

United States General Accounting Office

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**GAO**

Report to the Honorable  
Edward F. Feighan  
House of Representatives

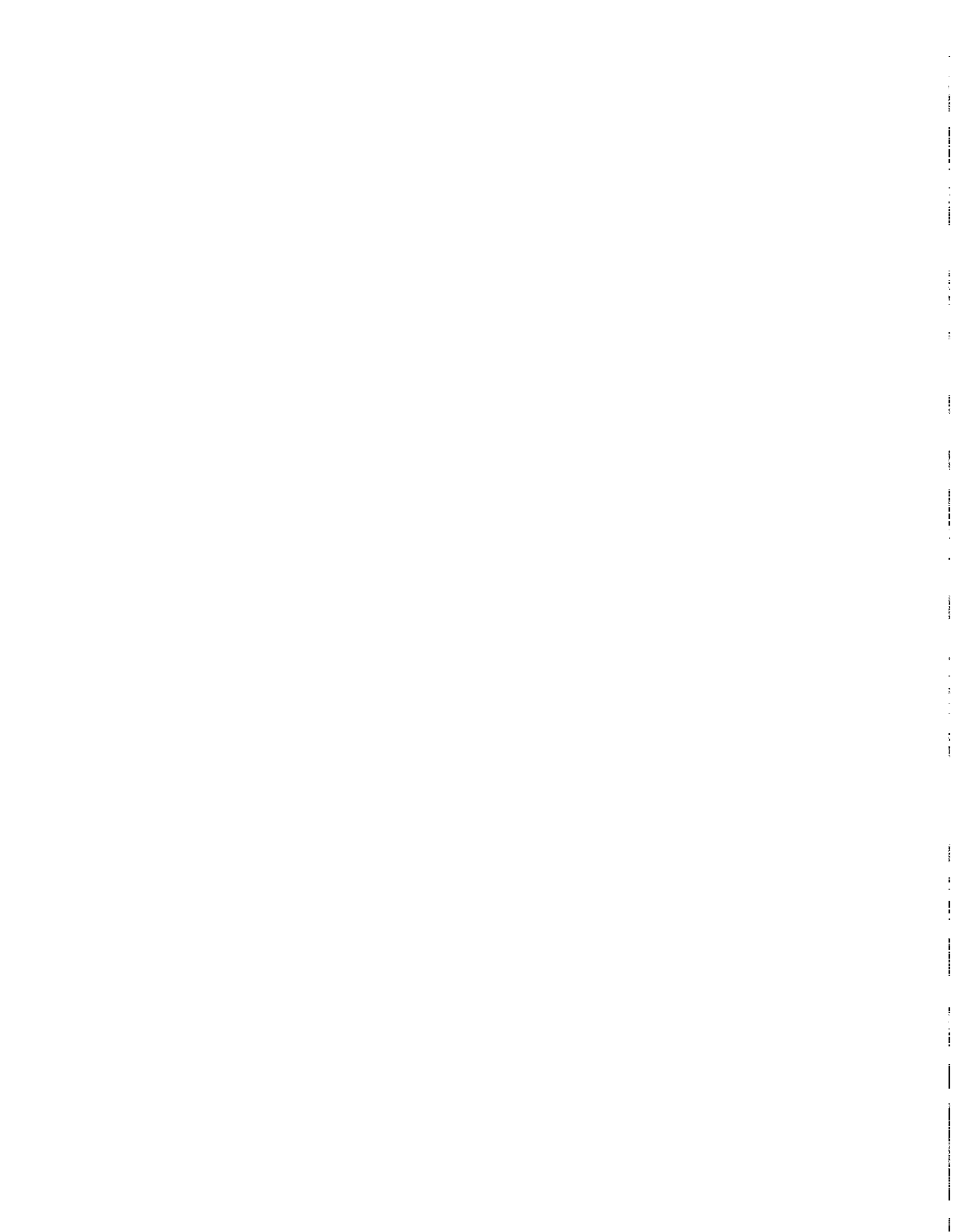
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February 1991

# DEFENSE STOCKPILE

## Defense Logistics Agency Contract Award for Cobalt







United States  
General Accounting Office  
Washington, D.C. 20548

National Security and  
International Affairs Division

B-241859

February 19, 1991

The Honorable Edward F. Feighan  
House of Representatives

Dear Mr. Feighan:

As you requested, we reviewed the Defense Logistics Agency's (DLA) 1989 contract awarded to Sherritt Gordon Limited, a Canadian company, to upgrade some of the U.S. government's strategic stockpile of cobalt. You raised concerns regarding DLA's decision to award this contract to the highest bidder. Specifically, you asked us to examine

- the objections that had been raised by another firm regarding DLA's cobalt contract award to Sherritt and
- the process DLA proposes to use to upgrade the U.S. strategic cobalt stockpile.

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## Results in Brief

DLA properly awarded the contract to Sherritt, the highest bidder, because the other two bidders did not offer cobalt from a "designated country," as required by the Trade Agreements Act.<sup>1</sup> Sherritt was the only company offering cobalt from an authorized source. Objections to DLA's contract award to Sherritt had no merit.

According to DLA officials, plans to further upgrade the strategic cobalt stockpile are only in the preliminary discussion phase. DLA officials also said that even after such plans have been made final, they would be considered procurement sensitive and could not be disclosed publicly.

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## Background

Responsibility for management of the National Defense Stockpile, created under the Strategic and Critical Materials Stock Piling Act, has been delegated to DLA. A 1990 Department of Defense (DOD) report on the stockpile shows an inventory of 53,105,165 pounds of cobalt valued at \$402.3 million.

Section 521 of Public Law 100-440 required that at least \$1 million, but not more than \$2 million, be obligated by October 1, 1989, for a pilot project to upgrade cobalt deposited in the National Defense Stockpile.

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<sup>1</sup>The Trade Agreements Act allows the President to designate, in accordance with criteria listed in the act, countries that are eligible for favorable treatment in U.S. government procurements.

On July 19, 1989, DLA issued an invitation for bids to upgrade government-owned cobalt in various forms.

DLA received bids from three firms: (1) Hall Chemical Company, a U.S. company offering cobalt from Zambia; (2) Gecamines Commerciale, a state-owned mining company of Zaire offering cobalt from Zaire; and (3) Sherritt, offering cobalt from Norway. DLA rejected lower bids from Hall and Gecamines, and on September 26, 1989, awarded the contract to Sherritt at \$1,472,788.

The Trade Agreements Act does two things. First, with respect to products of designated countries it authorizes the President to waive application of such procurement preference laws as the Buy American Act. Second, the Trade Agreements Act prohibits the procurement of foreign end products from non-designated countries, unless a waiver is obtained in the national interest. With certain exceptions, the Trade Agreements Act applies to procurements above a monetary threshold, which currently is \$156,000.<sup>2</sup> The designated countries, which are listed in the Federal Acquisition Regulation (FAR), include Norway, but not Zambia or Zaire.

The solicitation references a clause in Defense FAR Supplement (DFARS) that provides that the contractor must supply a domestic end product, unless the contractor indicated that it would supply a designated country end product. For unmanufactured items, the clause defined "domestic end product" as one that "has been mined or produced in the United States." The solicitation further indicated that bids would be evaluated in accordance with part 25 of the FAR and part 225 of the DFARS.

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## Evaluation of Hall's Concerns About DLA's Contract Award

The Hall Chemical Company stated that its bid, as well as that of Gecamines, was improperly rejected and that it objected to the award to Sherritt on several grounds. DLA denied Hall's protest on December 5, 1989. The following are the assertions put forth by Hall and our evaluation.

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<sup>2</sup>For example, the Trade Agreements Act does not apply to purchases of arms, ammunition, or war materials or contracts for construction or services.

Hall stated that in accordance with FAR 25.108 the cobalt it offered could have been considered as domestic because cobalt is not “mined, produced, or manufactured in the United States in sufficient and reasonably available commercial quantities of a satisfactory quality.” However, our review of FAR 25.108 showed that it listed articles, materials, and supplies that could be considered domestic only when incorporated into an end product; it did not provide that a raw material such as cobalt could be considered as domestic when it was the end product being procured. More importantly, DLA’s purchase of cobalt is covered under the Trade Agreements Act, which generally prohibits purchases of foreign end products that are not from designated countries.

Hall also said that DLA should have obtained a waiver for this procurement in the national interest as provided by the Trade Agreements Act. The act, however, only authorizes the U.S. Trade Representative to grant waivers when they are determined to be in the national interest. In this case, DLA explored the possibility of seeking a waiver from the Trade Agreements Act requirement to procure cobalt from a designated country, but in prior cases the possibility of obtaining a reduced price was not ordinarily considered adequate justification. DLA pointed out that abiding by the obligations of the Trade Agreements Act sometimes will result in instances where the government pays higher prices for some products. Nevertheless, DLA determined that taking into consideration supply and demand, the extended delivery schedule, and the cost of military packaging requirements, Sherritt’s price was fair and reasonable.

Hall further asserted that DLA “hid the ball” from the bidders by not explaining to Hall that bids offering cobalt from a non-designated country would be considered nonresponsive. We found no merit to this argument. While the solicitation did not specifically state that the criteria of the Trade Agreements Act applied, it clearly indicated that bids would be evaluated in accordance with FAR part 25, and by reference that procurements above the current monetary threshold of \$156,000 were subject to the Trade Agreements Act. FAR listed the designated countries, and the solicitation indicated the dollar threshold. Thus, Hall had adequate notice that the Trade Agreements Act applied to the procurement.

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## DLA's Process to Upgrade the Strategic Cobalt Stockpile

According to DLA officials, DOD is reviewing all national defense stockpile needs, including cobalt. The bulk of the stockpile inventory was acquired in the 1950s and 1960s, and a portion of this inventory has become obsolete due to changes in industrial capacity and new manufacturing and technological developments. DLA's future plans concerning the strategic cobalt stockpile are in the preliminary discussion phase; however, such plans to acquire cobalt or other materials for the strategic and critical materials stockpile, including those that have been finalized, are considered procurement sensitive and cannot be disclosed. DLA officials said, therefore, that they were not in a position to discuss the process they might use to upgrade the strategic cobalt stockpile.

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## Scope and Methodology

To develop information for this report we

- interviewed senior officials at DLA's Executive Directorate of Stockpile Management, responsible for the National Defense Stockpile, to obtain their views regarding the process used to award contracts and their plans to upgrade the stockpile inventory;
- reviewed documents related to the award to Sherritt and the bids submitted by Hall and Gecamines;
- interviewed the attorneys representing Hall to obtain their views regarding DLA's award to Sherritt; and
- analyzed relevant sections of the Trade Agreements Act of 1979, the Buy American Act, and implementing regulations.

We conducted our review between December 1989 and August 1990 in accordance with generally accepted government auditing standards.

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## Agency Comments

DOD provided written comments on a draft of this report, concurring with our findings. DOD's comments are reprinted in appendix I.

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We are sending copies of this report to the Secretary of Defense and the Director, Office of Management and Budget. Copies will also be made available to others on request.

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Please contact me on (202) 275-8400 if you or your staff have any questions concerning this report. The major contributors to this report are listed in appendix II.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Paul F. Math". The signature is stylized with a large, sweeping initial "P" and a distinct "M".

Paul F. Math  
Director, Research, Development,  
Acquisition, and Procurement Issues

# Comments From the Department of Defense

Note: GAO comments:  
The two minor editorial  
changes noted have been  
incorporated in the report.



PRODUCTION AND  
LOGISTICS

ASSISTANT SECRETARY OF DEFENSE  
WASHINGTON, D. C. 20301-8000

January 9, 1991

Mr. Frank C. Conahan  
Assistant Comptroller General  
National Security and International  
Affairs Division  
U.S. 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, "DEFENSE STOCKPILE: Defense Logistics Agency Contract Award for Cobalt," dated December 4, 1990, (GAO Code 396028/OSD Case 8555). The DoD has reviewed the report and concurs with the findings. Two minor editorial changes are noted in the attached copy of the report.

The Department appreciates the opportunity to review the draft report.

Sincerely,

A handwritten signature in cursive script that reads "David J. Berteau".

David J. Berteau  
Principal Deputy

Attachment



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# Major Contributors to This Report

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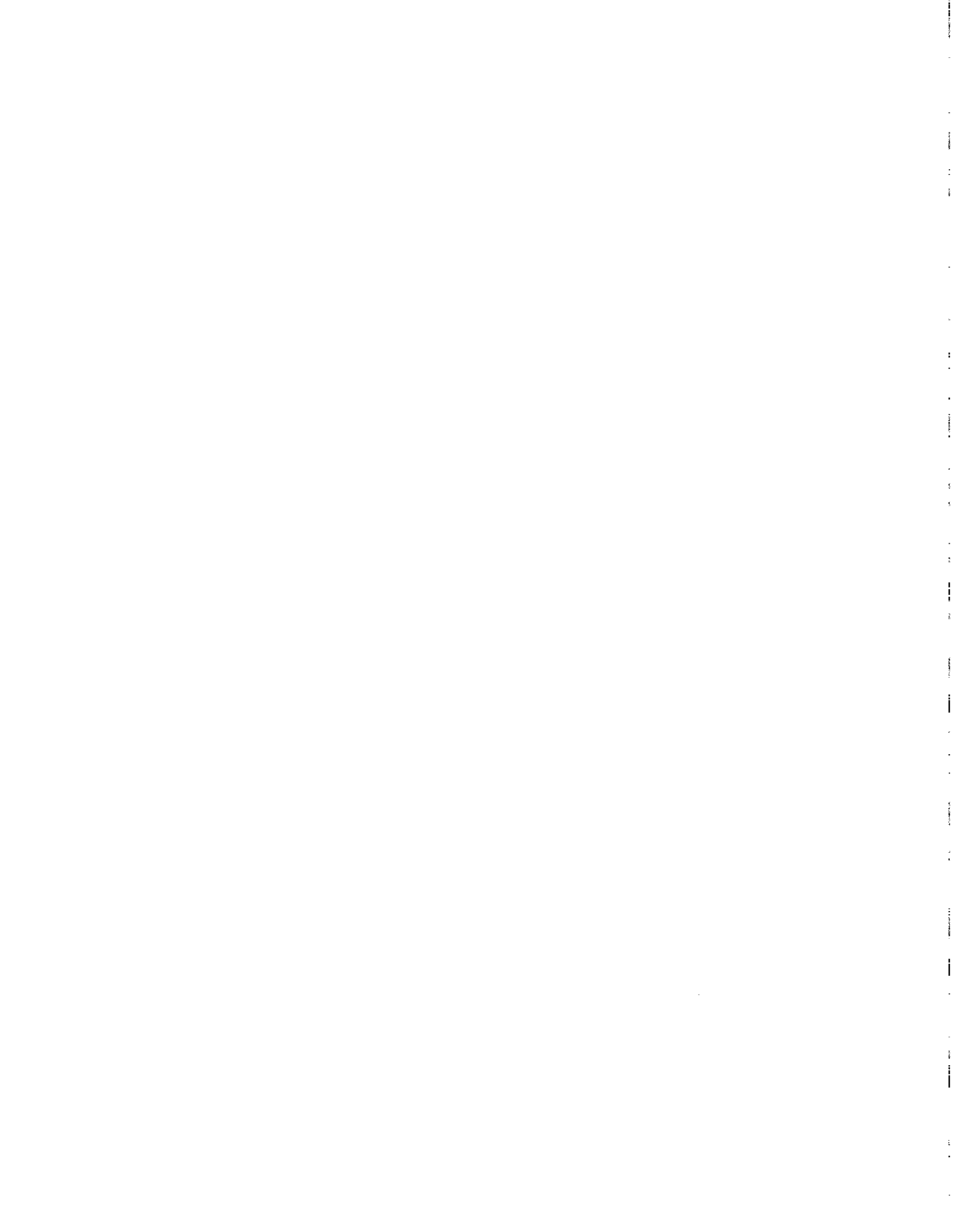
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