

GAO

June 1987

PROCUREMENT

Army Implementation of Spare Parts Initiatives



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**National Security and
International Affairs Division****B-220528**

June 8, 1987

The Honorable William V. Roth, Jr.
Ranking Minority Member
Committee on Governmental Affairs
United States Senate

Dear Senator Roth:

In response to your request we have assessed the Department of Defense's (DOD's) progress in implementing its spare parts initiatives. The Secretary of Defense announced the initiatives in July and August 1983 to improve the procurement of spare parts. A more detailed discussion of the initiatives and the results of our review are provided in the appendixes.

We previously reported to you on spare parts procurement at the San Antonio Air Logistics Center, Aviation Systems Command, Ships Parts Control Center, and Defense Electronics Supply Center.¹ Our follow-up work was performed at these same activities. This report presents the results of our review at the Army's Aviation Systems Command (AVSCOM), and includes the following:

- information on price increases during the two periods we examined (see app. III),
- an evaluation of the adequacy of the price analysis procurement officials performed during each of these periods (see app. IV),
- an assessment of the personnel changes made in response to the initiatives (see app. V), and
- our observations on how implementing selected initiatives could be improved (see app. VI).

Our methodology is explained in appendix II. Separate reports are being issued on the results of our review at other locations.

We compared the prices on 8,630 procurements totaling \$510 million to determine the changes that occurred during the 12-month period ending March 31, 1985. Our review showed that 8.2 percent of the procurements experienced price increases of 25 percent or more, while 55 percent had either no price change or a price decrease. We could not

¹DOD Initiatives to Improve the Acquisition of Spare Parts (GAO/NSIAD-86-52, Mar. 11, 1986).

quantify how much the initiatives, as opposed to other factors,² helped achieve these results.

We found, however, that inadequate price analyses occurred in 24.5 percent of our sample procurements with price increases of 25 percent or more. Price increases of this magnitude should prompt close scrutiny. Further, inadequate price analyses occurred in 28.6 percent of our sampled first-time procurements. Adequate price analyses on first-time procurements are particularly important because the acceptability of future prices often depends on how they compare with first-time prices.

The Army could make several changes to improve the environment at AVSCOM. The Army Materiel Command (AMC) directed AVSCOM to implement the spare parts initiatives and, at the same time, to reduce the time taken to award contracts. While we recognize that these priorities are not necessarily incompatible, they created difficulties at AVSCOM, because the workload (purchase requests to be placed under contract) had increased substantially but the staff increase was minimal. As a result, AVSCOM procurement officials had to decide whether the additional steps required by the initiatives were to be performed, the backlog of purchase requests increased, or time standards for contract award exceeded.

In addition, the initiative focusing on training had not been fully implemented—of the 238 authorized training slots for procurement personnel, 140 or 59 percent, were utilized. Moreover, specialized spare parts training was incomplete.

Finally, AVSCOM's competition rate was lower during the period of our follow-up work than in the period of our earlier review. This is an unusual condition, considering the emphasis on the use of competition to improve spare parts prices. We believe the conflicting directions, when combined with a heavy workload and the incomplete training of buyers, could perpetuate the environment described in our earlier report. Buyers were encouraged to award contracts as quickly as possible, thus reducing the quality of price analysis.

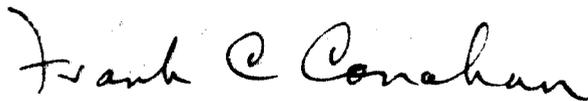
²Changes in spare parts prices could have been the result of several factors. Certainly, lower inflation and improvement in the economy played major roles. The attention given spare parts by top DOD officials and efforts by contractors to minimize price increases and avoid adverse media publicity may have also contributed.

We are, therefore, recommending that the Secretary of the Army reassess the reduction in time for awarding contracts to eliminate the potential conflict between rapid award of contracts and quality price analysis. We also recommend that the Secretary direct AVSCOM to increase the use of competition and provide its buyers with both regular and specialized training.

DOD agreed with our principal findings. (See app. VII.) DOD noted that significant, additional training was accomplished after completion of our review and that more emphasis was placed on reviewing price increases in excess of 25 percent. DOD also stated that it will ensure that the Army addresses the issues of lead time, quality price analysis, and competition.

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of the report. At that time we will send copies to interested parties and make copies available to others upon request.

Sincerely yours,



Frank C. Conahan
Assistant Comptroller General

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Abbreviations

AMC	Army Material Command
AVSCOM	Aviation Systems Command
DLA	Defense Logistics Agency
DOD	Department of Defense
FAR	Federal Acquisition Regulation
PALT	Procurement Administrative Lead Time

Background

In July and August 1983, the Secretary of Defense set the tone for DOD's position on unwarranted price growth and/or excessive pricing on spare parts procurement. In two memorandums, the Secretary announced a series of initiatives, such as

- pursuing refunds on a voluntary or legal basis;
- strengthening procedures for debarring and/or suspending contractors,
- refusing to do business with contractors guilty of excessive pricing, and
- identifying alternate sources, including foreign sources.

The Secretary of Defense asked each service and the Defense Logistics Agency (DLA) to initiate comprehensive programs to fully address the problem. In addition, the Secretary called for efforts by the DOD Inspector General and the Deputy Secretary of Defense, and established an Office of Spares Program Management. The Secretary's memorandums and the responses from the services and DLA have produced a corrective action plan commonly referred to as the "spare parts initiatives."

The Congress, also concerned with spare parts procurement, enacted the Defense Procurement Reform Act of 1984,¹ requiring DOD to address spare parts pricing problems by

- refusing to enter into contracts unless the proposed prices are fair and reasonable;
- continuing and accelerating ongoing efforts to improve defense contracting procedures to encourage effective competition and ensure fair and reasonable prices;
- using standard or commercial parts whenever such use is technically acceptable and cost effective;
- acquiring replenishment parts in economic order quantities and on a multiyear basis whenever feasible, practicable, and cost effective; and
- reexamining the policies relating to acquisition, pricing, and management of replenishment spare parts and technical data related to such parts.

In 1984 several congressional requesters asked us to analyze increases in spare parts prices and to discuss DOD's improvement initiatives and their status. A previous report² on these issues indicated that DOD was

¹Section 1201 of the Defense Authorization Act, 1985, was designated the Defense Procurement Reform Act of 1984.

²DOD Initiatives to Improve the Acquisition of Spare Parts (GAO/NSIAD-86-52, Mar. 11, 1986).

making progress but it would be some time before the initiatives could be fully evaluated. The report also indicated that from January 1980 through August 1983:

- significant price increases occurred in the procurement of spare parts at four DOD locations;
- contractors' prices were, in many cases, accepted by DOD procurement officials (buyers and principal contracting officers) without challenge;
- management emphasized the number of awards made rather than the quality of prices obtained;
- procurement officials were encouraged to limit the analysis performed on low dollar value procurements; and
- DOD announced the spare parts initiatives and established a system for monitoring their progress.

In 1985 the Chairman, Senate Committee on Governmental Affairs requested a follow-up review. As agreed with the Committee's representatives, we did the follow up at the same DOD locations where we did our earlier work and are reporting the results separately, by location (Air Force, Navy, and DLA).

AVSCOM is located in St. Louis, Missouri, and is one of six Army commands reporting to the U.S. Army Materiel Command (AMC). These commands are responsible for spare parts support of the Army's tactical equipment. AVSCOM's primary mission is to provide aviation spare parts and materiel to the Army. AVSCOM purchases over 50,000 spare parts to support about 8,400 helicopters and 565 fixed-wing aircraft, and other aviation related equipment.

As of August 31, 1985, the spare parts inventory managed by AVSCOM was valued at about \$3.1 billion, with another \$1.1 billion on order. About 644 civilian and 15 military staff directly and indirectly support the functions involved in awarding contracts through negotiation, formal advertising, simplified purchases, and delivery orders issued against basic ordering agreements.³

³The basic ordering agreements are not contracts but written agreements that provide the contract provisions that will apply to orders subsequently issued under the agreements. Orders under the basic ordering agreements may be issued as priced or unpriced. Priced orders occur before issuance. Unpriced orders are not priced until some time after issuance.

Objectives, Scope, and Methodology

Our objectives were to determine whether

- increases in spare parts prices had improved;
- the improvement, if any, indicated that the initiatives were working;
- the adequacy of price analyses performed by procurement officials on individual procurements had improved;
- personnel changes required by the initiatives had been implemented; and
- changes, other than personnel related changes, indicated that various initiatives are being followed.

To meet these objectives, we did the following:

- Identified price changes that occurred on procurements made during the 12-month period ending March 31, 1985, and grouped these changes into four categories: price decreases, prices that remained unchanged, price increases of up to 24.9 percent, and price increases of 25 percent or more.
- Analyzed whether factors such as competition, changes in quantity, and dollar value influenced price behavior. (We performed the same analyses during our previous review).
- Selected a statistical sample of 174 procurements (contract files) from a universe of 8,630 procurements to evaluate the adequacy of price analyses performed by procurement officials on individual procurements.
- Determined if AVSCOM had made changes in its personnel evaluation system as required by the initiatives.
- Determined the number of competitive awards and the number of procurements for which quantities had increased from previous buys. (The initiatives emphasize the need for competition as well as buying in larger quantities to avoid frequent buys of small quantities.)

To make unit price comparisons, we obtained the AVSCOM procurement history master file. This file contains detailed procurement information on all AVSCOM procurements, including end items, initial provisioning items, equipment modification and overhaul, and replenishment spare parts. Since we were concerned only with replenishment spare parts, we eliminated procurements that did not meet that definition from the data file.

We also excluded unpriced orders because price comparisons cannot be made on spare parts procured under such arrangements.¹ We included basic ordering agreements and other similar agreements in our sampling unless the final price determination was made by government representatives at contractor plants or other locations. We excluded those procurements because our objective was to assess the adequacy of price analyses at AVSCOM.

We used computer analysis to compare price changes for each item. This analysis compared the most recent unit price within our time frame (April 1, 1984, through March 31, 1985) to the second most recent unit price and then compared the second most recent price to the third most recent price. If an item was procured only once during our review no comparison was made unless a procurement occurred between January 1, 1980, and April 1, 1984.

This process resulted in 5,456 unit price comparisons. We adjusted percentage price changes if the interval between purchases exceeded 1 year by dividing 365 days by the number of days between procurements and multiplying this amount by the actual percentage price change:

$$\text{Annual percentage price change} = \frac{365}{\text{Number of days between procurements}} \times \text{Actual percentage price change}$$

If the interval between procurements was less than 1 year, we made no adjustment.

Our review covered replenishment spare parts procurements for 1 year and compared them with procurements occurring in that same year or, as far back as January 1, 1980. Our earlier report covered procurements for 3 1/2 years between January 1, 1980, and June 30, 1983, in which both procurements had to occur. Because of the differences in designs, the earlier study contained a higher proportion of more frequently purchased items and used a shorter period of developing comparisons. These differences could affect the proportion of items purchased at relatively longer intervals included in the two periods. Thus, the results of the two studies cannot be directly compared.

¹We performed a separate review of unpriced orders for the Senate Committee on Governmental Affairs.

Our results show price increases within each period for those procurements that met our selection criteria. They also indicate some differences in the price increases, but because of the design differences noted above, the exact differences between periods are not known. However, because of the large number of procurements involved, the results provide an indicator of change between periods.

To measure improvement, if any, in the adequacy of price analyses, we randomly sampled procurements from five categories: (1) single procurements (or buys), (2) those procurements with price decreases, (3) those without price change, (4) those with price increases up to 24.9 percent, and (5) those with price increases of 25 percent or more.

Price analysis is defined as the process used to determine whether the offered price—before making a contract award—is fair and reasonable. To evaluate the adequacy of the price analyses performed, we used criteria contained in the Federal Acquisition Regulations (FAR), the DOD FAR Supplement, and the Armed Services Pricing Manual Number 2, (also known as the Small Purchase Manual).

We based our analyses on the information contained in the AVSCOM procurement history master file and on data obtained during interviews with the responsible buyer or contracting officer. These interviews were made to resolve any questions arising from our review of the documents and to provide these personnel an opportunity to comment or discuss the case. Although we did not do a formal reliability assessment of this data base, we compared the award dates, national stock numbers, and unit prices on our sample contracts to data recorded in the automated file. We found only minor errors that would not preclude use of the automated data.

We did not review the implementation of each initiative nor could we identify improvement in relation to specific initiatives. Although we did not evaluate the implementation of each initiative, we attempted to identify, based on discussions with procurement officials and a review of procurement files, those instances where it was evident that selected initiatives were not being adequately implemented.

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

Spare Parts Prices and Factors That Influence Price

Spare Parts Prices

Our review indicated that spare parts prices are moving in the right direction. Table III.1 shows a 10.5-percent increase in procurements with decreased or unchanged prices, and a decrease of 40 percent in procurements with price increases of 25 percent or more over data from our previous review. Table III.2 presents this data in terms of dollars and shows a 25 percent increase in decreased or unchanged prices, fewer (17 percent) with higher prices, and a decrease of 46 percent in price increases of 25 percent or more.

Table III.1 AVSCOM's Spare Parts Procurements by Price Change Category by Transactions

Category	During the 42 months ended June 30, 1983		During the 12 months ended March 31, 1985	
	Number	Percent	Number	Percent
Price decrease	7,958	37.1	2,436	44.6
No change in price	2,710	12.6	560	10.3
0 to 24.9 % increase	7,844	36.6	2,014	36.9
25% or more increase	2,938	13.7	446	8.2
Total	21,450	100.0	5,456	100.0

Table III.2 AVSCOM's Spare Parts Procurement by Price Change Category

Category	During the 42 months ended June 30, 1983		During the 12 months ended March 31, 1985	
	Awards	Percent	Awards	Percent
Price decrease	\$262.3	35.6	\$238.8	46.8
No change in price	58.1	7.9	40.4	40.5
0 to 24.9% increase	351.8	49.7	206.6	40.5
25% or more increase	65.0	8.8	24.2	4.8
Total	\$737.2	100.0	\$510.0	100.0

These changes in spare parts prices may have been the result of several factors. Certainly, lower inflation and improvement in the economy played major roles. The attention given spare parts pricing by top DOD officials and efforts by contractors to minimize price increases and avoid adverse media publicity probably contributed. Also, AVSCOM's implementation of some of the initiatives may have had a favorable impact. We could not, however, quantify how much the initiatives, as opposed to other factors, contributed to the favorable direction spare parts prices have taken.

Price Increases

Our analyses showed significant price increases occurred less often, but when they did occur, the increases were apt to be more severe. For

**Appendix III
Spare Parts Prices and Factors That
Influence Price**

example, procurements with price increases of 300 percent or more increased substantially. Table III.3 shows the magnitude of price increases in the over 25-percent category for our current and previous reviews.

Table III.3: Magnitude of Price Increases in the Over 25-Percent Category by Transactions

Percent increase	During the 42 months ended June 30, 1983		During the 12 months ended March 31, 1985	
	Number	Percent	Number	Percent
25 to 99.99	2,237	76.1	319	71.5
100 to 199.99	368	12.6	48	10.7
200 to 299.99	116	3.9	16	3.6
300 to 399.99	60	2.0	15	3.4
400 to 494.99	23	.8	4	.9
495	134	4.6	44	9.9
Total	2,938	100.0	446	100.0

Table III.4 shows a larger proportion of procurements with substantial price increases occurred on the larger dollar value (over \$25,000) procurements.

Table III.4: Magnitude of Price Increases in the Over 25-Percent Category (In Dollar Ranges)

Dollar range	During the 42 months ended June 30, 1983		During the 12 months ended March 31, 1985	
	Number of procurements	Percent of total	Number of procurements	Percent of total
0 to - 1,000	802	27.3	133	29.8
1,001 to - 10,000	1,319	44.9	180	40.4
10,001 to - 25,000	428	14.5	59	13.2
25,001 to - 50,000	146	5.0	30	6.7
50,001 to - 100,000	128	4.4	11	2.5
over \$100,000	115	3.9	33	7.4
Total	2,938	100.0	446	100.0

Factors That Influence Spare Parts Prices

As in our previous review, we analyzed three factors to determine if they influenced price behavior. These factors are

- competitive versus noncompetitive procurement,
- quantities procured, and
- dollar value of procurements.

The following are the results of both our previous and current reviews.

Competition

In our previous review, we compared price increases in competitive procurements with those in noncompetitive procurements and found that 52.6 percent of the noncompetitive procurements, compared to 45.6 percent of the competitive procurements, experienced price increases. We also found that 14.1 percent of the noncompetitive procurements experienced price increases of 25 percent or more, compared with 12.8 percent for the competitive procurements. We concluded, therefore, that competition reduced both the frequency and severity of price increases. Competition is not a panacea, however, and its effectiveness depends to a large degree on conditions in the marketplace.

Our current and previous analyses have some similarities and some differences. (See table III.5).

Table III.5: Competitive and Noncompetitive Procurements by Price Change Category

	During the 42 months ended June 30, 1983				During the 12 months ended March 31, 1985			
	Competitive		Noncompetitive		Competitive		Noncompetitive	
	No.	Percent	No.	Percent	No.	Percent	No.	Percent
Price decrease	3,292	46.4	4,666	32.5	814	56.0	1,622	40.5
No change in price	568	8.0	2,142	14.9	76	5.2	484	12.1
0 to 24.9% increase	2,332	32.8	5,512	38.5	414	28.5	1,602	40.0
25% or more increase	909	12.8	2,029	14.1	150	10.3	296	7.4
Total	7,101	100.0	14,349	100.0	1,454	100.0	4,004	100.0

Table III.5 shows that 38.8 percent of the competitively awarded procurements experienced price increases while 47.4 of the noncompetitive procurements experienced price increases. In our earlier analyses 45.6 percent of the competitively awarded procurements experienced price increases compared to 52.6 percent of the noncompetitive awards. Thus, our current work also indicates that competition appears to reduce the frequency of price increases.

Regarding the magnitude of price increases, our earlier analysis showed 14.1 percent of the noncompetitive awards experienced increases of 25 percent or more, compared to 12.8 percent of the competitive awards. Our current analysis shows 10.3 percent of the competitive awards experienced price increases of 25 percent or more, compared to 7.4 percent of the noncompetitive awards.

Table III.6 shows that AVSCOM's use of competition went down from 33.1 percent to 26.6 percent.

Appendix III
Spare Parts Prices and Factors That
Influence Price

Table III.6: Competition Rates

	During the 42 months ended June 30, 1983		During the 12 months ended March 31, 1985	
	No.	Percent	No.	Percent
Competitive	7,101	33.1	1,452	26.6
Non-competitive	14,349	66.9	4,004	73.4
Total	21,450	100.0	5,456	100.0

Purchase Quantity

Our previous review showed that for 58 percent of the procurements, unit prices decreased or remained unchanged when purchase quantities were increased. In our current review, the unit price decreased or remained unchanged for 63 percent of the comparisons where quantities increased. (See table III.7).

Table III.7: Price Change by Quantity Variation

Category	During the 42 months ended June 30, 1983		During the 12 months ended March 31, 1985		Quantity decrease	Percent	Quantity increase	Percent
	Quantity decrease	Percent	Quantity increase	Percent				
Price decrease	1,963	24.7	5,702	46.2	424	26.8	1,960	52.7
No change	965	12.1	1,458	11.8	162	10.2	384	10.3
0 to 24.9 percent	3,463	43.5	3,971	32.2	759	47.9	1,183	31.8
More than 25 percent	1,569	19.7	1,201	9.7	238	15.0	193	5.2
Total	7,960	100.0	12,332	99.9	1,583	99.9	3,720	100.0

AVSCOM increased the number of procurements involving increased quantity. In our current review, 70.1 percent of all procurements had quantity increases, as shown in table III.8.

Table III.8: Increased Quantity
Procurements

	During the 42 months ended June 30, 1983		During the 12 months ended March 31, 1985	
	No.	Percent	No.	Percent
Increased quantity	12,332	60.8	3,720	70.1
Decreased quantity	7,960	39.2	1,583	29.9
Total	20,292	100.0	5,303	100.0

Dollar Value

Severe price increases occurred on procurements in all ranges. Table III.9 shows, however, that such increases were most frequent in the

**Appendix III
Spare Parts Prices and Factors That
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lowest dollar range, \$1,000 or less, and the highest dollar range, \$100,000 or more. Thus, while dollar value influences the frequency of severe price increases, it is significant that over seven percent of the time high dollar value procurements experienced severe increases.

**Table III.9: Total Procurements and
Procurements Increasing in Price by 25
Percent or More (In Dollar Ranges)**

Dollar ranges	Total procurement	Procurements increasing in price by 25 percent or more	
		Number	Percent
0 - 1,000	789	319	40.4
1,000 - 10,000	2,304	48	2.1
10,001 - 25,000	922	16	1.7
25,001 - 50,000	503	15	3.0
50,001 - 100,000	333	4	1.2
over \$100,000	605	44	7.3
Total	5,456	446	8.2

Adequacy of Price Analyses on Individual Procurements

Improvement has been made in the adequacy of price analyses performed by procurement officials on procurements with price increases of 25 percent or more. Table IV.1 shows that on a sample basis, 24.5 percent of such procurements were inadequately analyzed. In our earlier analyses, 41.5 percent of the sampled items were inadequately analyzed. Although improvement has occurred, the opportunity exists for further improvement, since price increases of this magnitude should prompt close scrutiny.

Other procurement categories where analyses needed improvement were first-time buys and price increases up to 25 percent. Of the 35 first-time buys randomly selected for review, price analyses on 10 or 28.6 percent were inadequate. Inadequate analyses on first-time buys can perpetuate price increases because the acceptability of future prices often depends on how they compare with first-time prices. Of the 32 procurements where prices increased up to 25 percent, price analyses on 7, or 21.9 percent, were inadequate.

To determine the adequacy of price analysis, we reviewed 174 procurements randomly selected from the universe of 8,630 contracts awarded between April 1, 1984, and March 31, 1985. We concluded that price analyses were adequate on 121 contracts and inadequate on 35 contracts, as shown in table IV.1. We were unable to reach a conclusion on the remaining 18 contracts.¹ Our conclusions were based on a review of the documents in individual contract files and interviews with responsible buyers and/or contracting officers. These interviews were made to resolve any questions arising from our review of the documents and to provide procurement officials an opportunity to discuss or comment on the case.

¹Seventeen contracts did not meet our criteria for review. One contract file was not available for review.

**Appendix IV
Adequacy of Price Analyses on
Individual Procurements**

Table IV.1: Summary of AVSCOM's Price Analyses on 174 Sample Contracts Awarded During the 12-Month Period Ended March 31, 1985

	Total sample	Adequate price analysis		Inadequate price analysis		No conclusion reached	
		No.	Percent	No.	Percent	No.	Percent
Single buys ^a	35	25	71.4	10	28.6	•	•
Price decrease	36	31	86.1	5	13.9	•	•
No change	22	20	90.9	1	4.5	1	4.5
0 to 24.9 percent%	32	24	75.0	7	21.9	1	3.1
Price increase over 25%	49	21	42.9	12	24.5	16	32.7
Total	174	121	69.5	35	20.1	18	10.3

^aSingle buys are those procurements made only once from January 1980 through March 1985.

Projecting our sample results, we estimate that procurement officials' price analyses may have been inadequate on 1,821 contract awards, plus or minus 621 of the 8,630 procurements. The estimate was made at the 95 percent confidence level, with a standard error rate of plus or minus 7.2 percent. In short, between 1,200 to 2,442 contract awards may not have been adequately analyzed.

Our evaluation of price analyses does not provide a basis for determining whether prices were fair and reasonable. However, it does suggest AVSCOM's vulnerability to unreasonable prices because adequate price analyses were not performed.

Procurement Officials' Analyses Adequate

In evaluating whether the contracts included in our sample received adequate price analysis, we relied on guidance in the FAR, the DOD FAR Supplement, and the Armed Services Pricing Manual Number Two. These documents state that procurement officials are responsible for selecting and using price analysis techniques that will ensure a fair and reasonable price. For example, the Armed Services Pricing Manual states that

"For every procurement, the contracting officer must decide as to fairness and reasonableness of the price to be paid for a product or a service. The obligation to contract at fair and reasonable prices does not diminish as we move down the scale from multi-million dollar contracts for systems acquisition to the nickel and dime item prices for nuts, bolts, and screws The conclusion that a price is fair and reasonable must be based on some form of analysis How detailed the analysis is will depend on the dollars and the nature of the product . . . being purchased."

To determine that a price is fair and reasonable, a procurement official may do one or more of the following:

- compare competitive price quotations received in response to a solicitation,
- compare prior quotations and contract prices with current quotations for the same or similar items,
- compare proposed prices with independent government cost estimates,
- compare proposed prices with competitive published lists, and
- exercise personal knowledge that the price quoted reflects the value of the item being purchased.

Procurement Officials' Analyses Inadequate

Table IV.2 summarizes our reasons for concluding that procurement officials did not perform adequate price analyses on 35 contracts.

Table IV.2: Reasons for Inadequate Price Analyses

Last supplier not solicited	9
Inadequate analysis when only one quote received	15
Large price increase over short time period	3
Documentation did not support bases for price analyses	5
Other	3

Last Supplier Not Solicited

In 9 of the 35 cases, the procurement official did not solicit the supplier who sold the same item to the government the last time it was purchased. Five of the cases were formally advertised procurements and four were simplified purchases. For formally advertised procurements, the FAR states that the previous supplier shall be solicited. For simplified purchases over \$1,000, the FAR states that, generally, solicitations shall be limited to three qualified suppliers, two of which were not included on the previous solicitation. This would indicate that the third supplier to be solicited should be the previous supplier.

In all 9 cases, we found that the procurement officials did not follow up on the status of the previous procurement before requesting quotes from contractors. For example, in one case the buyer received a purchase request to purchase 75 bell cranks. The buyer did not identify the most recent procurement and, as a result, did not request a quote from the vendor awarded that contract. The buyer awarded the contract to the sole bidder at a unit price of \$137. That price represented a 32-percent

increase over the \$103.85 paid on the previous procurement awarded 78 days earlier. The buyer had access to current procurement data through use of computer terminals located throughout the procurement directorate, but did not utilize references to the previous procurement.

Inadequate Justification for Acceptance of Price When Only One Bid Was Received

In 15 of 35 cases, procurement officials did not perform adequate price analyses when only one bid or quote was received. The FAR states that the reasonableness of a proposed price should be based on competitive quotations and when just one response is received, additional effort on the part of procurement officials is required. In these cases, procurement officials simply accepted a single response without question.

Our study further showed that solicitation was limited to one source for 10 of the 15 cases and to two sources for 5 of the 15 cases, and that single bids were received for all 15 cases in this category. Solicitation was restricted because the Army had insufficient or no technical data to solicit additional suppliers, or because the Army requires suppliers to become approved sources to be considered for a contract award. For example, the Army purchased 2 cable guides at a unit cost of \$5,516.40 for a total of \$11,032.80. There was one approved source for this unit and it was deemed uneconomical for the government to seek other suppliers. The contract file contained no evidence which detailed the buyer's determination that the price was acceptable and the contracting officer was unable to say why the quoted price was accepted without analysis.

Large Price Increases in Short Periods

We found three cases where prices increased significantly in a short time, when compared to the last price paid. For example, the price paid for one item increased 68 percent in 5 months; and in another case, increased 42 percent in 11 months.

In all three cases, the vendors' quotes appeared competitive and the procurement official accepted the lowest quote, as permitted by the FAR. The FAR presumes adequate price competition will establish acceptable prices. However, because of the significant price growth over a short time, the procurement official should have taken further action to determine the acceptability of the price. For example, the buyer could have questioned the price increase; contacted the government representative at the contractor's plant; or referred the price to AVSCOM's technical personnel for an in-house estimate.

**Documentation Did Not
Support Basis for Price
Determination**

In 5 of the 35 cases the buyer's documents did not adequately explain why the current price was accepted. For example, in one case the procurement official negotiated a unit price of \$93.69 for 54 access screen doors for use on a helicopter. An analysis done by the Plant Representative's Office located at the contractor's plant recommended a unit price of \$19.70. The primary difference between the contractor's proposal and the plant representative's recommendation concerned labor hours. The procurement official at AVSCOM did not address this issue in documenting the case and the price negotiation memo merely concluded that the negotiated price was "fair and reasonable" despite the fact that the \$93.69 price represents an annual rate of increase of 93 percent over the previous price.

FAR 15.803 (c) requires that

"... the contracting officer should include comments in the price negotiation memorandum when significant audit or other recommendations are not adopted."

We believe that the issue surfaced by the plant representative in its recommendation should have been addressed by the procurement official documenting the case.

Other

In 3 of the 35 cases, we found the buyer had made erroneous, incomplete, or inadequate price analysis when concluding that price was acceptable. For example, in one case a buyer purchased 82 vertical indicators at a unit cost of \$353, for a total cost of \$28,946. In evaluating the vendor's proposal, the procurement official calculated the government's objective using an incorrect producer price index. Had the correct index been used, the government's objective would have been lower and, as a result, a better price may have been negotiated. The contracting officer believed a price of \$2 to \$5 less per item could have been negotiated had the correct producer price index been used.

Personnel Changes Related to Spare Parts Initiatives

We found that AVSCOM had made a number of changes in its personnel system, as required by the initiatives. For example, AVSCOM revised its performance evaluation factors to emphasize the quality of price analysis; established an incentive program for recognizing cost reductions and increases in competition when buying spare parts; and initiated training of procurement personnel. Additional details on training are presented in appendix VI.

Performance Standards

One of the Secretary of Defense's spare part initiatives required the military departments and DLA to:

"Revise performance evaluation factors for acquisition and logistic managers to include emphasis on spare parts pricing, breakout, competition, and value engineering accomplishments."

AVSCOM subsequently issued a policy statement that directed managers and supervisors to identify positions with spare parts responsibilities and begin review and revision of applicable standards. As of June 30, 1985, AVSCOM had identified 1,207 military and civilian positions with spare parts responsibilities and revised the performance standards for the positions.

According to an AVSCOM Civilian Personnel Office official, the initiatives caused AVSCOM's personnel system to focus on the importance of quality price analysis. Thus, procurement officials are required, under the performance standards, to

- support breakout¹ efforts that will increase the use of competition in the procurement of spare parts,
- obtain assistance from AVSCOM technical personnel, and when necessary, have them prepare estimated prices when contractors' proposed prices appear excessive, and
- comply with special approval procedures on price increases of more than 25 percent.

While AVSCOM revised the performance standards of its procurement officials to improve the quality of price analysis, AMC reduced the standards

¹The term breakout has two meanings. One meaning involves buying parts directly from manufacturers that were previously bought from prime contractors which did not actually manufacture the part. The second meaning involves seeking alternate sources for items previously furnished by only one source.

governing the amount of time procurement officials were to take to perform price analysis. It would appear, therefore, that these actions are working at cross purposes, improving quality by requiring additional steps in price analysis, while reducing the amount of time permitted to award contracts. Further discussion is in appendix VI.

AVSCOM's Incentive Awards Programs

Another of the Secretary of Defense's initiatives suggested "reward of employees who rigorously pursue cost savings."

AVSCOM's Civilian Personnel Office developed a booklet to help supervisors understand the relationship between the incentive awards program and performance during spare parts procurement. This booklet provides general guidance and procedures governing employee recognition through the incentive awards program for accomplishments achieved in the procurement of spare parts. The recognition includes monetary and honorary awards for performance and suggestions. Honorary awards are available to military personnel, civilian employees, and contractors. Monetary awards are available to GS employees, Merit Pay employees, and military personnel. Table V.1 summarizes AVSCOM's fiscal year 1985 incentive awards for civilian and military personnel.

Table V.1: Incentive Awards for Fiscal Year 1985 Relating to Spare Parts Procurement

Type of award	Number of recipient(s)	Awards	Projected benefits
Performance (Civilian)	11	\$12,849.86	\$271 million
Suggestion	1	\$ 25.00	Intangible
Suggestion	1	Certificate	\$13,493.94 and intangible
Performance (Military)	3	Meritorious Service Medal	\$6.6 million
	1	Army Achievement Medal	Intangible
	1	Meritorious Service and Army Achievement Medals	\$12 million

Status of Disciplinary Actions

In addition to rewarding employees, the Secretary of Defense also called for

"stern disciplinary action, including reprimand, demotion, or dismissal of those employees who are negligent in implementing spare part duties."

According to an AVSCOM Civilian Personnel Office representative, AVSCOM has not taken disciplinary action against any of its employees. Rather than take disciplinary action, the command attempts to exhaust all other avenues of corrective action (counseling and warning notices) before taking measures such as reassignment, demotion, and removal. The command believes that "corrective actions," taken for poor spare parts performance, satisfies the intent of the requirement to discipline employees.

AVSCOM took one corrective action against an employee whose performance under Procurement Administration Lead Time (PALT) standards had been unsatisfactory.² According to a personnel representative, disciplinary action is the next step if the employee does not show improvement. The AVSCOM representative also told us that informal corrective action is probably being taken at the division level within the Directorate for Procurement and Production and that those actions are not reflected in personnel records.

Training

Another of the spare parts initiatives calls for

"Expansion of training curricula to insure proper emphasis, understanding, and technical skill level for all personnel engaged in the acquisition of spare parts."

AVSCOM buyers receive a series of seven mandatory training courses as they move from entry level to more advanced procurement positions. AVSCOM also provides up to 7 or 8 weeks of entry level training to buyers.

In addition to this training, AMC initiated action that required special training as a result of the spare parts initiatives. The primary course was called "Spare Parts Management" and consisted of 40 hours of training.

While AVSCOM initiated action to meet the intent of the training required by AMC, progress has been slow and all of the personnel that should have had the training have not. Additional information on training is presented in appendix VI.

²PALT standards establish the number of days it should take to place a purchase request on contract. Buyers are required to meet or exceed these standards 85 percent of the time.

Observations on Implementation of the Spare Parts Initiatives

The Army's directions for implementing the initiatives and reducing the time taken for contract award could result in buyer confusion regarding the priority of quality price analysis and rapid contract award. Further, specialized spare parts training was not completed, and slots allocated for overall training was not utilized. AVSCOM was authorized 238 training spaces and 140 (59 percent) were filled.

Additional Analysis

The Army's implementation of the initiatives added several steps to the Army's procurement procedures. Some examples of these are

- identifying price disparities and seeking special approval for price increases over 25 percent,
- challenging the procurements when the proposed prices appear unrelated to estimated values,
- screening items for breakout, and
- pursuing refunds in cases of apparent overpricing by contractors.

Additional steps will tend to increase the amount of time it takes AVSCOM buyers to award contracts. However, at the same time, buyers were told to award contracts faster.

Reduction in Time

AMC reduced Procurement Administrative Lead Time standards for fiscal year 1985 as follows:

Table VI.1: Procurement Administrative Leadtime Standards at AVSCOM (in Days)

	Formal advertising	Competitive negotiation	Noncompetitive negotiation
Purchase requests			
\$25,000 and less			
FY 1984	•	90	90
FY 1985	•	88	77
Difference		2	13
Purchase requests			
over \$25,000			
FY 1984	180	200	150
FY 1985	164	180	157
Difference	16	20	(7)

**Appendix VI
Observations on Implementation of the Spare
Parts Initiatives**

Table VI.2 shows the number of purchase requests placed on contract in fiscal years 1984 and 1985. The work load increased with substantially more purchase requests placed on contract.

Table VI.2: Purchase Requests Placed on Contract

Quarter	Fiscal Year 1984	Fiscal Year 1985	Difference
1st	1,303	1,094	(209)
2nd	1,493	2,714	1,221
3rd	3,552	4,955	1,403
4th	4,143	5,779 ^a	1,636
Total	10,491	14,542	4,051

^aEstimated, based on the increase in purchase requests placed on contract during the 3rd and 4th quarters of fiscal year 1984. (4,143 divided 3,552 = 1.1664 times 4,955 = 5,779).

The average number of purchase requests placed on contract each quarter during fiscal year 1984 was 2,623 compared to 3,635 in fiscal year 1985, an increase of 38.6 percent. Although awards increased by an estimated 38.6 percent, staffing positions with spare parts responsibilities increased 1.6 percent, from 313 in fiscal year 1984 to 318 in fiscal year 1985.

Training

AMC directed AVSCOM to initiate specialized training as a result of the initiatives. The special training is a 40-hour course called "Spare Parts Management." Forty-four percent, or 140 of the 318 persons in the target population completed the specialized training in fiscal year 1984. However, no one completed the training in fiscal year 1985. The remaining 178 persons or 56 percent of those designated to receive the course had not received the training.

In addition, an AVSCOM training official told us that the procurement directorate had originally been authorized 238 training slots but had the slots reduced to 208 because the directorate was not fully utilizing available slots. Fifty-nine percent of the original authorized training slots were utilized and 67 percent of the reduced slots were utilized.

Also, during our review of sampled cases, we asked 27 buyers and contracting officers how much training had they received

- 18, or 67 percent, stated no training had been provided. Of the 9 remaining buyers and contracting officers, 6, or 22 percent, stated they

had received one week or less, and 3 stated that they had received more than a week.

In commenting on our draft report, DOD said that since the completion of our review additional training had been provided to AVSCOM personnel. In addition to local training of AVSCOM, 153 procurement people have received formal training in cost and price analysis, and 177 people have attended the "Spare Parts Management" course.

Conclusions

One of the objectives of the initiatives was to change the atmosphere or environment in which buyers were working at the buying centers. Emphasis had been on rapid contract award with little, if any, price analyses performed on small dollar value (\$25,000 or less) procurements.

We believe AVSCOM buyers receiving directions to carry out the initiatives and, at the same time, reduce the time it takes to award contracts were left with little criteria for determining priorities. Further, while the need to carry out the initiatives was emphasized by revised performance criteria and an incentive awards program, the sole corrective action reported by the personnel office involved an individual who did not meet PALT standards.

The increased work load without a corresponding increase in staffing added further impetus to an emphasis on rapid contract award. These conditions could have contributed to AVSCOM's failure to complete specialized spare parts training or to utilize other available training slots.

Recommendations

We recommend that the Secretary of the Army reassess the reduction in standard times for awarding contracts to minimize the conflict between rapid contract award and quality price analysis. We also recommend that the Secretary direct AVSCOM to increase the use of competition in spare parts procurement and to provide buyers with both regular and specialized training.

Agency Comments

DOD agreed with our principal findings. DOD stated that significant additional training was accomplished after completion of our review and that more emphasis was placed on reviewing price increases in excess of 25 percent. DOD also said that it will ensure that the Army addresses the issues of lead time, quality price analysis, and competition.

Comments From the Assistant Secretary of Defense for Acquisition and Logistics



ACQUISITION AND
LOGISTICS
L-SPM

ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D.C. 20301-8000

APR 15 1987

Mr. Frank C. Conahan
Director, National Security and
International Affairs Division
US General Accounting Office
Washington, DC 20548

Dear Mr. Conahan:

This is the Department of Defense (DoD) response to the General Accounting Office (GAO) draft report, "SPARE PARTS: Initiatives at the Aviation Systems Command," dated February 24, 1987 (GAO Codes 396411 and 396418) OSD Case 6851-F. The DoD agrees with the report. Comments relative to each of the major points raised in the report are enclosed.

Although the GAO examined data for the 12-month period ending March 31, 1985, further progress has been made in the intervening two years at the Army's Aviation Systems Command (AVSCOM). Since April 1985, in addition to local training at the AVSCOM, 153 procurement people have received formal training in cost and price analysis, and 177 people have attended the Spare Parts Management Course. Also, more emphasis has been placed on reviewing price increases in excess of 25 percent annually. As a result of initiatives to improve spare parts acquisition, the AVSCOM recorded savings of \$84 million in FY 1985 and \$69 million in FY 1986. The DoD will ensure that within 60 days of this letter, the Army addresses the remaining issues of lead time, quality price analyses and competition.

The GAO report implied that increasing competition and making quality price analyses result in greater procurement lead times. By proper resourcing and streamlining the acquisition process, these need not be competing or mutually exclusive goals. For example, another GAO report described how innovation and management attention at one DoD activity improved lead time results without degrading competition ("PROCUREMENT: Project 12,000 at the San Antonio Air Logistics Center," GAO/NSIAD-86-119BR OSD Case 7067).

Progress is also evident in the other Services and the Defense Logistics Agency, and was recently confirmed by the DoD Inspector General in the "Summary Report on the Follow-up Defense-Wide Audit on Procurement of Spare Parts," dated February 17, 1987. That DoD report included additional data on spare parts programs at the AVSCOM.

**Appendix VII
Comments From the Assistant Secretary of
Defense for Acquisition and Logistics**

In summary, the DoD considers the Army spares program at the AVSCOM one that has achieved some measure of success, but still requires additional management attention. The DoD appreciates the opportunity to comment on the GAO draft report.

Sincerely,

Thomas P. Christie
for Robert B. Costello
Assistant Secretary of Defense
(Acquisition and Logistics)

Enclosure

GAO DRAFT REPORT - DATED FEBRUARY 24, 1987
(GAO CODE 396418) OSD CASE 6851-F

"SPARE PARTS: INITIATIVES AT THE AVIATION SYSTEMS COMMAND"
DEPARTMENT OF DEFENSE COMMENTS

* * * * *

FINDINGS

- **FINDING A: Trends In Spare Parts Prices At The Army's Aviation System Command.** The GAO reported that it compared the prices on 5,456 procurements, valued at \$510 million, made by the Army's Aviation Systems Command (AVSCOM) during the 12-month period ending March 31, 1985. The GAO found that 8.2 percent of these procurements, valued at \$24.2 million, experienced price growth of 25 percent or more. The GAO also found that 54.9 percent of the AVSCOM procurements, totaling nearly \$280 million, had either no price change or a price decrease. The GAO compared these trends with similar data for the 42-month period ended June 30, 1983, and concluded that the AVSCOM spare parts prices have moved in the right direction. (p. 2, pp.17-18/GAO Draft Report)

DOD RESPONSE: Concur.

- **FINDING B: Factors That Have Influenced AVSCOM Spare Parts Prices.** The GAO found that, in addition to the DoD initiatives, the changes in AVSCOM spare parts prices may have been the result of several other factors, including (1) lower inflation and improvement in the economy, (2) the attention given spare parts by DoD officials, and (3) efforts by contractors to minimize price growth and avoid adverse media publicity. The GAO also found that the AVSCOM has made progress in implementing some of the DoD initiatives. The GAO found, for example, that the AVSCOM increased the number of procurements involving large quantities. In addition, the GAO found that the AVSCOM has made a number of personnel changes as required by the initiatives, including (1) revised performance evaluation factors to emphasize the quality of price analysis, (2) an incentive program for recognizing cost reductions and increases in competition when buying spare parts, and (3) initiated training of procurement personnel. The GAO reported, however, that it could not quantify the extent to which the initiatives, as opposed to the other factors, affected the trends in AVSCOM spare parts prices. The GAO

ENCLOSURE

Now on page 0, page 13

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nonetheless concluded however, that the implementation of some of the initiatives by the AVSCOM may have had a favorable impact. (p. 2, pp. 18-25, pp. 35-39/GAO Draft Report)

DOD RESPONSE: Concur.

- FINDING C: Adequacy Of AVSCOM Price Analyses. The GAO found that of the 174 contracts sampled, inadequate price analysis had been performed on 35, representing about 20 percent of the contracts completed. The GAO also found that of the 49 sampled contracts with price growth of 25 percent or more, 12 contracts, or 24.5 percent, did not have adequate price analysis performed. While noting that this represents an improvement in analyses performed for this category, the GAO concluded that price growth of this magnitude should prompt close scrutiny. The GAO further found that price analyses were inadequate on (1) 7 of 32, or 21.9 percent, of procurements where prices increased up to 25 percent, and (2) 10 of 35, or 28.6 percent, of first-time buys. The GAO observed that adequate price analysis on first-time procurements is particularly important because the acceptability of future prices often depends on how they compare with first-time prices. The GAO identified several reasons for the inadequate price analyses. According to the GAO, the two most prevalent reasons, which accounted for 24 of the 35 procurements, were because the buyer either (1) did not solicit the suppliers who sold the same item to the Government previously, or (2) did not perform adequate analysis when only one bid or quote was received. The GAO concluded that the AVSCOM needs to improve the price analyses being performed. The GAO further concluded that if such analyses are not performed the AVSCOM could be vulnerable to unreasonable prices. (p. 2, pp. 26-34/GAO Draft Report)

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DOD RESPONSE: Concur. More emphasis has been placed on reviewing price increases in excess of 25 percent per annum at the AVSCOM.

- FINDING D: Conflicting Directions Regarding Contracting Priorities. The GAO found that, in accordance with the DoD spare parts initiatives, the AVSCOM revised its performance standards for procurement personnel to focus on the need for quality price analysis. The GAO reported that to improve price analysis, procurement officials were required to perform several additional steps, including (1) screening items for breakout, (2) identifying price disparities and seeking special approval for price increases over 25

percent, (3) challenging procurements when proposed prices appear unrelated to estimated values, and (4) pursuing refunds in cases of apparent overpricing. The GAO also found that at the same time, however, the Army Material Command (AMC) directed the AVSCOM to reduce the time taken to award contracts. As a result, the GAO found that the AVSCOM buyers received conflicting directions regarding priorities--rapid contract award or quality price analysis. The GAO also found that compliance with these directions created difficulties because the workload had increased substantially, but the staff increase was minimal. The GAO concluded that the Army needs to reassess these two contracting priorities to improve the environment at the AVSCOM. (p. 3, pp. 35-38, pp. 40-44/GAO Draft Report)

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DOD RESPONSE: Concur. By proper resourcing and streamlining the acquisition process, the goals of increasing competition and making quality price analyses need not conflict with the goal of reducing procurement lead times. For an example of how innovation and management attention at one DoD activity improved lead time results without degrading competition, see the GAO report entitled "PROCUREMENT: Project 12,000 at the San Antonio Air Logistics Centers" (GAO/NSIAD-86-119BR), OSD Case 7067.

- **FINDING E: Further Training Improvements Needed.** The GAO reported that in conjunction with the DoD initiative on training, the AMC directed the AVSCOM to begin specialized training in addition to prescribed training for its buyers. The GAO found that while the AVSCOM initiated action to meet the intent of the AMC requirement, progress has been slow and all of the personnel that should have received the training have not yet received it. The GAO also reported that, according to an AVSCOM official, the training slots originally authorized to the procurement directorate were reduced because they were not being fully utilized. In addition, the GAO found that 67 percent of the procurement officials surveyed said no training had been provided, while another 22 percent said they had received one week or less of training. The GAO concluded that the conditions at the AVSCOM (also see Finding D) could have contributed to the failure of the AVSCOM to complete specialized spare parts training or utilize other available training slots. (p. 3, p. 39, pp. 43-44/GAO Draft Report))

Now on page 2, page 29

DOD RESPONSE: Concur. Since April 1985, in addition to local training, 153 procurement people have received formal training in cost and price analysis, and 177 people have attended the Spare Parts Management Course.

- **FINDING F: Decreased Use Of Competition By The AVSCOM.** The GAO found that 26.6 percent of the AVSCOM contracts awarded during the 12-month period ended March 31, 1985, were awarded competitively. The GAO compared this competition rate with that during the 42 months ended June 30, 1983 and found that the AVSCOM competition rate had decreased from the 33.1 percent rate previously achieved. The GAO observed that this is an unusual condition considering the emphasis on the use of competition to improve spare parts prices. The GAO concluded the decreased use of competition may indicate that the conflicting directions regarding contract priorities, when combined with a heavy workload and the incomplete training of buyers (also see Findings D and E), could have perpetuated the environment that previously existed at the AVSCOM. (p. 3, pp. 20-22, pp. 43-44/GAO Draft Report)

Now on page 3, page 17,
page 33

DOD RESPONSE: Concur.

RECOMMENDATIONS

- **RECOMMENDATION 1:** The GAO recommended that the Secretary of the Army reassess the reduction in standard times for awarding contracts, with the goal of eliminating the conflict between rapid contract award and quality price analysis. (p. 4, p. 44/GAO Draft Report)

Now on page 3, page 33

DOD RESPONSE: Concur. As stated in the DoD response to Findings C and D, since the GAO review was performed the AVSCOM has placed greater emphasis on price analysis. The DoD will ensure that the Army addresses the issues of leadtime and quality price analysis within 60 days. By proper resourcing and streamlining of the acquisition process the goals of increasing competition and making quality price analyses need not conflict with the goal of reducing procurement leadtime, as recognized by the GAO report entitled "PROCUREMENT: Project 12,000 at the San Antonio Air Logistics Center" (GAO/NSIAD-86-119BR), dated June 25, 1986, OSD Case 7067.

- **RECOMMENDATION 2:** The GAO recommended that the Secretary of the Army direct the AVSCOM to increase the use of competition in spare parts procurement, and to provide buyers with both regular and specialized training. (p. 4, p. 44/GAO Draft Report)

Now on page 3, page 33

DOD RESPONSE: Concur. Further Army direction to increase competition is required, and will be issued within 60-days. Also, additional training, will continue (such as that discussed in the DoD response to Finding E).

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