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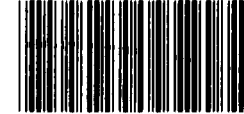
UNITED STATES GENERAL ACCOUNTING OFFICE

WASHINGTON, D.C. 20548

PROCUREMENT AND SYSTEMS
ACQUISITION DIVISION

B-168450

JANUARY 4, 1979



108275

The Honorable Harold Brown
The Secretary of Defense

Attention: Assistant Secretary of Defense
(Comptroller)

Dear Mr. Secretary:

We have reviewed the pricing of subcontract 11-52792 awarded on October 10, 1974, by the Grumman Aerospace Corporation to the General Electric Armament Department, Burlington, Vermont. This firm-fixed-price subcontract for \$2,407,360 was for 80 20MM internal feed and drive systems to be used on the F-14 aircraft. The F-14 is being manufactured by Grumman for the Department of the Navy under prime contracts N00019-75-C-0078 and N00019-75-C-0013. *DLG 0 038)*

This subcontract was selected as part of a nationwide review of the pricing of negotiated noncompetitive subcontracts awarded under Department of Defense (DOD) negotiated noncompetitive prime contracts. Our objective was to determine the reasonableness of the subcontract price in relation to cost or pricing data available to the subcontractor at the time of subcontract negotiation.

Our review was performed at the subcontractor's facility where we reviewed documents and held discussions with subcontractor personnel. We also considered work done by the Defense Contract Audit Agency and Defense Contract Administration Services Office staffs located at the subcontractor location.

In summary, we found that General Electric's proposed costs for labor variances were not based on current data. We believe that had such data been disclosed, Grumman would have had a sound basis to reduce the subcontract price by about \$101,732.

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BACKGROUND

Public Law 87-653 (The Truth in Negotiations Act) requires that with certain exceptions, contractors and their subcontractors be required to submit cost or pricing data in support of proposed prices for noncompetitive contracts and contract modifications expected to exceed \$100,000. In addition, contractors are required to certify at the time of negotiations that data submitted is current, complete, and accurate. A clause is inserted in the contract which gives the Government a right to a price reduction, where it is determined that the price was increased because the data submitted was not in accordance with the certification.

In response to a Grumman request, General Electric submitted a firm-fixed-price proposal dated February 5, 1974, for 80 internal feed and drive systems at a price of \$2,666,016. The Grumman request resulted from a proposed fiscal year 1975 procurement of F-14 aircraft by the Department of the Navy. The proposal was evaluated by personnel of the resident Defense Contract Administration Services Office (DCASO) and Defense Contract Audit Agency (DCAA). On April 23, 1974, General Electric submitted a revised proposal which was used as the basis for negotiating the subcontract price. The negotiations were conducted between April 23 and April 25, 1974. On April 29, 1974, General Electric executed a Certificate of Current Cost or Pricing Data, as of April 25, 1974, the date the subcontract negotiations were completed.

RESULTS OF REVIEW

General Electric's proposal was overpriced by about \$101,732 because the cost proposed for manufacturing and reliability and quality control (R&QC) variances was not based on current cost or pricing data.

General Electric's manufacturing and R&QC variance cost estimates, for its initial proposal, were based on a variance forecast that incorporated actual cost history through September 1973. The revised proposal included the same variance percentage estimates; however, the cost or pricing data submitted included actual cost history through December 1973 and supported variance estimates lower than the cost proposed. As shown below, the variance amounts supported were about \$101,732 lower than that proposed.

	<u>Manufacturing</u>	<u>R&QC</u>	<u>Total</u>
Variance estimate included in the revised proposal	\$78,298	\$72,425	\$150,723
Variance estimate supported by cost or pricing data submitted	<u>66,825</u>	<u>64,967</u>	<u>131,792</u>
Unsupported variance estimate included in the revised proposal	\$11,473	\$7,458	\$ 18,931
Plus: Wage adjustments (10.8%)	<u>1,239</u>	<u>805</u>	<u>2,044</u>
	<u>12,712</u>	<u>8,263</u>	<u>20,975</u>
Plus: Vacation and holiday (10.0%)	<u>1,271</u>	<u>826</u>	<u>2,097</u>
	<u>\$13,983</u>	<u>\$9,089</u>	<u>\$ 23,072</u>
Plus: Indirect manufacturing expense (214.8%)	<u>30,035</u>	<u>19,523</u>	<u>49,558</u>
	<u>\$44,018</u>	<u>\$28,612</u>	<u>\$ 72,630</u>
Plus: General expenses (21.8%)	<u>9,596</u>	<u>6,237</u>	<u>15,833</u>
	<u>\$53,614</u>	<u>\$34,849</u>	<u>\$ 88,463</u>
Plus: Profit (15.0%)	<u>8,042</u>	<u>5,227</u>	<u>13,269</u>
	<u>\$61,656</u>	<u>\$40,076</u>	<u>\$101,732</u>

According to General Electric officials, they became aware of actual first quarter 1974 manufacturing and R&QC variance percentages just before submitting the revised proposal to Grumman. Three of the four actual variance percentages were greater than had been forecasted using cost history through December 1973. As a result, General Electric decided not to use the variance percentage estimates supported by the cost or pricing data submitted. General Electric officials claimed that the basis for this difference was presented to Grumman at the negotiations, but were unable to provide us with documentation despite General Electric's internal cost estimating requirements that all additional data disclosed to the customer at negotiations should be carefully documented.

According to Defense Acquisition Regulation (DAR) 3-807.3(i):

"The requirement for submission of cost or pricing data is met when all accurate cost or pricing data reasonably available to the contractor at the time of agreement on price is submitted either actually or by

specific identification in writing * * *. The mere availability of books, records and other documents for verification purposes does not constitute submission of cost or pricing data."

In addition, the instructions to offerors included in DOD Form DD-633 states as part of the specific information required, the offeror must submit and clearly identify as such, cost or pricing data. In addition, the offeror must submit any information reasonably required to explain the offeror's estimating process, including the judgmental factors applied and the mathematical or other methods used in the estimate.

CONCLUSIONS AND RECOMMENDATIONS

We believe General Electric's basis for using higher variance percentages in the cost proposal than those supported by the updated cost or pricing data should have been explained in writing and included as part of the cost proposal. The failure to do so resulted in the subcontract being overpriced by about \$101,732.

Accordingly, we recommend that you have the Naval Air Systems Command consider the findings presented herein, along with any additional information available, to determine whether the Government is entitled to a price adjustment under Grumman prime contracts N00019-75-C-0078 and N00019-75-C-0013. We have not determined the total dollar effect of Grumman's add-on factors resulting from the overpricing of the General Electric subcontract. This will have to be computed to determine the total amount of overpricing.

Copies of this letter are being sent to General Electric Armament Department; Grumman Aerospace Corporation; the Director, Office of Management and Budget; and the Secretary of the Navy. We are also sending copies to the Chairmen of the Senate and House Committees on Appropriations and Armed Services, the House Committee on Government Operations, and Senate Committee on Government Affairs.

As you know, Section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on

our recommendations to the House Committee on Government Operations and the Senate Committee on Government Affairs not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We would appreciate receiving your comments on these matters and would be pleased to discuss any questions that you may have.

Sincerely yours,

A handwritten signature in cursive script, appearing to read "J. H. Stolarow".

J. H. Stolarow
Director