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STATEMENT OF

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BEFORE THE

S. 2802

SUBCOMMITTEE ON ANTITRUST AND MONOPOLY LEGISLATION

SENATE COMMITTEE ON THE JUDICIARY

ON

[THE EFFECT OF DEPARTMENT OF DEFENSE PROCUREMENT
ON COMPETITION AND CONCENTRATION]

I am pleased to appear before this Subcommittee today to participate in your study of the effect of Department of Defense procurement on competition and concentration.

Our country has become increasingly dependent upon the use of private industry in the development of weapons for the national defense. Each year the Department of Defense (DOD) spends vast sums of money for research, development, facilities, supplies, and services. This year it will approach $50 billion. For this reason, the Department's procurement policies and practices are bound to have a significant impact on defense-oriented industries such as aerospace, electronics, and shipbuilding and their subcontractors and suppliers.

Competition is a natural, regulatory force vital to the economy and future well-being of our country but undue concentration of

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Government procurement can result in diminution or loss of benefits that flow from viable competition. Thus, the importance of your study is overwhelmingly clear.

We understand that the purpose of the hearings is to acquaint the Congress with some of the matters that may have a bearing on competition and concentration in American industry and to serve as a basis on which your Committee and other committees can select areas requiring more intensive study. Our remarks will therefore be directed to the methods of procurement used by DOD as they bear on the extent of competition that may be expected from the use of each.

ARMED SERVICES PROCUREMENT ACT OF 1947

The Armed Services Procurement Act of 1947, as amended, is the basic statute which governs current defense procurement procedures. The statute, as amended, and its implementing regulation--the Armed Services Procurement Regulation--express the basic philosophy that the interests of the Government are best served when the maximum amount of competition possible under the circumstances of a particular procurement is achieved.

The 1947 act, as amended, requires the military departments to use formal advertising procedures whenever feasible and practicable to do so. The act also provides 17 specific "exceptions" which authorize the departments to award a purchase or contract through negotiation when it is determined under one of these "exceptions" that formal advertising cannot be used. Attachment I to our statement contains a listing of the 17 exceptions.

One of these exceptions allows for negotiations when it is deemed impracticable to formally advertise a contract. Under this general exception the Armed Services Procurement Regulation cites 17 illustrative conditions for its use and they are listed in Attachment II to our statement.

When using these negotiating authorities, and when time permits, the military departments are required by Public Law 87-653 amendment, effective December 1, 1962, to solicit proposals from the maximum number of qualified sources consistent with the nature and requirements of the procurement and to hold written or oral discussions with those offerors considered to be within a competitive range. By custom the process is referred to as "competitive negotiation."

In summary, there are three basic methods of procurement employed in the Department of Defense today

--Formal advertising

--Competitive negotiation

--Single source negotiation

DOD REPORTING OF PROCUREMENT ACTIONS TO THE CONGRESS

DOD regularly reports statistics to the Congress on the nature of its procurement actions. These statistics show how much defense procurement is formally advertised and how much is negotiated either through single-source solicitation or multiple-source solicitation. Going back to the first year, 1951, when recorded statistics became available, we have summarized them in a table which I will include in the record.

Fiscal year	Total procurement (billions)	Formally advertised (percent)	Negotiated (percent)		
			Multiple sources solicited (competitive procedure)	Single source solicited (noncompetitive procedure)	Total
1951	$30.8	12.1%	(a)	(a)	87.9%
1961	24.7	11.9	(a)	(a)	88.1
1962	28.1	12.4	27.1%	60.5%	87.6
1963	29.0	12.7	28.1	59.2	87.3
1964	28.2	14.4	30.7	54.9	85.6
1965	27.4	17.6	31.1	51.3	82.4
1966	37.2	14.2	35.8	50.0	85.8
1967	43.4	13.4	34.1	52.5	86.6
1968(b)	29.8	11.5	32.8	55.7	88.5

(a) Statistics not furnished for these years.

(b) Through March 31, 1968 or three quarters of the fiscal year.

Statistics for all three methods of procurement are available only since 1962. For this 6-year period formally advertised procurement averaged about 14 percent, competitive negotiation about 31 percent and single-source procurement about 55 percent. The statistics show a trend toward increased use of competitive procurement under both advertised and negotiated procedures from 1961 to 1966. The decline in competitive procurement during the past two fiscal years has been attributed to urgent procurements for the Southeast Asia conflict.

I should point out here that these statistics reflect reporting criteria of the Armed Services Procurement Regulation, which our Office has found to be in need of improvement in some respects for reporting

accurately on competitive procurements. The details are contained in attachment III to my statement. This matter was fully discussed in the Joint Economic Committee hearings last year and DOD has taken positive action to amend its reporting procedures.

We believe that statistics on methods of procurement would be more meaningful to the Congress if they were more closely related to amounts of procurement susceptible to use of the particular method. The reporting of about 13 percent formally advertised procurement last year would be more meaningful if, at the same time, the Congress knew approximately how much of DOD procurement is susceptible to the use of the formally advertised procurement procedure. That is, if DOD could segregate those types of procurements that even under optimum conditions would not be subject to formal advertising, the Congress would then be able to better evaluate the extent of procurements made under this method in light of urgency and other factors that may be involved. The same principle is true with respect to statistics for the other two methods of procurement.

FORMALLY ADVERTISED METHOD OF PROCUREMENT

The formally advertised method of procurement is generally used by the Department of Defense in the procurement of commercial-type items--such as clothes, petroleum products, lumber, and paint--as well as items of conventional military equipment which can be supplied by many concerns. These items are normally purchased by formal advertising except where the time and expense of preparation for formal advertising cannot be justified as in small purchases and emergency procurements. According to DOD statistics, formally advertised procurements last year amounted to about $5.8 billion, or 13.4 percent of its total procurement expenditure.

As previously stated, under existing law the general rule is that the Department of Defense must use the formally advertised method of procurement where feasible and practicable. Historically, this has been the most understood method of procurement. Before formal advertising procedures can be used to award a contract, however, the following conditions must be met:

1. A number of firms who are capable of producing the item and who are willing to actively compete for the contract;
2. Sufficient time to prepare for and solicit competitive bids;
3. Well-defined and stable design or performance specifications exist; and
4. Selection of the successful bidder can be made on the basis of price alone.

Advertised procurement can best be used when there is a broad production base already engaged in supplying the same or similar items and sufficient capacity exists to provide for the Government's requirements. Under such circumstances the maximum benefits of competition can be realized.

Probably the greatest deterrents to the use of formal advertising are the requirements for well defined and stable design specifications and the complex, highly sophisticated nature of weapon systems used in the nation's defense. For formal advertising to be effective, it is imperative that the specifications be clearly spelled out in the invitation for bids so that all prospective suppliers will have a complete understanding of what is required and may compete on an equal basis.

The problems associated with developing adequate specifications for use in formal advertising were explored in great detail during a procurement study conducted in 1959-60 by a Procurement Subcommittee of the Committee on Armed Services, United States Senate.

One of the principal problems brought out in these hearings was that designs are ordinarily not static in the area where most procurement dollars are being spent. If these designs were static, of course, there would be the danger of not utilizing rapidly advancing technology and industrial techniques--and outmoded weapons would be procured.

Another deterrent to the effective use of formal advertising is the lack of enough companies who are able or are willing to place themselves in a position to bid on the items. Unless real competition can be obtained, the use of formal advertising could result in substantial detriment to the Government because of the absence of restraints and controls which are applicable under other methods of procurement. In a survey we have underway we noted at one activity that about one-fourth of the advertised contracts awarded during a three-month period were awarded to sole bidders. We do not know that this situation is widespread but the apparent lack of interest on the part of prospective suppliers would indicate that advertising may have been used in inappropriate circumstances.

Introduction of two-step formal advertising

Because of the limited areas where formal advertising could be appropriately used, it became evident that there was a need for a procurement procedure that would permit some flexibility (for example, clarification of specifications) while retaining the formal and stringent characteristics of the formal bidding procedure. As a result, the Defense Department introduced the two-step formal advertising method of procurement to bridge the gap between negotiated and formally advertised procurements. Two-step formal advertising becomes most desirable usually on completion of development of a complex item or after an initial production run, when active price competition is desirable but definitive specifications sufficient for formal advertising are not yet available.

The first step in two-step formal advertising requires the submission of technical proposals by the offerors to determine their conformity to the user's technical requirement. Each technical proposal is then evaluated on the basis of the stated criteria, and a determination is made as to its acceptability. Discussions may be conducted with any offeror and must be conducted with any offeror whose proposal could be classified as acceptable after a reasonable effort had been made to clarify it or to add further information. No discussion is required, however, when it is determined that a proposal is unacceptable and a reasonable effort could not make it acceptable.

The second step is the invitation to the offerors who have submitted acceptable technical proposals to price out their proposals. Based on the bids then submitted, award is made to the lowest bidder.

This procedure does permit price competition between those suppliers whose proposals are found to be or can be made technically acceptable. It is probably most useful where reasonable performance specifications can be prepared for the item to be procured and sufficient time is available for the processes involved. It does entail some added expense to the contractor in preparing his technical proposal and for this reason may limit the number of suppliers willing to engage in such competition.

COMPETITIVE NEGOTIATION METHOD OF PROCUREMENT

The Department of Defense has, except for the last two years, made increasing use of a second method of procurement which is referred to as

competitive negotiation. This method is often used in the development and production of complex military weapons and equipment. These include aircraft, missiles, ships, tanks, radar and other complicated items which generally have no counterparts in the commercial market and other items procured under urgent conditions. The value of items negotiated last year under this kind of competitive procedure through price or technical competition amounted to about $14.8 billion, or about 34 percent of total procurement expenditures.

In competitive negotiation, factors other than price tend to have a much greater influence on the award. These factors are technical design, management capability, speed of delivery, and size and nature of a contractor's organization, personnel and facilities.

Under this procedure proposals are requested from potential suppliers and responses are evaluated on the basis of design, speed of delivery, contractor capability and price. Based on this evaluation negotiations are conducted with offerors to resolve differences and to arrive at a firm contract with the successful offeror.

It can best be used in design and developmental stages of complex systems or where time does not permit use of formal advertising. Its main advantage in these procurements is that it preserves some degree of competition in the many cases where procurement lead time is limited or the more rigid requirements for formal advertising, such as firm specifications, cannot be met.

History of efforts to improve competitive negotiation and minimize buy-in-bidding

Department of Defense studies showed that, because many years of valuable production were at stake, there was a tendency for contractors,

when competing for the initial contract for new programs, to promise overly optimistic performance and to underestimate what this performance would cost.

When buy-in-bidding occurred, the DOD was in a weakened negotiating position since the contractor, having won the initial contract, was locked in and virtually immune from the stimulus of competition in follow-on procurements for the remainder of the program--often lasting several years. This was true because awards to a new producer without adequate facilities or experience would require an extended period of preparation for manufacture and necessitate a substantial duplication of investment and effort.

Once a company had obtained an initial contract for a major system or subsystem it was reasonably sure of future procurements which would be negotiated on a single-source basis. Without competition, there was little incentive for the contractor to reduce or control the ultimate cost of the weapon system since such efforts would merely reduce the contractor's base for computing profits in follow-on awards.

The DOD has included in its Armed Services Procurement Regulation a policy statement which discourages buy-in-bidding. It states that such practice is not favored by the DOD since its long term effects may diminish competition and result in poor contract performance. The regulation was revised in April 1968 to encourage procurement officials to obtain from the contractor a binding price commitment covering as much of the entire program as is practical. Procurement techniques

suggested for accomplishing this were multi-year procurement and options for additional quantities. These techniques are intended to minimize buying-in by eliminating the opportunity for recovering initial losses in follow-on contracts.

Contract definition

One management discipline adopted by DOD to improve the negotiation process for weapon systems is contract definition. It requires that the full implications of a commitment to a particular contractor's product or system be examined prior to commencing full-scale development. This is usually accomplished on the basis of competitive proposals from several contractors that include planning estimates for production, operation, and maintenance of the system as well as firm development commitments. In addition, contract definition provides for verifying technical approaches to a previously approved concept and for developing and refining the system's performance specifications.

Total package procurement concept

The most recent technique adopted by the DOD in major weapon systems acquisition is total package procurement. This concept is still in the experimental stage and has only recently been included in the Armed Services Procurement Regulation. The reason this is called a total package is that the initial award is for as much of the program as can be awarded competitively including spares and support equipment. This is in contrast to the sequential approach wherein following the initial competition, follow-on production and spare parts contracts are frequently individually negotiated with a single company--simply because no other company is in a position to provide realistic competition.

The advantages claimed for this procedure are that the contractor, when competing for the total program, must initially design for economical production, for simplicity and reliability of the operational hardware, and for ease of maintenance since they can greatly influence the total price proposed and source selection. Thus, the use of the total package method of procurement is expected to increase and extend the benefits of technical and price competition over a greater part of the life of the weapon system.

Mr. Chairman, we have not as yet evaluated these and other innovations and procurement disciplines for acquiring major weapon systems. However, because of the importance of this area we are giving it increasing attention and we expect to be in position next year to report to the Congress on some aspects of our work.

SINGLE-SOURCE PROCUREMENT

The third method of procurement, referred to as single-source or sole-source procurement, is perhaps the most controversial since competition is non-existent. Under certain conditions its use may, in fact, be the only practicable method available. At the same time, this method of procurement obviously requires more safeguards in the procurement procedures followed and to avoid its use when competitive forces can be effectively utilized in the Government's interest.

This method is the predominant one from the standpoint that its use usually extends over about one half of total Department of Defense procurement dollars obligated--about $22.8 billion last year. The number of procurement actions involved is much smaller however--about 7 percent.

The most obvious situation which dictates the use of single-source procurement is in follow-on awards to contractors. According to DOD statistics, over one third of single-source procurements in fiscal year 1967 were in the category of follow-on awards after design or price competition.

When a company has been selected to undertake design, development, and production of a new complex weapon system, a considerable period of time and substantial sums of money are usually required to prepare for manufacture and delivery of the system. Except in rare cases where military requirements are so great as to justify establishing more than one source, it would generally delay the defense effort and be uneconomical to attempt to duplicate the time and money required to prepare another source for manufacture and delivery of the same weapon.

Another situation when single-source procurement may be in the best interest of the Government is when the item has been privately developed at the expense of an individual company and the item will satisfy the military's immediate need.

Before concluding our discussion on single-source procurement, it should be recognized that, in the absence of the protection in pricing afforded by the forces of competition, reliance must be placed on the contractor's actual or estimated cost, depending on the type of contracting involved.

For this reason, the Congress in 1962 enacted Public Law 87-653, better known as the "Truth in Negotiations" act. It was designed to safeguard against inflated cost estimates in negotiated contracts and subcontracts over $100,000 by requiring contracting officials to obtain from suppliers cost or pricing data in support of their estimates. It requires also a certification that the data submitted is accurate, complete and current, and provides for an adjustment of prices increased as a result of defective cost data.

We believe that this law serves as a substantial safeguard of the Government's interest in situations where the single-source method of procurement is the most practical one under the circumstances. Practical problems in administering the act are still being worked on by DOD and industry and we intend to assist in this endeavor.

While it is recognized there are circumstances that necessitate the use of sole-source procurement, we believe continuous vigilance must be exercised by procurement personnel to limit its use. Our past work has

shown that the use of competitive procurement procedures can be increased by early break-out of components and spare parts, the prompt acquisition and full use of technical data in the procurement process and early attention to developing requirements. The DOD has programs in these areas which are designed to increase competition in the procurement of such items but continuous surveillance is necessary to assure their full application in the procurement process.

DOD PARTICIPATION IN COST OF CONTRACTORS' INDEPENDENT RESEARCH AND DEVELOPMENT (IR&D)

The policies followed by the Department of Defense (DOD) (and the National Aeronautics and Space Administration (NASA) with respect to participation in the cost of contractors' IR&D also appear to have a significant impact on certain segments of the economy and may lead to further concentration of procurement activities.

The Armed Services Procurement Regulation (ASPR) provides that the cost of a contractor's IR&D activities will be an allowable cost, subject to certain limitations, for distribution as an overhead charge. While the Government does not necessarily absorb the entire allocable amount of such costs, the amount which is absorbed by the Government is significant.

A study now in process within this Office indicates that the cost of IR&D and related technical effort of major contractors in 1966 was $1.1 billion, of which about $500 million was absorbed by DOD. In addition, the NASA share was over $100 million. Thus, the Government share was over $600 million.

A recent report by the National Science Foundation shows that 58 percent of all the industrial research and development (R&D) in 1966 was performed by two industries--aircraft and missiles, and electrical equipment and communication. These two industries together accounted for 83 percent of all Federal R&D funds used by industry during the year. The aircraft and missiles industry performed 86 percent of its R&D work with Federal funds, while the electrical equipment and communication industry performed 61 percent of its R&D work with Federal funds.

Inasmuch as the Government's expenditures for IR&D are made to those companies already engaged in Government contract work, and as the bulk of such work is concentrated in those two industries, it follows that these industries receive the bulk of the IR&D allowances. Consequently, the effect of this practice on competition and concentration in American industry may warrant study.

The Government does not receive rights to patents developed under the contractor's IR&D program. Under the terms of Department of Defense research and development contracts, contractors grant to the Government a royalty free license to use patents developed under such contracts.

PATENT INFRINGEMENT IN COMPETING FOR GOVERNMENT PROCUREMENT

Another problem relating to competitive procurement stems from rights of patent holders.

Section 1498 of title 28, United States Code, relieves Government contractors and their subcontractors of liability for infringing patents embodied in items accepted or to be accepted by the Government pursuant to its contracts. The patent holder's remedy in such cases lies against the Government by an action in the Court of Claims for damages. The legislative history of section 1498 makes it clear that the statute's purpose is to furnish the patent owner an adequate and effective remedy and, at the same time, protect the Government from having its procurements delayed and thwarted while private parties carry on a long drawn-out litigation. In view of section 1498, we have held that the procuring agency must make award to the low responsive responsible bidder under an invitation for bids notwithstanding a protest from a patent holder that his patent would be infringed by performance of the contract. 38 Comp. Gen. 276.

In June 1966, the NASA Administrator questioned whether patent holders were being adequately protected under the existing procedure. He proposed a new approach for the procurement of patented items, a so-called preprocurement license procedure. He proposed that a royalty would be established which would be payable to the patent holder if an item was to be procured from an unlicensed source. The amount of this royalty would be included in the evaluation of bids. That is, in determining the standing of bidders, the amount of the royalty would be added to the

bid prices of the unlicensed supplier. The "preprocurement license" would be applicable only for the single procurement.

In decision B-136916 dated September 12, 1966 (published as 46 Comp. Gen. 205), we approved the adoption of the preprocurement license procedure on a trial basis, as suggested by the NASA Administrator. The Administrator stated to us at the time that he thought the procedure would be applicable only in a limited number of cases in view of the conditions which had to be satisfied for its use. Still, he felt it would serve a salutary purpose, both for the patent owner and for the Government.

The new procedure was put into effect by NASA under a regulation issued October 24, 1966. On March 26, 1968, the NASA Administrator reported to us that the experience so far gained under the preprocurement license procedure had been rather limited, consisting of only four (4) specific requests for such licenses, all of which, for various reasons, were denied. However, he stated there was interest in the procedure in Congress, in industry and in other Government agencies; and therefore he proposed continuing the trial period for at least an additional year, at which time he would present a more complete analysis, including recommendations. We stated that we had no objection to this proposal. (B-136916 dated April 15, 1968).

GAO WORK RESULTING FROM BID PROTESTS

Each year we review several hundred bid protests received from unsuccessful bidders for Government contracts. Many of these protests come to us through congressional channels and concern alleged failures on the part of procurement agencies to follow applicable statutes or regulations in the procurement of goods or services for the Government. Although the bid protests cover the entire range of procurement problems, they frequently deal with the problem of whether or not procurement agencies are obtaining maximum competition under individual procurements, as contemplated by procurement statutes and regulations. Examples of two recent cases follow.

Last year we received a protest that the Air Force, in one of its computer procurements, was not holding negotiations with all offerors on the basis that the offerors had not met certain technical requirements. After a study of the matter we held that the action was contrary to the provisions of Public Law 87-653 and directed that the Air Force reopen negotiations in this procurement. As I previously mentioned, this Law requires that negotiations be conducted with those offerors considered to be within a competitive range. The Air Force subsequently conducted additional negotiations with those offerors previously determined to be within a competitive range. As a result, a contract was awarded to a contractor other than the one originally selected at a net savings estimated by the Air Force to be about $36 million.

In a second case, we reviewed the Army's procurement of anthracite coal for use in Europe, at the request of a member of Congress.

As a result of our review, we concluded that competition sufficiently effective to ensure that the Army was obtaining the coal at the lowest price was lacking. In our report to the Congress, dated June 4, 1968, we stated that these conditions stemmed from (1) the Army's contractual practices which permitted the sources of supply to be limited almost entirely to one exporter which, in turn, procured its coal only from a limited number of anthracite producers and (2) from the use by the Army of unduly restrictive specifications.

Several of the elements of this coal procurement were also the subject of two earlier decisions of our Office issued in response to protests by an association of independent miners. These decisions directed certain changes to be made in the independent price determination clause, in the competition in subcontracting clause, and in other contract clauses. These changes are designed to achieve greater competition in the fiscal year 1969 and future procurements.

Mr. Chairman additional details concerning these 2 bid protest cases are contained in attachment IV to my statement.

GAO PROCUREMENT REVIEWS

From time to time we perform reviews of defense procurement activities which inquire into the extent of competition obtained in particular procurements.

In a report to the Congress last year concerning a Government-wide review by our Office of statutory and regulatory requirements relating to architect-engineer fees, we made certain recommendations, among others, for new legislation and/or regulations to provide competition in the procurement of these services by various Federal agencies, including the Department of Defense.

We found that contracts awarded for architect-engineer services were not being subjected to competitive negotiation procedures whereby proposals are obtained and evaluated in the light of their greatest value to the Government in terms of possible performance, ultimate productibility and other factors, including costs. We believe that the requirements of Public Law 87-653 apply to this type of procurement and hope that the matter can be clarified in the near future.

In the spare parts area we have found over the years that noncompetitive procurements have been made under circumstances where competition could have been obtained. This year we completed a survey in response to the expressed interest of the Subcommittee on Economy in Government, Joint Economic Committee. Our report will soon be released to the Congress and a copy will be provided to your Subcommittee. It shows that, while

DOD has made significant progress, some of the problems identified in our prior work still require management attention.

Over the years probably the greatest hindrance to obtaining competition in the spare parts area has been the problems associated with acquiring, in a timely manner, usable technical data. Our reviews have also shown a need to continually stress the screening of parts and use of available data for competitive procurement.

Additional details concerning the results of our review in these 2 areas are contained in attachment IV to our statement. We have also added as attachment V some comments on defense procurement policies and practices in the areas of small business and subcontracting which may be of interest to you.

Conclusion

As discussed earlier, three separate methods of procurement have evolved. These are formal advertising, competitive negotiation, and single-source negotiation. Each of these methods, when used in appropriate situations, is an acceptable method of procurement.

The Congress shows a continuing interest in the Federal Procurement Process through several of its committees. The House Committee on Armed Services is performing an overall review of military procurement policies, procedures, and practices. In addition, the House Committee on Government Operations introduced and held hearings on a bill to create a Commission on Government Procurement to study procurement problems and make findings and recommendations to the President and to the Congress.

In the hearings on the bill to establish a commission, we testified that our work in the procurement area indicated that there was room for improvement in Government procurement procedures and confirmed the need for a broad across-the-board investigation and study.

We believe that studies and investigations of this nature are desirable and beneficial to both the Government and the business community.

Mr. Chairman this concludes my statement and I will be happy to discuss any of these matters in further detail or answer any questions the Subcommittee may have on our statement.

ATTACHMENTS TO THE

COMPTROLLER GENERAL'S STATEMENT BEFORE

SUBCOMMITTEE ON ANTITRUST AND MONOPOLY

SENATE COMMITTEE ON THE JUDICIARY

ON THE EFFECT OF DEPARTMENT OF DEFENSE

PROCUREMENT OF COMPETITION AND CONCENTRATION

Contents

17. EXCEPTIONS TO FORMAL ADVERTISING UNDER THE LAW

2304. Purchases and contracts: formal advertising; exceptions.

(a) Purchases of and contracts for property or services covered by this chapter shall be made by formal advertising in all cases in which the use of such method is feasible and practicable under the existing conditions and circumstances. If use of such method is not feasible and practicable, the head of an agency, subject to the requirements for determinations and findings in section 2310, may negotiate such a purchase or contract, if--

(1) it is determined that such action is necessary in the public interest during a national emergency declared by Congress or the President;

(2) the public exigency will not permit the delay incident to advertising;

(3) the aggregate amount involved is not more than $2,500;

(4) the purchase or contract is for personal or professional services;

(5) the purchase or contract is for any service by a university, college, or other educational institution;

(6) the purchase or contract is for property or services to be procured and used outside the United States and the Territories, Commonwealths, and possessions;

(7) the purchase or contract is for medicine or medical supplies;

(8) the purchase or contract is for property for authorized resale;

(9) the purchase or contract is for perishable or nonperishable subsistence supplies;

(10) the purchase or contract is for property or services for which it is impracticable to obtain competition;

(11) the purchase or contract is for property or services that he determines to be for experimental, developmental, or research work, or for making or furnishing property for experiment, test, development, or research;

(12) the purchase or contract is for property or services whose procurement he determines should not be publicly disclosed because of their character, ingredients, or components;

(13) the purchase or contract is for equipment that he determines to be technical equipment whose standardization and the interchangeability of whose parts are necessary in the public interest and whose procurement by negotiation is necessary to assure that standardization and interchangeability;

(14) the purchase or contract is for technical or special property that he determines to require a substantial initial investment or an extended period of preparation for manufacture, and for which he determines that formal advertising would be likely to result in additional cost to the Government by reason of duplication of investment or would result in duplication of necessary preparation which would unduly delay the procurement of the property;

(15) the purchase or contract is for property or services for which he determines that the bid prices received after formal advertising are unreasonable as to all or part of the requirements, or were not independently reached in open competition, and for which (A) he has notified each responsible bidder of intention to negotiate and given him reasonable opportunity to negotiate; (B) the negotiated price is lower than the lowest rejected bid of any responsible bidder, as determined by the head of the agency; and (C) the negotiated price is the lowest negotiated price offered by any responsible supplier;

(16) he determines that (A) it is in the interest of national defense to have a plant, mine, or other facility, or a producer, manufacturer, or other supplier, available for furnishing property or services in case of a national emergency; or (B) the interest of industrial mobilization in case of such an emergency, or the interest of national defense in maintaining active engineering, research, and development, would otherwise be subserved; or

(17) negotiation of the purchase or contract is otherwise authorized by law.

17 CONDITIONS CITED IN ASPR FOR USE OF EXCEPTION WHEN IMPRACTICABLE TO USE FORMAL ADVERTISED PROCUREMENT

(i) when supplies or service can be obtained from only one person or firm ("sole source of supply");

(ii) when competition is precluded because of the existence of patent rights, copyrights, secret processes, control of basic raw material, or similar circumstances (however, the mere existence of such rights or circumstances does not in and of itself justify the use of the authority of this paragraph);

(iii) when bids have been solicited pursuant to the requirements of Section II, and no responsive bid (a responsive bid is any bid which conforms to the essential requirements of the solicitation) has been received from a responsible bidder, or when step one of two-step formal advertising results in no acceptable technical proposal or only one acceptable technical proposal;

(iv) when bids have been solicited pursuant to the requirements of Section II, and the responsive bid or bids do not cover the quantitative requirements of the solicitation of bids, in which case negotiation is permitted for the remaining requirements of the solicitation of bids;

(v) when the contemplated procurement is for electric power or energy, gas (natural or manufactured), water, or other utility services or when the contemplated procurement is for construction of a part of a utility system and it would not be practicable to allow a contractor other than the utility company itself to work upon the system;

(vi) when the contemplated procurement is for training film, motion picture productions, or manuscripts;

(vii) when the contemplated procurement is for technical nonpersonal services in connection with the assembly, installation or servicing (or the instruction of personnel therein) of equipment of a highly technical or specialized nature;

(viii) when the contemplated procurement is for studies or surveys other than those which may be negotiated under 3-205 or 3-211;

(ix) when the contemplated procurement involves construction, maintenance, repairs, alterations or inspection, in connection with any one of which the exact nature or amount of the work to be done is not known;

(x) when the contemplated procurement is for stevedoring, terminal, warehousing, or switching services, and when either the rates are established by law or regulation, or the rates are so numerous or complex that it is impracticable to set them forth in the specifications of formal solicitation of bids;

(xi) when the contemplated procurement is for commercial transportation, including time, space, trip, and voyage charters, except for such transportation services as are furnished by common carriers (for which negotiation is authorized under 3-217, and Section 321 of the Transportation Act of 1940, 49 U.S.C. 65), and including services for the operation of Government-owned vehicles, vessels or aircraft;

(xii) when the contract is for services related to the procurement of perishable subsistence such as protective storage, icing, processing, packaging, handling, and transportation, whenever it is impracticable to advertise for such services a sufficient time in advance of the delivery of the perishable subsistence;

(xiii) when it is impossible to draft, for a solicitation of bids, adequate specifications or any other adequately detailed description of the required supplies or services;

(xiv) when, under the procedures set forth in Joint Regulation DOD 4145.16, AR 743-455, NAVSANDA PUB 297, AFR 67-61 and NAVMC 1133, the contract is for storage (and related services) of household goods;

(xv) when the contemplated procurement is for parts or components being procured as replacement parts in support of equipment specially designed by the manufacturer, where data available is not adequate to assure that the part or component will perform the same function in the equipment as the part of component it is to replace;

(xvi) when the contract is a facilities contract as defined in 13-101.11 and the performance required can be obtained from only one person or firm; or

(xvii) when the contemplated procurement involves construction where a contractor or group of contractors is already at work on the site, and it would not be practicable to allow another contractor or an additional contractor to work on the same site or when the amount is too small to interest other contractors to mobilize and demobilize.

ATTACHMENT III

REPORTING OF NONCOMPETITIVE PROCUREMENT ACTIONS AS COMPETITIVE

We found that a number of procurement actions that were classified and reported as competitive were awarded, in our opinion, under noncompetitive conditions. These actions consisted of those valued at $2,500 and under and some over that amount. Our work showed that these misclassifications were caused by inadequate criteria in the Armed Services Procurement Regulation, by the manner in which the Regulation was applied, and by the format of procurement actions reports. We felt that the Regulation needed revision to provide additional guidance to contracting officers for classifying and reporting of negotiated procurement actions.

In September 1967 the Department of Defense issued revised instructions which should improve the reporting of negotiated procurement actions. These revised instructions were incorporated into the ASPR this February.

Among the more important changes in determining whether price competition existed in procurements in excess of $2,500 is generally that at least two offers should be received from responsible offerors capable of satisfying the Government's requirements. In the past, one offer could be classified as competitive as long as two or more bids had been solicited.

The changes still permit a situation to be reported as competitive when one offer is received after soliciting two or more firms who normally contend for the same or similar items. However, contracting officers are required to exercise sound judgment in evaluating the relevant information in reporting a transaction as price competitive.

Through the first quarter of fiscal year 1968, all procurements of $2,500 or less were reported as competitive. Now, however, as a result of the revised instructions, these small purchases are to be reported as noncompetitive unless it is economically feasible to record and tabulate the price competition status of such actions. As can be seen from the figures below, the revised DOD reporting system is beginning to reflect this new criteria.

1968:	Total Small Purchases (millions)	Reported as Competitive (millions)	Reported as Competitive (Percentage)
1st Quarter	$350.5	$350.5	100%
2nd Quarter	368.6	186.7	56.1%
3rd Quarter	393.9	159.2	40.4%

ATTACHMENT IV

GAO WORK IN AREAS OF COMPETITIVE PROCUREMENT RESULTING FROM BID PROTESTS AND PROCUREMENT REVIEWS

Following are several cases involving past and current GAO work in areas of competitive procurement which resulted from either bid protests received from private companies or reviews initiated by our Office.

Each year we receive several hundred bid protests from unsuccessful bidders for Government contracts, principally smaller companies. The review of bid protests is one of the important but not well known functions of our Office of direct concern to taxpayers generally and to business in particular.

The protests concern alleged failures on the part of procurement agencies to follow applicable statutes or regulations in the procurement of goods or services for the Government. Although the bid protests cover the entire range of procurement problems, they frequently deal with the problem of whether the procurement agencies obtain maximum competition as contemplated by the procurement statutes and regulations. A recent case follows.

Need for further negotiation under Air Force computer procurement

In a decision dated July 14, 1967, the Air Force was directed to reopen negotiations in a computer procurement. We held that elimination

without further negotiation of an otherwise qualified offeror for failure to reach certain technical requirements was contrary to the provision of 10 U.S.C. 2304(g). This provision requires that negotiations be conducted with all offerors within a competitive range including consideration of technical capability as well as price.

Following our decision, the Air Force issued an amended request for proposals, conducted additional negotiations with those offerors previously determined to be within a competitive range, and awarded a contract to a company other than the one originally selected. The Air Force estimates the net savings of the recompetition at about $36 **million after deducting about $18 million for an eight-month delay in rebidding of the contract.**

This decision had the beneficial result of promoting competition by allowing all offerors the opportunity to show that they could meet the Air Force needs with minor modifications of their respective technical approaches.

It occasionally occurs that although our decision in a particular case sustains the protest, we are unable to authorize effective relief because of practical considerations such as status of performance or urgency of the procurement. However, our decisions even in these cases do have a beneficial effect in the form of directives to the agencies involved that practices not in accord with procurement statutes and regulations should not be repeated in future procurements. The coal procurement for Europe to be discussed next is a case in point.

Restrictive competition in coal procurement for Europe

We recently had occasion to consider both from an economical and legal standpoint the methods used by the Department of the Army in its annual procurement of domestic anthracite coal for use at European bases. As a result of a request from Congressman George M. Rhodes of Pennsylvania, a review of this procurement was performed resulting in our audit report, B-159868, released this month to the Congress. Also, bid protests concerning the contracts for fiscal years 1968 and 1969 were filed by a group of independent coal miners who maintained that the request for proposals issued by the Army for the fiscal year 1968 coal procurement was restrictive of competition.

The background of this procurement, the findings contained in our audit report, and our decisions in the bid protest cases are briefly summarized below.

Prior to fiscal year 1962, the solid fuel requirements of the United States Armed Forces were met by procuring European coke and coal. However, in response to a presidential directive dated November 16, 1960, concerning steps to be taken to improve the United States balance of payments, the Army decided to obtain its solid fuel requirements for military installations in Germany from United States sources.

From fiscal year 1962 through fiscal year 1967, the Army awarded contracts totaling about 4.5 million metric tons of United States anthracite coal at a total cost of about $102 million. The coal was mined in Pennsylvania and shipped to Europe for use at various military installations.

In buying the coal, the Army negotiated with and awarded firm fixed-price contracts to European importers. The European importers obtained the coal from American exporters who, in turn, procured it from various coal sources in Pennsylvania.

The major anthracite suppliers had formed an association called the Anthracite Export Association and, under the provisions of the Webb-Pomerene Act, had entered into agreements among themselves to set prices and allocate quantities of coal for export and ultimate sale to the Army. The Webb-Pomerene Act provides immunity from the antitrust statutes in the case of associations entered into for the sole purpose of engaging in export trade. Incidentally, the question of whether or not Webb-Pomerene immunity attaches to the anticompetitive practices of the association in supplying coal to the Army is presently before the United States District Court for the Middle District of Pennsylvania. We have been advised, however, that it will be several months before a decision is issued.

It has been the general practice of the members of the Anthracite Export Association to offer their coal only to a certain export corporation. Further, that corporation has advised us that its practice has been to purchase coal only from members of the Anthracite Export Association. However, the majority of the 28 firms that are qualified to meet the Army's specifications, that is, the smaller producers, are not members of this association. Our review showed prices quoted by some of these firms to be lower than prices charged by the association's members. Further, this exporter has conditioned its quotations to importers on their purchasing all of their requirements for the Army procurement from it.

In this regard a bid protest was filed by the independent coal companies. The protestants alleged generally that price fixing and allocation of shares of coal to be supplied to the Army by the association were

in violation of the Armed Services Procurement Act and Regulation. This act and regulation require that negotiated procurement be on a competitive basis to the maximum practicable extent.

In our investigation of the protest, we found that the Army had inserted clauses requiring certificates of independent price determination and competition in subcontracting in requests for proposals for fiscal year 1967 and 1968 coal procurements.

These clauses had been worded in such a way, however, that the price fixing and allocation practices of the Association were permitted because it was believed by the Army that such practices were sanctioned by the Webb-Pomerene Act. We found also that, in compliance with the specially worded independent price certification clauses contained in the fiscal years 1967 and 1968 requests for proposals, statements had been submitted by the Association admitting price fixing and share allocations.

Our decision of November 7, 1967, sustained the protest on the basis that the Armed Services Procurement Regulation and the procurement statute prohibit these practices whether or not they are permitted under the anti-trust laws. Although practical considerations precluded us from disturbing the fiscal year 1968 contract, we directed that future requests for proposals contain clauses designed to ensure that effective competition is present at all levels of the procurement.

In acknowledging our November 7, 1967, decision the Army advised us that effective with the fiscal year 1969 coal procurement it would not permit prime contractors or subcontractors to claim exemption under the Webb-Pomerene Act.

Another aspect of this procurement which tended to reduce competition was that the Army established certain specifications for the coal which appeared to exceed its minimum needs. For example, the Army requires that the ash content of the coal not exceed 9.75 percent. Bids from importers whose sources were not certified by the Bureau of Mines as being able to meet this specification were rejected as nonresponsive. However, we found that in fiscal years 1965 and 1966 about 50 percent of the coal shipped to and accepted by the Army exceeded the 9.75 percent ash content requirement, and that in fiscal year 1967 in one instance an equitable price adjustment was obtained for high ash content coal.

As a result of a request by the independent coal companies for reconsideration and amplification of our November 7 decision, a supplemental decision was issued on April 18, 1968. The supplemental decision again stated that price fixing and share allocation should be precluded, and concluded that the November 7 decision should be fully implemented by redrafting the competition in subcontracting clause to require that all otherwise responsible suppliers be solicited without regard to any exclusive agency or franchise arrangements between suppliers and exporters, and to preclude the insertion of exclusive purchase conditions by exporters in their offers to prime offerors. The decision also concluded that any concerted refusals on the part of the Association coal suppliers to deal with exporters other than their customary exporter should be precluded by appropriate RFP language if the Army finds that such practices are or have been engaged in.

Additionally, in response to a request by the Army for our opinion, the decision agreed with the Army that noncompetitive discounts offered in the past by prime contractors having access to Association coal tend to restrict competition and therefore should be rejected, and suggested that a provision to that effect inserted in the fiscal year 1969 RFP be redrafted to more clearly indicate what kind of discounts will not be accepted. Finally, the decision strongly suggested that high ash content coal be accepted under the fiscal year 1969 contract on the basis of an adjustment formula.

As a result of our April 18 decision, the Army amended its fiscal year 1969 request for proposals to conform to the requirements for increased competition outlined above, including the relaxation of the ash content specification from 9.75 percent to 11.00 percent.

We believe that this action by the Army should bring about more economical and equitable coal procurements.

Need for increased competition in procurement of architect-engineer services

In a report to the Congress last year concerning a Government-wide review by our Office of statutory and regulatory requirements relating to architect-engineer fees, we made certain recommendations, among others, for new legislation and/or regulations to provide competition in the procurement of these services by various Federal agencies, including the Department of Defense.

We noted that the procedures followed by Federal agencies in the selection of contractors for architect-engineer services did not comply

with the requirements of Public Law 87-653 and related regulations. With certain exceptions, these requirements provide that, in all negotiated procurements in excess of $2,500, proposals be solicited from the maximum number of qualified sources consistent with the nature and requirements of the supplies or services to be procured and that written or oral discussions be conducted with all responsible offerors who submit proposals within a competitive range, price and other factors considered.

Although most of the construction agencies of the Government are subject to this requirement, they generally solicit a proposal only from the architect-engineer firm selected on the basis of technical ability. In our opinion, this does not comply with the statutory requirement.

Agency representatives advised us that they are opposed to the concept of soliciting multiple competitive proposals. The Department of Defense advised us that it believes that its present selection procedures constitute the maximum competition consistent with the nature and requirements of the services being procured. The Department also stated that, until the architect-engineer community demonstrates that it is prepared to countenance competition on price as well as on other factors, the Department, believing that it is complying with the provisions of law, would intend to proceed as before.

The architectural and engineering professional societies are also opposed to the concept of soliciting multiple competitive proposals. They expressed the belief that (1) the legislative history of Public Law 87-653 constituted substantial ground for concluding that the competitive negotiation requirements of the act were not intended to apply to architect-

engineer services and (2) in view of the expertise inherent in contracts for professional architect-engineer services and the individualized character of such services, it would be incompatible with the nature of the services to apply the requirements of the statute.

There is some basis for the position that the language of the statute which requires that competitive negotiations "shall be consistent with the nature and requirements of the supplies or services to be procured" justifies the procedures presently being followed. These procedures are also based on well-established methods of doing business with architect-engineers. However, we find no statutory basis which would exempt architect-engineer contracts.

In amplifying our position, we have pointed out that the "competitive negotiation" contemplated by Public Law 87-653 is clearly distinguishable from "competitive bidding" or price competition under the formal advertising for bids statutes. While the rigid rules applicable to formally advertised procurements generally require award to the lowest (price) responsive, responsible bidder, the flexibility inherent in the concept of negotiation permits an award to be made to the best advantage of the Government, "price and other factors considered." Negotiation permits, and indeed requires, the contracting officials of the Government to consider these "other factors" of the procurement, which in a proper case, may result in an award to one offeror as opposed to another less qualified offeror submitting a lower price. The award of an A-E contract may and properly should be influenced by a proposal which promises the greatest

value to the Government in terms of possible performance, ultimate producibility and other factors, including cost, rather than the proposal which merely offers the lowest price or probable cost and fixed fee.

We believe that competitive negotiation can be applied to the procurement of A-E services without adversely affecting the quality of the services to be furnished. Such a procedure would afford reasonable assurance that the Government would receive the best possible professional services, both from a design and price standpoint. Other professionally-oriented procurements, such as for management consultant services, for research and development, and for sophisticated and technically-advanced weapons or aerospace systems are accomplished successfully and without complaint by competitive negotiation. We find it difficult to see why A-E services cannot be obtained by the same method. In short, the justification for excluding the A E profession as a class from competitive negotiation requirements and at the same time subjecting without question or reservation other comparable services to these requirements is not apparent.

The questions involved in this matter are, in the final analysis, for resolution by the Congress. We, of course, have given thorough consideration to the views expressed by the Chairman of the Government Activities Subcommittee in his letter of November 16, 1967. In addition we have had discussions with the Chairman of the Senate Committee on Government Operations who presently has the matter under consideration.

Competitive procurement of spare parts

In the spare parts area, we have found over the years that noncompetitive procurements have been made under circumstances where competition could have been obtained. Beginning in 1961 we reported to the Congress on a review of aeronautical spare parts procurement within the Department of Defense. On the basis of a follow-up review, several reports were issued on the same subject during 1963.

These reports showed that the principal reason for noncompetitive procurement was the lack of adequate technical data. The reports pointed out the need for securing prompt replacements for illegible data, for determining the validity of restrictive legends placed on data by contractors, and for adequate procedures for receiving, storing, and controlling the data obtained. In addition, the reports included instances where the military services had not obtained competition when sufficient technical data were available.

This past year we completed a survey in this area. We performed this survey in response to the expressed interests of the Subcommittee on Economy in Government, Joint Economic Committee and the results of our work were discussed extensively in hearings before that Subcommittee in May and November 1967.

While DOD has made significant progress, our survey showed that some of the problems identified in our prior work still required management attention. Our report will soon be released to the Congress and a copy will be provided to this Subcommittee.

Our report to the Congress concerns:

1. Reporting of Noncompetitive Procurement Actions as Competitive (details are contained in Attachment III)

2. The High-Dollar Spare-Parts Breakout Program

3. Use of Technical Data

4. Uniform Reporting System

The last three areas having to do with management of competitive procurement of spare parts are discussed separately in the sections that follow.

High-Dollar Spare-Parts Breakout Program

The purpose of the Spare-Parts Breakout Program is to achieve savings for the Government through competitive procurement or direct procurement from the manufacturers of replacement spare parts rather than through the weapon systems supplier. The selection of parts is based on projected annual buys, with highest priorities being assigned to those items having the highest annual procurement values so that management attention is directed to those parts which represent the most procurement dollars.

Our latest evaluation showed that there was a need for the Department of Defense and the military services to continue to direct attention to the implementation of the Breakout Program in order to achieve increased competition. The following example shows the savings attainable when the Breakout Program procedures for reviewing the procurement history of an item are applied.

> The Army had been procuring replacement windows for the HU-1 helicopter directly from the aircraft manufacturer without obtaining competition. Last year the Army broke this item away from the aircraft manufacturer and awarded a contract for the windows on a competitive basis. As a result, we estimate that a saving of about $2 million will be realized on current and future procurements in meeting program requirements for the helicopter windows.

In October 1967 we were advised by the Department of Defense of actions being taken to improve the Breakout Program. Regarding the timely screening of spares and repair parts, the Department plans to revise its regulations to incorporate certain practices that have been developed since the program was initiated. Also, the Department proposes to emphasize the importance of beginning the screening process when spares and repair parts are first brought into the inventory and replenishment requirements can be estimated with reasonable accuracy.

Use of technical data

Our recent survey covered fiscal year 1966 aeronautical spare parts procurements totaling about $2 billion. An estimated $1.5 billion or 78.5 percent, represented noncompetitive procurements. Of the $174 million of noncompetitive procurement actions we reviewed, about $103 million worth, or 59 percent, were not awarded competitively due to various technical data problems.

Although the number of specific cases included in our survey was limited, they did highlight the existence of basic management problems such as:

1. The need to screen parts to determine whether adequate data are available for competitive procurement.

2. The need to use available technical data.

3. The need for better coordination and communication among the services in resolving contractors' claims that data are proprietary.

4. The need for interservice utilization of technical data on parts common to more than one service.

The following example illustrates the need to screen parts and use available data.

> In March 1966 the Army awarded a sole-source contract to a prime contractor for 879 filters valued at almost $150,000. The contracting officer justified the sole-source award on the basis of its being impossible to draft either adequate specifications or an adequately detailed description of the part within the time frame of this procurement.
>
> Our review at the data depository in May 1966 disclosed that adequate technical data to support a competitive procurement were on hand at the time of the sole-source award; however, the Army had not determined whether the data were available or complete. When we advised the contracting officer that data were available, he cancelled the contract and solicited three companies, two of which responded. In August 1966 a competitive award, valued at about $81,000, was made at a saving of about $69,000.

Uniform reporting system

Our survey work showed that, although information for identifying the reasons for noncompetitive procurement is available under each service's implementation of the Breakout Program, the methods for classifying the reasons are not uniform among the services. Also, the specific reasons are not summarized and reported to higher management levels in the services and the Department of Defense.

We have been informed that the Department of Defense, for some time, has been examining into the feasibility of assigning uniform codes for indicating the reasons for noncompetitive procurement. Recently, the Director, Defense Supply Agency, has been asked to include this additional information in the data bank of the Defense Logistics Service Center so that it will be available to procuring agencies. The Center will also provide periodic reports that will enable management to identify those areas of noncompetitive procurement requiring particular attention.

Defense Procurement Policies and Practices - Small Business and Subcontracting

Small Business

Congress has legislated that a fair proportion of the total purchases and contracts for supplies and services for the Government shall be placed with small business concerns in order to preserve free competitive enterprise. Neither the laws nor the Armed Services Procurement Regulation sets out criteria for determining when a fair proportion is obtained; however, recent statements by the Congress and the President show that they consider a greater participation by small firms to be desirable. In addition, Congress, in order to obtain full employment of the Nation's manpower, encourages the placing of contracts and facilities in areas of persistent or substantial labor surplus.

DOD has established various programs designed to attract greater participation by small business and labor surplus area firms in bidding on Government contracts and on subcontracts under Government contracts held by large business firms. Also, in accordance with the laws, DOD sets aside procurements in whole or in part for exclusive small business or labor surplus area firm participation whenever it is practical to do so.

Department of Defense reports show that, of total awards to all firms in FY 1967, small business firms got $6.45 billion, or about 16 percent, by bidding against large business firms plus another $1.9 billion, or about 4.6 percent, by means of the preferential set-aside procedures. Defense-wide,

about $29 million in set-aside awards were made to labor surplus area firms during the first 6 months of FY 1967. The amount of subcontracts to small business firms under Government contracts held by large business firms is estimated by DOD at about $6.7 billion.

Subcontracting

A large proportion of the procurement dollar is spent by prime contractors in subcontracting for work, raw materials, parts, and components. Basic responsibility rests with the prime contractor for decisions to make or buy, for selection of subcontractors, and for subcontract prices and subcontract performance. However, the contracting officer in evaluating contractors' price proposals where competition is lacking, is expected to have adequate knowledge of these elements. Where appropriate, he must inquire into the contractor's purchasing system, the principal components to be subcontracted, the degree of competition obtained, the price or cost analysis performed, types of subcontracts, and extent of subcontract supervision. For subcontracts over $100,000, compliance with the requirements of Public Law 87-653 for certified cost or pricing data is necessary where competition is lacking.

Certain prime contracts of a cost-type nature include a subcontract clause which provides for contracting officers' review and consent to individual subcontracts. This clause requires that prime contractors furnish certain information to contracting officers prior to their approval of the subcontract. In reviewing the proposed subcontract for the purpose of granting consent, the contracting officer is required to consider, among

other things, the basis for selecting the proposed subcontractor, including the price competition obtained.

For certain of the larger Government contractors the contractor's purchasing system may be approved by the contracting officer. Where a system has been approved, the contracting officer's consent to the award of individual subcontracts is generally not required. Approval of a contractor's purchasing system is granted only after the contracting officer has made a review of several factors, including the degree of competition obtained in subcontracting.

In regard to the Defense Department's small business and labor surplus area programs, it is the stated policy of the Department of Defense to promote equitable opportunities for small business and labor surplus area concerns to compete for defense subcontracts and to encourage prime contractors to place subcontracts with small business and labor surplus area concerns where this can be done, consistent with efficient performance of contracts. To this end, contracts over $5,000 generally contain clauses whereby the contractor agrees to award the maximum amount of his subcontracting to small business and labor surplus area concerns whenever it is consistent with the efficient performance of the contract.

In contracts over $500,000 the contractor is required by various contract clauses to undertake a number of specific responsibilities designed to assure that small business and labor surplus area concerns are considered fairly in the subcontracting role and to impose similar responsibilities on major subcontractors.

In order to broaden the opportunity in negotiated procurement for subcontracting by small business concerns and others, contracting officers are required to publish in the Commerce Business Daily the names and addresses of firms to whom requests for proposals are to be issued, unless the Government's best interests would not be served by so doing or that the subcontracting opportunities did not exist. This procedure is designed to offer opportunity to small business concerns and others interested in subcontracting to make direct contact with prospective prime contractors at an early stage in the procurement. In addition, prime contractors and subcontractors are encouraged to use the Commerce Business Daily to publicize opportunities in the field of subcontracting stemming from their defense business.

GAO work in small business and labor surplus areas

We have completed the preliminary phase of a survey into DOD's implementation of the national policies for small business and labor surplus area concerns. The major emphasis of our examination was directed to DOD's programs for setting aside procurements for exclusive participation by small business and labor surplus area concerns. As a result of our observations to date, we plan to conduct reviews into (1) DOD procedures which tend to limit awards to small business and (2) pricing of the set-aside portion of partial set-asides in relation to prices paid on the nonset-aside.