DEFENSE CONTRACTS

DOD’s Requests for Information from Contractors to Assess Prices

Accessible Version
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Why GAO Did This Study

DOD usually relies on competition to ensure it pays a reasonable price for supplies or services. For noncompetitive contracts, DOD relies on other methods for determining price reasonableness, such as information from previous contracts or from the contractor. For commercial items, there are limits on the types of data that may be requested from contractors.

Section 831 of the National Defense Authorization Act for Fiscal Year 2013 required DOD to issue guidance and provide training related to the information contracting officers may request to determine the reasonableness of contract prices. The act also included a provision for GAO to review contracts awarded between January 2013 and January 2015 and report on the extent DOD needed cost data from the contractors to assess the reasonableness of prices.

This report addresses (1) DOD’s actions to develop guidance and training on determining price reasonableness, and (2) circumstances under which DOD requested contractor cost or pricing information for determining prices.

What GAO Found

The Department of Defense (DOD) is taking several steps to develop guidance and training related to determining the reasonableness of prices. First, DOD issued a policy memo to provide guidance to contracting officers on the determination of price reasonableness for commercial items. Second, DOD plans to revise the Department of Defense Federal Acquisition Regulation Supplement (DFARS) and provide guidance to contracting officers on requesting cost or pricing information from contractors. DOD published the proposed rule for public comment in early August 2015. Third, DOD is developing training to complement the guidance and is establishing a cadre of cost and pricing experts to assist contracting officers. Since the guidance, regulation, and training plans have not been implemented, it is too early to determine the effectiveness of these initiatives on determining the reasonableness of proposed prices.

DOD contracting officials requested cost or pricing information from contractors to determine the reasonableness of proposed prices. Specifically, officials requested cost data, such as information on the cost of materials or labor, for 6 of the contracts reviewed and requested only pricing information, such as sales invoices, for 6 contracts. The contracts GAO reviewed showed that officials requested information for a variety of reasons. In some cases, officials requested information because the contractor’s proposal was incomplete. In other cases, officials determined that the information on hand was inadequate for purposes of assessing prices.

Contractors did not always provide all of the requested information, but contracting officials were able to use the available information to conclude that the prices paid were fair and reasonable. For 20 contracts, officials did not request any contractor information to determine price reasonableness. Officials determined the prices fair and reasonable based on information already available to the government, such as prices paid on previous contracts. Overall, GAO found that contracting officials faced challenges when determining price reasonableness, such as data currency and contractor reluctance to share data.

What GAO Recommends

GAO is not making recommendations. In written comments, DOD stated the report would assist the department’s implementation of Section 831.

Contractor Information Requested by the Department of Defense to Determine Price Reasonableness for Contracts GAO Reviewed

20 Requests for information from the contractor
12 Requests for both cost and pricing information
6 Requests for pricing information only
0 No requests for information from the contractor

Source: GAO analysis of DOD contracts. | GAO-15-680

August 2015

For more information, contact William T. Woods at (202) 512-4841 or woodsw@gao.gov.
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Abbreviations

AT&L  Office of the Undersecretary of Defense, Acquisition Technology and Logistics
DAU  Defense Acquisition University
DCAA Defense Contract Audit Agency
DCMA Defense Contract Management Agency
DFARS Department of Defense Federal Acquisition Regulation Supplement
DLA  Defense Logistics Agency
DOD  Department of Defense
FAR  Federal Acquisition Regulation
FPDS-NG Federal Procurement Data System—Next Generation
GSA  General Services Administration
NDAA National Defense Authorization Act

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August 12, 2015

Congressional Committees

The Department of Defense (DOD) usually relies on price information generated in a competitive market to help ensure that it is paying a reasonable price for supplies or services. A significant portion of DOD’s contracts, however, are awarded noncompetitively. In fiscal year 2014, DOD awarded about $119 billion (42 percent of total contract obligations) on noncompetitive contracts. In the absence of multiple offers, DOD relies on a variety of methods for determining the reasonableness of prices including reviewing prices paid previously for the same item, market research, or, under certain conditions, an analysis of cost or pricing data provided by contractors. For commercial items, laws and regulations limit the types of data that may be requested from contractors to determine a fair and reasonable price.

Section 831 of the National Defense Authorization Act (NDAA) for Fiscal Year 2013 required that DOD issue guidance and provide training on the use of cost or pricing information to determine the reasonableness of contract prices.¹ The NDAA also included a provision for us to report on DOD’s collection of cost data to assess the reasonableness of contract prices during the 2-year period from January 2013 through January 2015. This report addresses (1) the status of DOD’s actions to develop guidance and training on determining price reasonableness, and (2) circumstances under which DOD requested cost or pricing information from contractors for use in determining price reasonableness for noncompetitive contracts for commercial items awarded between January 2, 2013 and January 1, 2015.

To determine the status of DOD’s actions to develop guidance and training on determining price reasonableness, we obtained documents and interviewed DOD officials from the Office of the Undersecretary of Defense Acquisition Technology and Logistics (AT&L), Defense Contract Management Agency (DCMA), Defense Contract Audit Agency (DCAA), and Defense Acquisition University (DAU).

¹Pub. L. No. 112-239 § 831.
To address circumstances under which DOD requested cost or pricing information from contractors for determining price reasonableness, we used the Federal Procurement Data System-Next Generation (FPDS-NG) to select a nongeneralizable, random sample of 32 DOD contracts for commercial items that were awarded noncompetitively or which received only one offer from four DOD agencies—Air Force, Army, Navy, and Defense Logistics Agency (DLA)—eight contracts from each agency. These agencies had the highest dollar value of contracts awarded during the 2-year period specified in the mandate. We analyzed data from the contract files to identify the types of information used to determine price reasonableness. According to DOD officials, DOD does not track requests to contractors for cost or pricing information. We determined that the FPDS-NG data were sufficiently reliable for our purposes by comparing the data reported in FPDS-NG, such as the contract number and award value, to information in the selected contract files and by conducting electronic tests of the data. For additional details about our scope and methodology, see appendix I.

We conducted this performance audit from February to August 2015 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

The Federal Acquisition Regulation (FAR) requires that before purchasing supplies and services, contracting officers must determine that the prices proposed by contractors are fair and reasonable. Two statutes, 10 U.S.C. sections 2306a and 2379, describe circumstances when certain types of data are required to be obtained to support this determination, as well as exceptions that apply. In addition, the FAR and the Department of Defense Federal Acquisition Regulation Supplement (DFARS) provide additional guidance about the data that should be obtained in various circumstances. Generally, the data that contracting officers examine to determine the reasonableness of price depend on a series of circumstances including whether the particular contract is for a

\(^2\)FAR Subpart 15.4 and DFARS Part 215.
commercial or noncommercial item. The data examined could be cost data, such as the cost of materials, labor, and overhead, or pricing information, such as invoices for the same or similar items sold to commercial customers.

### Authority and Regulations

#### Governing Assessments of the Reasonableness of Price

The authority of contracting officers to collect cost or pricing data to determine price reasonableness is contained in 10 U.S.C. section 2306a, which is applicable to most awards; and section 2379, which is specific to the purchase of major weapon systems, subsystems, components or spare parts purchased as commercial items.\(^3\) Section 2306a states that the contractor for a proposal over a threshold (currently $700,000) will be required to submit certified cost or pricing data before an award unless an exception applies.\(^4\)

Exceptions to submitting certified cost or pricing data include contracts

- based on adequate price competition,
- where price is set by law or regulation,
- below the simplified acquisition threshold (generally $150,000),
- for which certified cost or pricing data are waived in writing by the head of the procuring activity, and

\(^3\)Under 10 U.S.C. § 2379, major weapons systems may only be treated as commercial items if, among other things, the offeror has submitted sufficient information to evaluate, through price analysis, the reasonableness of the price for such system. Under this statute, the contracting officer may obtain price information as well as information regarding the basis for price or cost, including information on labor and material costs. We did not find instances of the use of the authority provided by section 2379 in the contracts we reviewed. Major defense acquisition programs are those identified by DOD with a dollar value for all increments estimated to require eventual total expenditure for research, development, test, and evaluation of more than $480 million, or for procurement of more than $2.79 billion, in fiscal year 2014 constant dollars.

\(^4\)Certified cost or pricing data means cost or pricing data that were required to be submitted in accordance with the FAR have been certified, or are required to be certified. The certification states that to the best of the person’s knowledge and belief the cost or pricing data are accurate complete, and current as of a date certain before contract award. FAR § 2.101.
• for the acquisition of commercial items.\(^5\)

When an exception applies, such as where prices are based on adequate price competition, contracting officers generally do not have to request data from the contractor to determine the reasonableness of price. However, if the contracting officer determines that data are needed to determine the reasonableness of the price offered, the FAR encourages contracting officers to first collect current pricing information available within the government such as catalogs, the results of market research, or recent sales. If the reasonableness of the proposed prices cannot be determined from this information, contracting officers may obtain data other than certified cost or pricing data from the contractor to the extent necessary to determine a fair and reasonable price.\(^6\) At a minimum, unless certain exceptions apply, the submitted data should include information on the prices at which the same or similar items have previously been sold that is adequate for evaluating the reasonableness of the price.

Once contracting officers obtain the data needed, there are basically two analytical techniques they can use—singly or in combination—to determine price reasonableness. Because the complexity and circumstances of each acquisition influences the level of analysis needed, the FAR provides contracting officers discretion in deciding how to determine price reasonableness. The two techniques include:

• **Price analysis:** the process of examining and evaluating a proposed price without evaluating its separate cost elements and proposed profit. Information used in this analysis may include sales invoices or

\(^5\) The FAR definition of a commercial item includes any item other than real property that is of a type customarily used by the general public or by non-governmental entities for purposes other than governmental purposes and has been sold, leased, or licensed to the general public or has been offered for sale, lease, or license to the general public. See FAR § 2.101 for the full definition of the types of items and services that can be considered to be commercial.

\(^6\) As defined in FAR § 2.101, data other than certified cost or pricing data means pricing data, cost data, and judgmental information necessary for the contracting officer to determine a fair and reasonable price or to determine cost realism. This data could be the same as certified cost or pricing data, but without the accompanying certificate. Because of the nature of our sample of 32 commercial contracts, all of the data requested from the contractors qualifies as data other than certified cost or pricing data, as defined in FAR § 2.101. In our report, when we use the term “cost or pricing data,” we are referring to this data.
other sales data that show the price for which the same or similar items have been sold and previous contracts where prices were determined fair and reasonable.

- **Cost analysis**: the review and evaluation of any separate cost elements and profit or fee in a contractor’s proposal and the application of judgment to determine how well the proposed costs represent what the cost of the contract should be, assuming reasonable economy and efficiency. Information used in this analysis may include actual costs for materials, direct labor, indirect labor, and overhead.

### Recent Legislation

Section 831 of the NDAA for Fiscal Year 2013 required DOD to issue guidance on the use of the authority granted under 10 U.S.C. sections 2306a(d) and 2379 to include standards for determining:

- whether pricing information on the price that the same or similar items have previously been sold is adequate for evaluating the reasonableness of price, and
- the extent of uncertified cost information that should be required in cases in which price information is not adequate for evaluating the reasonableness of price.

The NDAA further provided that the guidance should ensure that this cost information be provided in the form in which it is maintained by the offeror and that cost information should not be required by DOD where there are sufficient non-government sales to establish reasonableness of price.

The act mandated that requests for this cost information for the purpose of evaluating the reasonableness of proposed prices be documented in the contract file to include:

- justification of the need for additional cost information,
- a copy of the request to the contractor for additional cost information, and
- any response from the contractor including any rationale or justification provided by the contractor for a failure to provide the requested information.
The NDAA also required that DOD train the acquisition workforce in the use of the authority provided by the statutes and develop a cadre of experts within DOD to provide advice to the acquisition workforce.

DOD Has Initiated Efforts to Help Determine Reasonableness of Prices

Consistent with requirements in section 831 of the NDAA for Fiscal Year 2013, DOD has initiated actions to provide guidance, training, and expert assistance regarding price reasonableness determinations. Since the guidance, regulation, and training plans have not been implemented, it is too early to determine the effectiveness of these initiatives on determining the reasonableness of proposed prices.

Initial Guidance and Proposed DFARS Rule

DOD issued a policy memorandum that provides specific guidance to contracting officers on DOD’s policy for the determination of the reasonableness of price for a commercial item and on obtaining cost or pricing data from contractors. According to the memorandum, documentation of requests to contractors is to include:

- a justification of the need for the additional cost information,
- a copy of any request from the government to the contractor for this cost information, and
- any response that the contracting officer receives from the contractor to the request, including any rationale provided by the contractor for a failure to provide the cost information requested.

In addition to the memorandum, DOD published a proposed DFARS rule, and plans to publish a related revision to the DFARS Procedures, Guidance, and Information, and revisions to its Commercial Item Handbook to address the requirements of section 831. According to DOD officials, the proposed DFARS rule provides guidance pertaining to determining price reasonableness, specifically addressing the need for

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cost or pricing information from the contractor. Furthermore, a DOD official stated that the proposed DFARS rule addresses issues such as data currency, the percent of sales to commercial parties needed for considering whether cost or pricing data should be requested from the contractors, and how the rule applies to subcontractors. According to a DOD official, DOD is providing a 60 day public comment period for the proposed rule. DOD plans to issue the corresponding Procedures, Guidance, and Information separately. In addition, a DOD official stated that DOD also plans to revise the Commercial Item Handbook to provide more examples, cases, and graphics to enable the contracting officers to apply the rule to their contracts.

Training and Other Assistance

DAU and the office of Defense Procurement and Acquisition Policy have conducted some training and held seminars on determining fair and reasonable prices for contracts. DCMA has additional training planned. The offerings have included a weeklong pricing seminar, an all-day symposium for DAU faculty and pricing experts, a symposium for senior officials in the defense pricing community, and meetings with industry representatives on price negotiations with subcontractors. In the near term, according to a DCMA official, DCMA’s plans include 2 weeks of training for DCMA’s integrated cost analysis teams at some DCMA locations in the United States, among other things.

DAU has already revised some courses to reflect the commercial item and the determination of price reasonableness memorandum, according to a DAU official. Further, DAU is preparing additional training for the acquisition workforce through formal training classes once the DFARs rule and related Procedures, Guidance, and Information are issued, and the Commercial Item Handbook is updated.

DCMA and DCAA provide pricing assistance to contracting officers upon request and are establishing additional support for contracting officers in determining price reasonableness. The DCMA Cost and Pricing Center has established a Commercial Cost and Pricing Team or cadre of pricing experts to provide expert procurement advice to the acquisition workforce. The Team’s mission is to provide direct support to the services’ buying commands, defense agencies, and DCMA contracting officers as well as a DOD-wide help desk capability. According to DCMA officials, since the cadre is new, DOD’s office of Defense Procurement and Acquisition Policy and DCMA are still evaluating its organizational structure and mechanisms for providing support to the acquisition community. Officials stated the cadre may become a collection of centers
across the United States since DCMA can best support its customers when they are on-site.

Lastly, DOD is currently developing a commercial item module in an existing database to provide pricing assistance to the acquisition workforce. According to an official, the module should be functioning in the near future with DCMA developing, testing, and deploying it in the acquisition community. The plan is to have the module contain data on commercial items purchased by DOD including commercial item determinations, pricing data, and supporting evidence.

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Contracting Officials Requested Information from Contractors to Determine Price Reasonableness in Some Cases, but Seldom Requested Cost Data

Our review of a random, nongeneralizable sample of 32 contracts for commercial items showed that contracting officials relied on information available to the government, such as market research or historical pricing, to determine the reasonableness of proposed prices for the majority (20 of 32) of the contracts we reviewed. For the remaining 12 contracts for which officials requested information from the contractor, there were 6 requests for both cost data and pricing information and 6 requests for only pricing information. Contracting officials did not always receive the information requested. Further, we observed that officials faced a number of challenges in determining the reasonableness of proposed prices such as ensuring the currency of the data used in price comparisons and assessing the commercial nature of an item, which can be technically challenging and time consuming.

Contracting Officials Did Not Request Contractor Information for a Majority of the Contracts Reviewed

We found that contracting officials did not request data from contractors to determine price reasonableness for a majority—20 of the 32—of the contracts in our sample. In these instances, the officials determined price reasonableness based on information available within the government such as historical prices paid on previous contracts, independent government cost estimates, or information gathered from sources other than the contractor such as market research. For example, on one contract, the contractor’s proposed prices were lower than prices paid by the government under the previous contract; therefore, the contracting official accepted the prices as fair and reasonable. In many cases, we

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The existing database is the Contract Business Analysis Repository which DCMA established in 2012. The repository facilitates information sharing among DOD contracting officers.
found that contracting officials evaluated the contractor’s proposal using more than one method of price comparison. For example, one official compared proposed prices to historical prices paid by the government on the previous contract, current market rates, and the independent government cost estimate. In another instance, an official compared proposed prices to historical prices paid by the government on the prior contract and proposed prices received in response to the competitive solicitation for the follow-on requirement.

For 12 of the 32 contracts we reviewed, contracting officials requested information from the contractor to determine price reasonableness. As shown in figure 1, officials requested both cost data and pricing information for 6 of these contracts and requested only pricing information for the other 6 contracts.

<table>
<thead>
<tr>
<th>Contracting Officials Requested Contractor Information for 12 Contracts</th>
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<tbody>
<tr>
<td>Requests for both cost data and pricing information</td>
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<tr>
<td>No requests for information from the contractor</td>
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</table>

Of the 12 contracts we reviewed in which contracting officials requested information from the contractor, 6 involved requests for both cost data and pricing information. Contracting officials did not receive the requested cost data from the contractor in one case:

![Figure 1: Contractor Information Requested to Determine Reasonableness of Proposed Prices for Contracts GAO Reviewed](image)
DLA requested cost data and pricing information for a contract for over 150 parts that support various major aircraft including the C-130 and the EA-6B. Due to large differences between proposed prices and the government’s maximum price objective derived from price analysis, DLA requested and received contractor commercial sales data. For several parts, however, DLA also requested contractor cost data because the sales data were judged as inadequate for comparison. The contractor declined to provide DLA with cost data despite intervention from a DLA management official. Although DLA did not achieve its pricing objective, it achieved reduced prices in the base year and reduced escalation rates for out years, among other contractual concessions. Ultimately, DLA determined the final negotiated rates were fair and reasonable using price analysis by comparing proposed prices to the sales data provided by the contractor and historical prices paid by the government from 5 years earlier.

In the other five cases, contracting officials received cost data from the contractor:

- The Navy requested contractor cost data and pricing information to evaluate a contractor’s proposal for engine supplies, services, and related support for the KC-130J aircraft, which transports personnel, cargo, and fuel. The contracting official and a DCMA price analyst made several requests to the contractor for cost data and pricing information needed to evaluate the proposed prices. The contractor provided some of the requested data such as a breakout of how it calculated labor costs, but declined to submit other information such as subcontractor costs and sales information for the same or similar services to non-government customers. The DCMA price analyst was able to view a redacted version of the subcontractor’s proposal at the contractor’s facility, and, after intervention from Navy management, the contractor allowed the Navy team to review a sample of commercial sales data at its facility. According to documents in the contract file, a review of the sales data provided insight into the contractor’s commercial practices and assisted the Navy in identifying which commercial price was the best basis for comparison to the proposed prices. The contracting official used this information along with other methods to establish the Navy’s negotiation objective and ultimately achieved a lower repair price per hour during final negotiations.

- The Navy requested contractor cost data and pricing information in its request for proposal for power units, electronic control boxes, and
associated support services for the E-6B aircraft. The contractor submitted pricing information with its proposal in the form of its commercial catalog, which a contracting official used to evaluate proposed prices for the equipment. The official requested contractor cost data to substantiate pricing for the proposed support services. The contractor provided the information the next day and noted that the cost data should have been submitted with the original quote. The contracting official used cost analysis to verify the proposed support costs with the contractor’s Forward Pricing Rate Proposal, information from the technical evaluator, and market research. During cost analysis, the contracting official requested and received clarification from the contractor on the labor mix used to calculate labor costs and a breakout of other direct costs. Based on the information provided by the contractor, the official determined the costs for support services to be fair and reasonable.

- The Navy requested contractor cost data and pricing information for a contract awarded to acquire jacks for performing aircraft maintenance. Specifically, the contracting official requested that the contractor provide cost data including a breakout of labor rates and material costs because, according to the official, the contractor’s original proposal only contained unit pricing. The contractor provided the necessary cost data—except for a breakout of material costs. After later conducting market research, which showed that the items were offered under a General Services Administration (GSA) federal supply schedule, the contracting official followed up with the contractor to verify recent sales for the items. The contractor provided four invoices for the same items to three non-government customers. As a result, the official determined the item was commercial and used price analysis to evaluate the proposed prices against the GSA schedule, invoices provided by the contractor, and an independent government cost estimate prepared by the program office. Because the proposed prices were equal to or less than the prices used for comparison, the contracting official determined they were fair and reasonable.

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10 Forward Pricing Rate Proposals are provided by contractors as part of a negotiation for a forward pricing rate agreement. The forward pricing rate agreement is a written record of rates agreed to by the contractor and the government that can be used in pricing contracts during a specified time period. FAR § 2.101 and Subpart 42.17.

11 GSA’s federal supply schedule program provides the government with a simplified process for acquiring commercial goods and services.
The Air Force requested a cost breakdown for select contract line items in its request for proposal for a test stand capable of testing a component of the B-2 bomber. The contractor supplied the requested information with its proposal, which the contracting officials used to conduct price and cost analysis to verify proposed prices. Based on the information submitted by the contractor, the officials took exception to some of the proposed subcontractor costs and were able to negotiate a final price that was approximately 5 percent lower than the contractor’s proposal.

DLA requested cost or pricing data for a delivery order of turbine rotor blades. The contractor supplied cost data, such as a breakdown of individual cost elements for each part, as well as pricing information including purchase history, quantity, and unit prices paid with its proposal. The contracting officials used price analysis and examined the cost data during negotiations to substantiate the contractor’s proposal and determine the final negotiated prices fair and reasonable.

Of the 12 contracts we reviewed for which contracting officials requested information from the contractor, 6 involved requests for pricing information only. In each of the 6 cases, the contracting official received that information. Specifically, contracting officials requested information on the prices at which the same or similar items had previously been sold, which represents the minimum amount of information required to be submitted by the contractor when a contracting officer determines that contractor information is necessary to make a fair and reasonable price determination for a commercial item.¹² The officials requested this information for a range of reasons such as updating old information and adapting to a change in the commerciality determination. The following examples illustrate what we observed in our sample:

The Navy requested contractor pricing information to verify proposed prices for a delivery order of KC-130J engine parts. Specifically, the contracting official requested and received invoices from the contractor to evaluate the proposed prices, which were based on the contractor’s commercial catalog. The official also compared proposed prices to unit prices contained in Federal Logistics Data, a centralized database of part prices maintained by DLA. Because proposed prices

¹²10 U.S.C. § 2306a(d).
were consistent with the contractor’s catalog and the total cost for all parts was approximately 25 percent lower than those contained in the database, the official determined the proposed prices were fair and reasonable.

- DLA requested contractor pricing information to support proposed prices for a contract for the infrared turret assembly of the Army’s Blackhawk helicopter. Although the contractor submitted sales invoices with the proposal, DLA requested additional information from the contractor to support the determination of a reasonable price because the catalogue prices and two invoices provided with the proposal were insufficient. The contractor provided additional sales history—all sales to Army National Guard units. DLA determined the final price was fair and reasonable based on comparison to the contractor’s sales data, invoices, and historical prices paid by the government on previous contracts, as well as a fair market value analysis.

- DLA requested contractor pricing information to evaluate proposed prices for a contract for control display units for the Army’s Chinook helicopter. The contractor requested the parts be declared commercial items, but the documentation initially submitted to support the claim was not sufficient. According to the contract file, DLA contracting officials requested sales documentation to verify the contractor’s catalog prices and information on the contractor’s price calculation including a breakout of the price for commercial components and government-specific requirements. The contractor declined to provide copies of the documentation but granted DCMA officials on-site inspection of the sales information, which the DCMA officials used to perform a price analysis of the contractor’s proposal. The price analysis accounted for a 25 percent discount usually offered to the government but not immediately apparent in the offered price. DLA contracting officials established the negotiation objective based on a review of the contractor’s price calculation and sales documentation, as well as a fair market analysis that accounted for economies of scale. The officials determined that the final total price, which was 5 percent lower than the contractor’s original proposal, was fair and reasonable based on price analysis of the contractor’s sales data.

- The Air Force requested contractor pricing information to evaluate proposed prices for an indefinite delivery, indefinite quantity contract for over 200 spare parts for airborne data recorder systems. Because of the volume of parts being acquired, many of which were listed on
the contractor’s published GSA schedule, the contracting official requested and received the most recent sales invoice for a sample of 20 percent of items with available GSA pricing and 100 percent of items without available GSA pricing. The contractor submitted the invoices within a week of the request. After making comparisons, the contracting official adopted the lowest of the three available prices for each item—the proposed price, the GSA price, or a recent sales invoice—as the objective for negotiations. During negotiations, the contractor did not accept the government’s counteroffer but agreed to lower its annual escalation rate. In many cases, this adjustment reduced the first-year price to less than the government’s objective. Therefore, the contracting official determined the negotiated prices to be fair and reasonable.

Challenges in Determining Price Reasonableness

We observed a number of challenges contracting officials face in determining the reasonableness of proposed prices. These challenges included ensuring the currency of the data used for price comparisons, delays in determining the commercial nature of an item, and the reluctance of contractors to share data. Specifically, in reviewing contract files, we observed the following:

- Contracting officials frequently compared proposed prices to the prices paid on previous government contracts. But for several of the contracts we reviewed, the previous contracts used for comparison were dated. For one Navy contract, for example, the data cited as supporting the prices of a previous contract were nearly 10 years old at the time of the contract award. In this case and others, we found no indication in the contract file that the contracting official determined that the previous prices still constituted a valid basis for comparison; nevertheless, the contracting official determined the prices to be fair and reasonable.

- When contractors and the government disagreed about whether an item was commercial, resolving the issue often added time to the process and the results sometimes affected the amount of information available for pricing purposes. On two DLA contracts we reviewed, for example, the solicitation initially categorized the required items as noncommercial, and several months elapsed before decisions were made that the offered products were, in fact, commercial.

- The reluctance of contractors to share data with the government presented an additional challenge. For one Navy delivery order, for example, the contractor provided sales invoices for the same or
similar items, but redacted the identification of the customer. As a result, the contracting official may have had difficulty determining whether the sales were to a government or commercial entity.

**Agency Comments**

We are not making recommendations in this report. We provided a draft of this report to DOD for review and comment. In its written comments, DOD expressed its appreciation for the information and stated that the report would assist the department in its implementation of Section 831 of the NDAA for fiscal year 2013. DOD’s written comments are reprinted in appendix III.

We are sending copies of this report to the appropriate congressional committees, the Secretary of Defense, the Under Secretary of Defense for Acquisition, Technology, and Logistics, and other interested parties. In addition, the report is available at no charge on the GAO website at http://www.gao.gov.

If you or your staff have any questions about this report, please contact me at (202) 512-4841 or at woodsw@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix IV.

William T. Woods
Director, Acquisition and Sourcing Management
List of Committees

The Honorable John McCain
Chairman
The Honorable Jack Reed
Ranking Member
Committee on Armed Services
United States Senate

The Honorable Thad Cochran
Chairman
The Honorable Richard Durbin
Ranking Member
Subcommittee on Defense
Committee on Appropriations
United States Senate

The Honorable Mac Thornberry
Chairman
The Honorable Adam Smith
Ranking Member
Committee on Armed Services
House of Representatives

The Honorable Rodney Frelinghuysen
Chairman
The Honorable Pete Visclosky
Ranking Member
Subcommittee on Defense
Committee on Appropriations
House of Representatives
Appendix I: Objectives, Scope and Methodology

Section 831 of the National Defense Authorization Act (NDAA) for Fiscal Year 2013 (P.L. 112-239) included a provision for GAO to review DOD’s requests for cost data from contractors. This report addresses (1) the status of DOD’s actions to develop guidance and training on determining price reasonableness, and (2) circumstances under which DOD requested cost or pricing information from the contractors for determining price reasonableness for contracts awarded between January 2, 2013 and January 1, 2015.¹

To determine the status of DOD’s actions to develop guidance and training on determining price reasonableness, we:

- reviewed 10 U.S.C. Sections 2306a and 2379 to determine the statutory authorities for obtaining information from contractors in order to determine reasonableness of proposed prices;

- examined Federal Acquisition Regulation (FAR) Parts 12 and 15 and Department of Defense Federal Acquisition Regulation Supplement (DFARS) Parts 212 and 215 for commercial and noncommercial procurements to determine practices and procedures for establishing reasonableness of proposed prices,

- examined policy documents from the Office of the Undersecretary of Defense Acquisition Technology and Logistics (AT&L) concerning determining reasonableness of proposed prices, and

- examined policy and training materials provided by the Defense Contract Management Agency (DCMA), the Defense Contract Audit Agency (DCAA), and the Defense Acquisition University (DAU).

In addition, we interviewed DOD officials from AT&L, DCMA, DCAA, and DAU about actions already taken to address the requirements of Section 831. We also discussed planned actions for implementing the provisions of Section 831 concerning the establishment of guidance on the use of authority granted by statute, guidance issued for training the acquisition

¹Section 831 required our report to assess various DOD actions, including the extent to which DOD needed access to additional cost information pursuant to sections 2306a(d) and 2379 of Title 10, U.S. Code during this two year period in order to determine price reasonableness, and the extent to which DOD needed access to additional cost information during this two year period to determine reasonableness of price, but was not provided such information by the contractor on request.
workforce, and establishment of a cadre of experts within DCMA. We obtained and analyzed such documentation as was available about proposed and on-going actions to compare to the actions prescribed in the mandate.

To discuss circumstances under which DOD requested cost or pricing information from the contractors for determining price reasonableness, we analyzed information from contract files for contracts awarded between January 2, 2013 and January 1, 2015—the dates identified in the mandate—from Federal Procurement Data System-Next Generation (FPDS-NG).

We selected a nongeneralizable, random sample of 40 DOD contracts: 32 identified as being for commercial items and 8 identified as being for noncommercial items. The sample of 40 contracts was comprised of 10 contracts (8 commercial and 2 noncommercial) from each of four DOD agencies with the highest dollar value of contracts awarded during the 2-year period. For each agency we selected contracts from a single command:

- Air Force: Air Force Materiel Command
- Army: Army Materiel Command
- Navy: Naval Air Systems Command
- Defense Logistics Agency: Aviation

From among the contracts awarded during the 2-year period, we selected contracts that were:

- awarded between January 2, 2013 and January 1, 2015,
- noncompetitive, or competitive that received only one offer, and

2For the 8 noncommercial contracts we reviewed, DOD requested certified cost or pricing data. DOD received certificates certifying the contractor’s cost or pricing data and used the information to verify proposed costs as fair and reasonable or to establish the government’s objective for negotiations. Once we verified that certified cost or pricing data were used, we did not discuss these contracts further in the report.
Appendix I: Objectives, Scope and Methodology

- awarded for $700,000 or more—the threshold for requesting certified cost or pricing information for noncommercial contracts.

We excluded orders under General Service Administration federal supply schedules and government-wide acquisition contracts and those contracts awarded using simplified acquisition procedures or sealed bidding as well as basic ordering agreements because these types of contracts have differing pricing approaches and do not necessarily use FAR Part 15 to determine the reasonableness of proposed prices.

We examined documents from the contract file including the Justification and Approval for Other than Full and Open Competition, the Price Negotiation Memorandum, any reports documenting assistance by DCAA or DCMA, any correspondence between the contracting official and the contractor requesting additional data, the Commercial Item Determination Memorandum, and other documents that the contracting official used for determining the reasonableness of the proposed prices. We analyzed the information in the documents to determine:

- the method or methods used to determine reasonableness of prices offered;
- whether the contracting officer requested information from the contractor, either cost or price, to determine the reasonableness of the price offered;

We determined whether or not documentation for the determination of reasonableness of proposed price was provided but did not assess the adequacy of the information provided. In cases where the contract file was unclear about the procedures used or the information obtained, we interviewed contracting officials to clarify the issues.

To assess the reliability of the data reported in FPDS-NG, we compared the contract number, the date of the award, the award value of the contract, the award type, and the designation as noncompetitive or competitive that received only one offer to information provided by the agencies for each contract we selected. We also conducted electronic tests of the data for missing data, outliers, or obvious errors. We concluded that the data were sufficiently reliable for the purpose of selecting a sample and determining whether the requests contained the required information in accordance with our objectives.

We conducted this performance audit from February to August 2015 in accordance with generally accepted government auditing standards.
Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.
## Appendix II: Summary of Contracts GAO Reviewed

<table>
<thead>
<tr>
<th>Department of the Air Force - Air Force Materiel Command</th>
<th>Description of item or service</th>
<th>Total value at contract award</th>
<th>Commercial designation</th>
<th>Received certified cost or pricing data</th>
<th>Requested information from contractor</th>
<th>Type of information requested from contractor</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Airborne Warning and Control System simulation training</td>
<td>$85,410,075</td>
<td>Noncommercial</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Research and development of aircraft protection sensors</td>
<td>$746,496</td>
<td>Noncommercial</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Airborne data recorder system spare parts</td>
<td>$9,974,618</td>
<td>Commercial</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Technical and supply support services for the Air Force Sustainment Center</td>
<td>$4,095,347</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Military medical modernization support services</td>
<td>$2,718,462</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Precision measurement and equipment laboratory services for the Air Force Sustainment Center</td>
<td>$2,136,779</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Integrated test stand for a B-2 bomber component</td>
<td>$1,053,121</td>
<td>Commercial</td>
<td>✓</td>
<td></td>
<td>cost data &amp; pricing information</td>
</tr>
<tr>
<td></td>
<td>TF-33 aircraft engine laser weld repair services</td>
<td>$998,958</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>TF-33 aircraft engine laser weld repair services</td>
<td>$823,120</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Repair of aircraft engine inspection tools</td>
<td>$763,184</td>
<td>Commercial</td>
<td></td>
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<tr>
<td></td>
<td>Department of the Army - Army Materiel Command</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Expeditionary business operations support services</td>
<td>$9,267,713</td>
<td>Noncommercial</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Enhancements to the Ultra Wide Band Ultra High Frequency Synthetic Aperture Radar</td>
<td>$5,117,314</td>
<td>Noncommercial</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Enhanced bandwidth efficient modem production and support</td>
<td>$30,641,786</td>
<td>Commercial</td>
<td>✓</td>
<td></td>
<td>pricing information</td>
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<tr>
<td></td>
<td>Technical writing and illustration services for installation manuals</td>
<td>$4,000,000</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Goodyear tires</td>
<td>$3,290,902</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Multiband manpack radio systems and operator training</td>
<td>$1,742,712</td>
<td>Commercial</td>
<td>✓</td>
<td></td>
<td>pricing information</td>
</tr>
<tr>
<td></td>
<td>Aviator goggles and spare parts</td>
<td>$1,651,171</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### Appendix II: Summary of Contracts GAO Reviewed

<table>
<thead>
<tr>
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<th>Received certified cost or pricing data</th>
<th>Requested information from contractor</th>
<th>Type of information requested from contractor</th>
</tr>
</thead>
<tbody>
<tr>
<td>Technical Support Force Unit training support</td>
<td>$991,000</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Compact metal detector software and display cover upgrades</td>
<td>$722,000</td>
<td>Commercial</td>
<td></td>
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<tr>
<td>Ordinance training development support</td>
<td>$403,365</td>
<td>Commercial</td>
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<tr>
<td><strong>Department of the Navy - Naval Air Systems Command</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>F-35 aircraft, supplies, and sustainment support</td>
<td>$388,310,396</td>
<td>Noncommercial</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Data models for information sharing</td>
<td>$945,211</td>
<td>Noncommercial</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>KC-130J aircraft engine supplies, services, and related support</td>
<td>$52,742,603</td>
<td>Commercial</td>
<td>✓</td>
<td>cost data &amp; pricing information</td>
<td></td>
</tr>
<tr>
<td>E-6B aircraft power units, electronic control boxes, and support</td>
<td>$3,743,170</td>
<td>Commercial</td>
<td>✓</td>
<td>cost data &amp; pricing information</td>
<td></td>
</tr>
<tr>
<td>KC-130J aircraft engine inspection and repair services</td>
<td>$2,554,000</td>
<td>Commercial</td>
<td></td>
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</tr>
<tr>
<td>T-700 aircraft turbo shaft engine, cold section assemblies, and power turbine assemblies repairs</td>
<td>$1,920,195</td>
<td>Commercial</td>
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<tr>
<td>KC-130J aircraft engine repair services and parts</td>
<td>$1,892,068</td>
<td>Commercial</td>
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</tr>
<tr>
<td>P-8A aircraft equipment and engineering support</td>
<td>$1,539,377</td>
<td>Commercial</td>
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<tr>
<td>KC-130J aircraft engine parts</td>
<td>$922,869</td>
<td>Commercial</td>
<td>✓</td>
<td>pricing information</td>
<td></td>
</tr>
<tr>
<td>Aircraft maintenance jacks</td>
<td>$850,822</td>
<td>Commercial</td>
<td>✓</td>
<td>cost data &amp; pricing information</td>
<td></td>
</tr>
<tr>
<td><strong>Defense Logistics Agency - Aviation</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Blackhawk weapons system control unit</td>
<td>$7,260,175</td>
<td>Noncommercial</td>
<td>✓</td>
<td></td>
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<tr>
<td>C-135 aircraft parts</td>
<td>$735,822</td>
<td>Noncommercial</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gyroscopes for aircraft navigation systems</td>
<td>$100,000,000</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Chinook helicopter control display units</td>
<td>$54,900,000</td>
<td>Commercial</td>
<td>✓</td>
<td>pricing information</td>
<td></td>
</tr>
<tr>
<td>Aircraft wheel and brake parts</td>
<td>$18,937,472</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Description of item or service</td>
<td>Total value at contract award</td>
<td>Commercial designation</td>
<td>Received certified cost or pricing data</td>
<td>Requested information from contractor</td>
<td>Type of information requested from contractor</td>
</tr>
<tr>
<td>--------------------------------------------------------------------</td>
<td>------------------------------</td>
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<td>----------------------------------------</td>
<td>---------------------------------------</td>
<td>-----------------------------------------------</td>
</tr>
<tr>
<td>Blackhawk helicopter infrared turret assembly spare parts</td>
<td>$15,385,578</td>
<td>Commercial</td>
<td>✔</td>
<td></td>
<td>pricing information</td>
</tr>
<tr>
<td>Screw ball actuator assembly</td>
<td>$3,761,720</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Spare parts to support various major aircraft including the C-130 and EA-6B</td>
<td>$2,511,173</td>
<td>Commercial</td>
<td>✔</td>
<td></td>
<td>cost data &amp; pricing information</td>
</tr>
<tr>
<td>Turbine rotor blades</td>
<td>$1,005,947</td>
<td>Commercial</td>
<td>✔</td>
<td></td>
<td>cost data &amp; pricing information</td>
</tr>
<tr>
<td>T56 engine spare parts</td>
<td>$819,003</td>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: GAO analysis of DOD contract documents. | GAO-15-680
Appendix III: Comments from the Department of Defense

Mr. William T. Woods  
Director, Acquisition and Sourcing Management  
U.S. Government Accountability Office  
441 G Street, N.W.  
Washington, DC 20548

Dear Mr. Woods:

This is the Department of Defense (DoD) response to the Government Accountability Office (GAO) Draft Report GAO-15-680, “DEFENSE CONTRACTS: DoD’s Requests for Information from Contractors to Assess Prices,” dated July 1, 2015 (GAO Code 121266). The comprehensive and beneficial information contained in this draft report will greatly assist the Department in its efforts in this area, especially with regard to the implementation of Section 831 “Guidance and training related to evaluating reasonableness of price” of the National Defense Authorization Act for Fiscal Year 2013.

Claire M. Grady  
Director, Defense Procurement and Acquisition Policy
Appendix IV: GAO Contact and Staff Acknowledgments

<table>
<thead>
<tr>
<th>GAO Contact</th>
<th>William T Woods, (202) 512-4841, or <a href="mailto:woodsw@gao.gov">woodsw@gao.gov</a></th>
</tr>
</thead>
<tbody>
<tr>
<td>Staff Acknowledgments</td>
<td>In addition to the contact named above, Penny Berrier (Assistant Director); Aryn Ehlow; Andrea Evans; Laura Greifner; Julia Kennon; Carol Mebane; Jean McSween; Roxanna Sun; and Alyssa Weir made significant contributions to this review.</td>
</tr>
</tbody>
</table>
Appendix V: Accessible Data

Data Tables

Data Table for Highlights Figure: Contractor Information Requested by the Department of Defense to Determine Price Reasonableness for Contracts GAO Reviewed

<table>
<thead>
<tr>
<th>Requests for information from the contractor</th>
<th>No requests for information from the contractor</th>
<th>Requests for both cost and pricing information</th>
<th>Requests for only price information</th>
</tr>
</thead>
<tbody>
<tr>
<td>20</td>
<td>12</td>
<td>6</td>
<td>6</td>
</tr>
</tbody>
</table>

Source: GAO analysis of DOD contracts. | GAO-15-680

Data Table for Figure 1: Contractor Information Requested to Determine Reasonableness of Proposed Prices for Contracts GAO Reviewed

<table>
<thead>
<tr>
<th>Requests for information from the contractor</th>
<th>No requests for information from the contractor</th>
<th>Requests for both cost and pricing information</th>
<th>Requests for only price information</th>
</tr>
</thead>
<tbody>
<tr>
<td>20</td>
<td>12</td>
<td>6</td>
<td>6</td>
</tr>
</tbody>
</table>

Source: GAO analysis of DOD contracts. | GAO-15-680

Agency Comments

Department of Defense

Accessible Text for Appendix III: Comments from the Department of Defense

OFFICE OF THE UNDER SECRETARY OF DEFENSE
3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000
ACQUISITION, TECHNOLOGY AND LOGISTICS

August 3, 2015

Mr. William T. Woods
Director, Acquisition and Sourcing Management
U.S. Government Accountability Office
441 G Street, N.W.
Washington, DC 20548

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Signed by
Claire M. Grady
Director, Defense Procurement and Acquisition Policy
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