



COMPTROLLER GENERAL OF THE UNITED STATES  
WASHINGTON, D.C. 20548

RELEASED

SEP 17 1974

B-181493

76-0675

The Honorable John J. McFall  
House of Representatives



Dear Mr. McFall:

This is in further response to your letter of June 11, 1974, asking us to determine whether the Air Force determination and finding 74-16C-3, for the procurement of aircraft wheels and brakes from only three sources, violated the Armed Services Procurement Regulation and resulted in a restraint of trade.

Before issuing the determination and finding, the Air Force competitively procured various aircraft wheel and brake systems from Bendix Corporation, B. F. Goodrich Company, and Goodyear Tire and Rubber Company, commonly referred to as the original equipment manufacturers. As part of a defense program to increase competition and save money, the Air Force procured selected components from qualified producers other than the original equipment manufacturers. The Air Force later decided to terminate this program and to procure wheels and brake spare parts through negotiation with the three original equipment manufacturers, in order to maintain an adequate mobilization base.

On October 29, 1974, (B-181493), we reported that the Air Force decision did not violate procurement regulations. We agreed at that time to make a further evaluation after contracts were awarded to the original equipment manufacturers and, after sufficient time had elapsed, to permit these manufacturers to award subcontracts.

Department of the Air Force instructions for implementing the determination and finding required the original equipment manufacturers to identify the parts they would make or purchase and to establish a small business subcontracting program. The instructions also provided that items which the Air Force had previously procured from other than the original equipment manufacturers not revert to sole-source procurement from the original equipment manufacturers.

PSAD-76-18

702784

BEST DOCUMENT AVAILABLE

096819

Our primary emphasis, therefore, was to determine (1) whether procurement procedures required under the instructions implementing the determination and finding were properly followed, (2) whether items previously procured from the original equipment manufacturers reverted to sole-source procurements from these same manufacturers, and (3) the extent of small business participation in the original equipment manufacturers' subcontracting programs.

At Air Force-conducted conferences with each of the manufacturers, the items to be made and the items to be purchased were identified. Items to be purchased by the manufacturers were identified also by source and procurement method as small business, large business, or open competition. The Air Force also identified those items previously procured from other than the original equipment manufacturers so that none of the items reverted to a sole-source procurement from the original equipment manufacturers.

The Air Force had awarded contracts totaling \$38,477,000 for wheel and brake spare parts by March 31, 1975. Details on the extent of competition, compliance with make-or-buy provisions, and participation by small business firms follow.

#### EXTENT OF COMPETITION

Competitive procurement totaled \$6,757,000, or 18 percent of the total procurement. This amount included one contract valued at \$3,186,000 that was awarded to B. F. Goodrich on the basis of the best proposed delivery schedule for urgently needed requirements.

We did not find that any items procured from sources other than the original equipment manufacturers had reverted to a sole-source procurement from the original equipment manufacturers.

#### COMPLIANCE WITH MAKE-OR-BUY PROVISIONS

We reviewed the procurement files of 70 out of 100 subcontracts the original equipment manufacturers awarded.

The manufacturers, with only minor exceptions, were complying with the contractual requirements of the Air Force instructions implementing the determination and finding. Thus, the procurement procedures required by the determination and finding were properly followed.

EXTENT OF PARTICIPATION  
BY SMALL BUSINESS

The original equipment manufacturers awarded sub-contracts totaling \$736,000, or about 2 percent of the total procurement, to small business firms.

Small business participation is actually somewhat greater because components for many items to be made by the manufacturers are purchased under subcontracts awarded to small business firms. We did not identify the total dollar value of these transactions.

EXTENSION OF THE DETERMINATION AND FINDING

An Air Force official told us that the determination and finding had been extended for 3 months beyond fiscal year 1975, after which the Air Force plans to determine whether the basis for its issuance is still valid. The Air Force also plans to assess the impact the determination and finding has had on small business before it makes any further extension.

ACCOUNTING PRACTICES

In a previous review we noted that the wheel and brake industry had not charged product development costs directly to a contract for a new system but had identified those costs as indirect expenses and had allocated them to the sale of spare parts.

The industry allocates product development costs indirectly to orders for spare parts. This permits proposing lower prices on competitive contracts for developing new wheel and brake systems and recovering product development costs from sales of spare parts.

B-181493

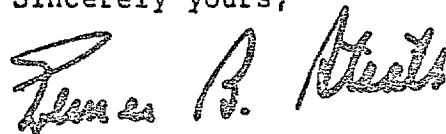
For 15 to 20 years the Government has accepted the accounting system the wheel and brake industry uses for accumulating and allocating such costs. In recent years the Defense Contract Audit Agency has questioned this method of accounting for product development costs, citing noncompliance with Armed Services Procurement Regulation 15-202 which states that "Costs identified specifically with the contract are direct costs of the contract and are to be charged directly thereto." Generally accepted accounting principles require that costs specifically identified with a contract be charged directly to that contract. We agree with the Agency's auditors' position. The Cost Accounting Standards Board staff has told us that the Board has undertaken research to lead to the development of certain cost accounting standards which should cover the problem of allocating these types of costs.

We discussed the issue of whether the determination and finding is a restraint of trade with the Bureau of Competition of the Federal Trade Commission. After it evaluated the data we presented, the Commission decided to make a preliminary investigation of this matter. You may want to follow up with the Commission on the results of its investigation.

As your office requested, we are providing copies of this letter to the Department of the Air Force.

We shall be pleased to discuss our report with you or members of your staff if you so desire.

Sincerely yours,



Comptroller General  
of the United States

DELETED COPY AVAILABLE