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

DEFENSE DIVISION

Lt. General Wallace H. Robinson, Jr.  
Director, Defense Supply Agency  
Attention: DSAH-CM  
Cameron Station  
Alexandria, Virginia 22314

SEP 21 1971

Dear General Robinson:

The General Accounting Office has reviewed the pricing and administration of seven petroleum supply contracts awarded by the overseas Fuel Division of the Defense Fuel Supply Center, Defense Supply Agency, Alexandria, Virginia (DFSC) to the Asiatic Petroleum Corporation. The contracts, totaling about \$384 million, covered the supply, storage and transportation of petroleum products in Southeast Asia for the years 1967 to 1970 (see appendix).

Under the contracts, Asiatic delivered JP-4 fuel, aviation gasoline, motor gasoline and diesel fuel to Vietnam and Thailand for Government use. The contract prices were negotiated on the basis that Asiatic would buy crude oil in the Persian Gulf or Caribbean areas, ship it to Singapore for refining, and from there ship it to Vietnam and Thailand facilities for storage and distribution to the various military services.

Contract prices were stated in terms of gallons, except for miscellaneous charges. In negotiating the prices of the first five contracts, DFSC contracting officials determined that the fuel prices were based on adequate competition or on market prices and did not request cost or pricing data. For pricing the last two contracts, DFSC requested certified cost or pricing data for certain cost elements added to the fuel prices such as overhead, storage and inland transportation. Asiatic provided such data only for the last contract.

Cost or pricing data, however, were not requested by DFSC for the product portion nor the ocean transportation charges on the basis that market prices were used to determine that contract prices were reasonable.

OPPORTUNITIES FOR IMPROVING PRICE  
NEGOTIATIONS FOR OCEAN TRANSPORTATION

Ocean transportation from the source of crude oil to contractor facilities in Singapore, prior to deliver to Vietnam or Thailand, accounts for a substantial portion of total costs to the Government under these contracts. This cost was included in the per-gallon product

prices in each of the contracts awarded to Asiatic. For most of the contracts, it was estimated that 80 percent of the petroleum products to be delivered would be blended or refined at Singapore.

General-purpose vessels bearing higher rates per ton of cargo normally are used to transport refined products, whereas medium or large vessels, normally are used to transport crude at lower rates. The ocean transportation rates used in contract negotiations we reviewed were based on the use of published rates for general-purpose vessels, the most expensive method of ocean transportation. We estimate that, in calendar year 1969 alone, over \$1 million could have been eliminated from ocean transportation cost included in the negotiated contract prices if freight rates used in the negotiations had been based on a combination of 80 percent use of medium vessels for crude oil and 20 percent use of general-purpose vessels for refined product.

In commenting on this matter, DFSC officials stated that overall the contract prices negotiated with Asiatic for petroleum products have been reasonable. They indicated that any attempts to negotiate a reduction in the ocean transportation portions of the prices probably would have been offset by contractor-proposed price increases in some other cost element. In our opinion, this rationale does not afford a sufficient basis for not attempting to negotiate transportation rates consistent with the type of vessels that could be used.

#### Recommendation

We recommend that DFSC obtain cost information in support of its estimates for ocean transportation and conduct future price negotiations for ocean transportation costs using freight rates for general-purpose, medium or large vessels in proportions they are likely to be used to transport estimated quantities of oil products from the acquisition sources to Singapore.

#### NEED TO STRENGTHEN CONTRACT ADMINISTRATION

Our review showed that more effective administration by DFSC of contract provisions could have resulted in savings to the Government of \$395,000 as shown below.

	<u>Estimated amount of overpayment</u>
Payment for higher priced gasoline than was actually furnished	\$247,000
Overpayment for the transportation of fuel from Singapore to Vietnam	103,000

Credit not obtained for returned cargo	20,000
Contractor permitted to retain overpayment for intransit losses	<u>25,000</u>
Total	<u><u>\$395,000</u></u>

Payment for higher priced gasoline  
than was actually furnished

Under the terms of the contract effective October 1, 1966, Asiatic agreed to deliver up to 63 million gallons of aviation gasoline from the contractor's Singapore facilities to Vietnam and Thailand during the period October 1, 1966, to June 30, 1967. The contract provided the gasoline was to come originally from the Caribbean area. The purpose of this provision was to enable the DFSC to meet a Department of Defense requirement then in effect which established a minimum dollar amount of petroleum products to be purchased in the Caribbean. Since gasoline from the Caribbean was more costly than gasoline from the Persian Gulf, the higher cost was included in the contract price.

Reports by the contractor during the contract period show that about 46.5 million gallons of gasoline were delivered to Vietnam and Thailand under the contract. Of this amount, only 12 million gallons were shipped from the Caribbean. Another 4.7 million gallons were in the contractor's inventory in Southeast Asia when the contract became effective. The original source of this gasoline could not be determined from available records.

The remainder of the 29.8 million gallons was not obtained by the contractor from the Caribbean contrary to the contractual requirement. The Government paid the higher price as though the gasoline had come from the Caribbean. Our comparison of the delivered prices for gasoline from the Caribbean with those from the Persian Gulf, Asiatic's normal source, indicated that the Government is legally entitled to a refund of about \$247,000 for gasoline not purchased from Caribbean sources.

Contract administration personnel of DFSC were aware that not all the gasoline had been shipped from the Caribbean. The contracting officer suggested to the contractor, in a letter dated August 11, 1967, that a price reduction for the non-Caribbean gasoline was in order. The contract files indicate, and an agency official confirmed, that Asiatic did not reply to this letter. The official indicated that the only further action in the matter had consisted of an unofficial conversation with one of Asiatic's officials. The contract files did not contain a record of this conversation or of any other follow-up action. We were informed, however, that the matter had not been dropped.

Overpayment for transportation  
of fuel from Singapore to Vietnam

From October 1966 through December 1969, the contracts provided that the contractor would be paid a transportation charge for each day a ship was (1) at sea while carrying cargo from Singapore to Vietnam or Thailand, (2) at ports of destination in Vietnam or Thailand, and (3) at sea while returning to Singapore.

The contracts provided that, if a vessel could not complete its voyage (from Singapore to Vietnam or Thailand and back to Singapore) because of a "force majeure" (an event that could not reasonably be foreseen or controlled), the Government would pay transportation charges for that voyage up to the time of its interruption. It would also reimburse the contractor on a limited basis for any costs resulting from the vessel's inability to complete the voyage, including the cost of returning the vessel to Singapore. The Government's total obligation to the contractor was limited to the amount of transportation charges that would have been payable if the voyage had been completed.

We noted two instances in which a contractor-controlled vessel, after delivering part of its cargo to a destination in Vietnam, encountered circumstances which prevented it from delivering the remainder of its cargo. The "Amastra" was involved in an accident in a Vietnamese harbor on April 12, 1967, and the "Helisoma" was damaged by a mine in the same Vietnamese harbor on December 22, 1968. Because of the damage sustained by the vessels, they could not complete their voyages but had to return to Singapore.

The contractor billed the Government and was paid a net amount of \$216,000 covering all transportation charges for the time spent by the two vessels, including salvage operations and returning the vessels to Singapore, and by other contractor-controlled vessels in rendering salvage assistance. The amounts paid exceeded the amounts of transportation charges that would have been payable if the two vessels had been able to complete their voyages. We estimate that, if the voyages had been completed, transportation charges of about \$113,000 would have been payable. Thus we estimate the contractor was overpaid \$103,000.

DFSC officials indicated that overpayments may have been made and that they would review the situation and take appropriate action.

Credit not obtained for returned cargo

The contract in effect at the time the "Helisoma" sustained its mine damage in December 1968 provided that the contractor would be paid for petroleum products on the basis of quantities loaded at Singapore and delivered to destinations in Vietnam or Thailand. Under these conditions the Government should receive credit for any cargo loaded at Singapore that was not delivered to its destination.

Some of the cargo from the "Helisoma" was not delivered to its destination but was returned to Singapore. Although a credit is due the Government for this cargo, our review of credit invoices revealed no evidence that a credit had been processed. We estimate that about \$20,000 should have been credited to the Government for the cargo that was returned.

DFSC officials stated that they would review this matter and take appropriate action.

Contractor permitted to retain over-payment for intransit losses

Three of the contracts that we reviewed contained a provision to reimburse the contractor for replacing fuel lost intransit through normal leakage or evaporation on voyages from Singapore to Vietnam or Thailand. The contracts provided that the amounts payable to the contractor for intransit losses were to be computed as a percentage of the product price under the first contract and as a percentage of the product price plus cargo insurance and transportation charges under the other two contracts. Under the terms of the contracts, most of the intransit-loss charges were billed by the contractor and paid by the Government at tentative rates that were subject to adjustment after fuel shipments had been completed and insurance costs, transportation charges, and product prices had been finally determined.

We found that the payments made to the contractor for intransit losses had not been adjusted retroactively on the basis of finally determined insurance costs, transportation charges, and product prices. We estimated that, as a result, the contractor was overpaid about \$25,000 for intransit losses under the three contracts.

DFSC officials stated that the need to make retroactive adjustment to the intransit-loss charges had been overlooked in the administration of the contracts involved.

Recommendations

We recommend that action be taken to recover the amounts overpaid the contractor for:

- gasoline charged at the higher Caribbean price but actually shipped from a less expensive source,
- transportation charges from Singapore to Vietnam in excess of contract limitations,
- cargo loaded at Singapore that was not delivered, and
- any intransit-loss payment determined to be excessive.

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We would appreciate receiving your comments concerning any action taken or planned on the matters discussed in this report as well as your views as to whether an internal audit of other petroleum contracts in Southeast Asia should be made.

Sincerely yours,

  
Associate Director

Appendix

Asiatic Petroleum Corporation Contracts  
Reviewed by GAO

<u>Contract</u>	<u>Effective Date</u>	<u>Dollar Value</u>	<u>Period of performance</u>
DSA-600-67-D-0591	Oct. 1, 1966	\$62,721,225	Oct. 1, 1966 - June 30, 1967
DSA-600-67-D-2263	July 1, 1967	41,235,870	July 1, 1967 - Dec. 31, 1967
DSA-600-68-D-0656	Jan. 1, 1968	61,244,487	Jan. 1, 1968 - June 30, 1968
DSA-600-68-D-1641	July 1, 1968	51,314,431	July 1, 1968 - Dec. 31, 1968
DSA-600-69-D-0576	Jan. 1, 1969	71,213,823	Jan. 1, 1969 - June 30, 1969
DSA-600-69-D-1747	July 1, 1969	59,666,338	July 1, 1969 - Dec. 31, 1969
DSA-600-70-D-0990	Dec. 23, 1969	<u>36,425,410</u>	Dec. 23, 1969 - June 30, 1970
		<u>\$383,821,584</u>	