative Service representatives are located at or near some of the vendors' plants so additional costs to monitor quality control would be nominal for parts bought direct from these vendors.

We agree that after breakout the Government may absorb the same fixed costs when they are allocated on some basis other than volume. However, the Government's share of fixed costs allocated on the basis of volume would be reduced and absorbed by commercial business if the basis remains unchanged. Whether the total amount of fixed cost absorbed by the Government after breakout is reduced or remains the same cannot be determined without a detailed knowledge and review of Pratt & Whitney's cost system.

Similarly, the savings associated with breaking out individual parts cannot be determined without the economic evaluation called for by AFR 57-6. To clarify this matter, we added item (4) to the following statement on page 4:

"We call the change in price alone 'gross savings' because other factors must be considered such as the cost to the Government for (1) administering the breakout program, (2) qualifying new contractors, (3) competing the procurement, and (4) providing engineering, quality control and other necessary activities carried out by the prime contractor before breakout."

We also noted on page 4 that AFR 57-6 requires DOD activities to determine the economics of breaking out individual parts, but that we did not cover these evaluations as part of our review. We limited our review to 73 high dollar value spare parts because we believe the economic evaluations associated with breaking out these parts are likely to show the greatest savings.

PRATT & WHITNEY COMMENT

"Relative to removing impediments for breakout, we believe that the inference to 'questionable restrictions' in the use of technical data is inappropriate. This term suggests that Pratt & Whitney has wrongfully marked the data delivered. We firmly believe that the 'limited rights' legends were properly applied under the provisions of the contract under which this data was generated."

GAO response

We have no objections to removing "questionable" to avoid possible improper inference. Accordingly, we have revised the sentence on page 8 to read as follows:

"OC-ALC has not made a concerted effort to identify and remove restrictions that may no longer apply to the use of technical data for procurement of replenishment spare parts."