



UNITED STATES GENERAL ACCOUNTING OFFICE  
REGIONAL OFFICE  
ROOM 7000, FEDERAL BUILDING  
300 NORTH LOS ANGELES STREET  
LOS ANGELES, CALIFORNIA 90012

JUL 26 1973

Rear Admiral Philip Crosby  
Commanding Officer  
U. S. Navy Aviation Supply Office  
700 Robbins Avenue  
Philadelphia, Pennsylvania 19111

Dear Admiral Crosby:

As part of our review of ~~the negotiation of~~ contract prices under the provisions of Public Law 87-653, we have examined into the price proposed and negotiated for firm fixed-price contract N00383-71-C-2324 awarded to Talley Industries of Arizona, Mesa, Arizona, by the U. S. Navy Aviation Supply Office (ASO). The contract was awarded on January 19, 1971, in the amount of \$198,668 and provided for the production of inertia reels, actuators, and reel part kits.

Our examination was primarily concerned with the reasonableness of the price negotiated in relation to cost or pricing data available at the date of contract negotiations and the adequacy of technical and audit evaluations of the contractor's cost proposal.

Our review was limited to the costs proposed and negotiated for inertia reels because a Certificate of Current Cost or Pricing Data was not obtained from the contractor supporting costs proposed for actuators and reel part kits. Also, our review of proposed labor hours was limited to historical data on completed job orders for previous procurements as the contractor prematurely disposed of cost accounting records and supporting documents reflecting labor hours experienced on substantially or partially completed contracts for the same items. Accordingly, we were unable to completely determine if the most current experienced labor hour data was disclosed by the contractor in support of proposed costs.

We found that:

- The proposed and negotiated material costs were higher than indicated by cost data available at the time of negotiation by about \$15,900 including add-on pricing factors and profit.
- The proposed and negotiated labor costs were \$2,800 to \$9,000 higher than indicated by information available at the time of negotiation, including add-on pricing factors and profit.

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- The contract did not include a Price Reduction for Defective Cost or Pricing Data clause required by the Armed Services Procurement Regulation (ASPR).
- A Certificate of Current Cost or Pricing Data as required by ASPR was not obtained from the contractor in support of costs proposed for actuators and reel part kits.

BACKGROUND

Talley submitted a firm fixed-price proposal dated March 9, 1970, in the amount of \$127,949 in response to ASO's request for quotation (RFQ) N00383-70-Q-0351 for inertia reels. On November 24, 1970, Talley revised the proposed price to \$120,915 based on more current cost information. The Defense Contract Audit Agency (DCAA) performed a preaward audit of the original cost proposal for inertia reels. In addition, the following Talley firm fixed-price proposals for actuators and reel part kits totaling \$88,978 were combined with the inertia reel requirement in order to enhance the negotiation position.

<u>ASO RFQ</u>		<u>Talley proposal</u>	
<u>Number</u>	<u>Item</u>	<u>Date</u>	<u>Amount</u>
N00383-71-Q-0045	Actuator	8/28/70	\$15,276
N00383-71-Q-0162	Reel part kit	10/30/70	41,484
N00383-71-Q-0189	Reel part kit	10/29/70	32,518
		Total	<u>\$88,278</u>

Contract negotiations were concluded on December 2, 1970, and resulted in a total contract price of \$198,068, as follows:

<u>Item</u>	<u>P/N</u>	<u>Quantity</u>	<u>Unit price</u>	<u>Total</u>
Inertia reel	1293-17-1	95	\$1,228.22	\$116,681
Actuator	1000-146	6	2,240.50	13,443
Reel part kit	1293-150E1-2	88	437.00	38,456
Reel part kit	1293-17-102-1	388	76.00	29,488
		Total		<u>\$198,068</u>

The contractor executed a Certificate of Current Cost or Pricing Data on December 2, 1970, for costs in support of the proposal for inertia reels only. A defective pricing clause was not incorporated into the contract.

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## RESULTS OF REVIEW

### Material costs

We estimate that proposed material costs for inertia reels were higher than indicated by available cost information by about \$15,900 as a result of the contractor not disclosing the most current purchase data on ball screw assemblies used in the manufacture of the inertia reels prior to negotiations.

The contractor's initial cost proposal included a unit cost of \$199.50 for P/N 1293-55, ball screw assembly, based on a vendor quotation dated November 18, 1969. The DCAA preaward audit report recommended a price of \$125.00 a unit on the basis of prices paid by the contractor for the purchase of 500 units in April 1968. A large inventory of the units was on hand and could possibly meet the contract requirements.

Talley's revised proposal included a unit cost of \$287.50 for P/N 1293-55 based on a vendor quotation dated August 4, 1970, and reconfirmed on November 18, 1970. The price was accepted during negotiations on the basis that the contractor's existing inventory of ball screw assemblies was defective and had to be scrapped.

Our review showed that on November 3, 1970, 1 month prior to negotiations, the contractor issued a purchase order for the rework of 238 ball screw assemblies. The price was to be negotiated at a later date. A rework price of \$37.50 a unit was agreed to on March 9, 1971.

Talley officials advised us that the rework purchase order was not disclosed to the contracting officer because the magnitude of the problem was not known prior to negotiations.

In our opinion, however, the rework purchase order constitutes evidence of Talley's intent to have the units reworked and not scrapped which should have been disclosed to the contracting officer.

### Direct labor costs

The direct labor costs negotiated for inertia reels were higher than indicated by current data available prior to negotiation by from \$2,800 to \$9,000. This resulted because the contractor did not disclose to the contracting officer the most current labor hour data experienced on completed contracts for inertia reels.

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The contractor's initial cost proposal included 2,453 labor hours for 95 units or 25.8 hours a unit. The proposal was based on historical labor hours experienced in the production of inertia reels and gas generators under job orders (J/O's) 6292, 6417, 6527 completed between July and September 1968, and J/O 2182 completed August 1969. The experienced labor of 42.14 hours a unit was computed after deleting labor effort related to gas generators for J/O's 6527 and 2182. The estimate was judgmentally adjusted downward to 25.8 hours. The contractor was unable to provide us the basis for the adjustment.

In the revised proposal, Talley reduced the labor hour estimate to 2,157 or 22.7 hours a unit for labor costs questioned by DCAA in their audit of the contractor's original proposal. These hours were accepted in negotiations.

Our review showed that four additional job orders for the production of inertia reels were completed prior to negotiation of contract -2324 at significantly lower labor hours than proposed and negotiated. These orders, not disclosed to the contracting officer and not identified during the DCAA preaward audit, are summarized as follows:

<u>J/O</u>	<u>Date completed</u>	<u>Units</u>	<u>Average labor hours</u>
2177	2/7/69	26	17.5
2313	5/8/69	35	11.8
2359	6/20/69	5	9.2
2569	2/5/70	46	<u>20.8</u>
	Weighted average		<u>16.7</u>

Had the proposal been based on the labor hours experienced on these completed orders, Talley would have proposed 6 hours a unit less, or 570 hours for the total contract requirement. This amounts to about \$9,000. If the experienced data for J/O 2569, the most current completed job prior to negotiations, were used as an estimating basis, about 180 less hours would have been proposed, or about \$2,800 less than negotiated.

Talley officials acknowledged that labor hours experienced on recent production contracts had not been disclosed to the Government. These officials, however, stated that the historical labor hours recorded against J/O's 2177, 2313, and 2359 were understated because certain parts used in the manufacture of these units were produced under other job orders without corresponding cost transfers. They were unable, however, to furnish us any evidence to support this statement.

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In the performance of contract -2324, recorded labor hours in Talley's cost records for the production of inertia reels reflect 12.9 hours a unit. Under the circumstance, we have no basis for assuming that the recorded hours for J/O's 2177, 2313, and 2359 were not accurate representations prior to negotiation.

Defective pricing clause

Contract -2324 did not include a Price Reduction for Defective Cost or Pricing Data clause as required by ASPR 7-104.29. The contracting officer advised us that the omission of the clause was an administrative oversight.

The contracting officer further stated that failure to incorporate the defective pricing clause in the contract did not affect the Government's right to a price adjustment. Under the Christian Doctrine, all mandatory ASPR clauses are considered automatically included in the contract, although not physically included or cited therein. The contracting officer advised us that this position was concurred in by the ASO legal counsel.

Nevertheless, we believe the clause provides certain rights to the Government and accordingly should have been included in the contract.

Certificate of Current Cost  
or Pricing Data

A Certificate of Current Cost or Pricing Data was not obtained from the contractor prior to negotiations for cost proposed relative to actuators and reel part kits as required by ASPR 3-807.4. The contracting officer advised us that this also apparently resulted from an administrative oversight.

Under a recently issued decision of the Armed Services Board of Contract Appeals, a certificate is required as a condition precedent to a price reduction if data furnished is inaccurate, incomplete, or non-current. Thus, the certificate provides certain rights to the Government and should have been obtained from the contractor in support of costs proposed for actuators and reel part kits.

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We believe the contracting officer should consider the above findings, along with any additional information available, to determine whether the Government is legally entitled to a price adjustment under contract -2324.

Rear Admiral Philip Crosby  
Commanding Officer, U.S. ASO

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We would appreciate being advised of actions taken or contemplated with regard to the matters discussed in this letter. Copies of this letter are being sent to the Commander, Defense Contract Administration Services Region, and the Regional Manager, Defense Contract Audit Agency.

Sincerely yours,

James T. Hall, Jr.  
JAMES T. HALL, JR.  
Regional Manager

cc: Commander, DCASR, Los Angeles  
Regional Manager, DCAA, Los Angeles

bcc: Deputy Director, PSAD/GPM - J. H. Hammond  
Regional Manager, Philadelphia  
Assistant Director, PSAD/GPM - Charles Weinfeld