



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

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MAR 31 1965

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RELEASED

Dear Mr. Speaker:

In our review of certain aspects of the procurement of powder for .30 caliber blank ammunition, we found that the Government had incurred excessive costs that we estimate at over \$1 million because the Department of the Army permitted Remington Arms Company, Inc., a contractor with a cost-plus-a-fixed-fee contract, to procure the powder from a sole-source subcontractor, Olin Mathieson Chemical Corporation, without taking appropriate action to determine if the price was reasonable. Although the Government had previously procured similar powder at about \$0.90 a pound, the Army contracting officer approved Remington Arms' purchases at \$1.72 a pound without requesting a review of Olin Mathieson's cost. Remington Arms took no action to have the Army review Olin Mathieson's costs even though it had not previously procured powder of this type and had no valid basis for ascertaining the reasonableness of Olin Mathieson's price. Furthermore, even after the excessive prices were disclosed by the Army Audit Agency, contracting officials did not take timely action to obtain a lower price from Olin Mathieson.

Olin Mathieson earned profits amounting to about 162 percent of the cost of powder sold to Remington Arms during the period December 1958 to January 1962. When the excessive prices were eventually disclosed by an Army Audit Agency review, Olin Mathieson and the Army negotiated a significantly lower price for deliveries of powder beginning in April 1962. On the basis of the actual costs incurred, and by applying the rate of profit negotiated in 1962, we estimate that Olin Mathieson's billings of \$2.1 million for powder sold to Remington Arms from December 1958 to January 1962 were overstated by over \$1 million. In June 1962, and again in December 1963, the Department of the Army requested that Olin Mathieson make a voluntary refund of the excessive profits realized. However, Olin Mathieson refused, on the grounds that its overall profit pattern in recent years on defense business had been considerably below levels it considered acceptable for purposes of renegotiation.

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The Department of the Army, in commenting on our findings, agreed that Olin Mathieson had earned excessive profits and informed us that it had initiated further discussions with Olin Mathieson with the objective of obtaining an equitable adjustment. We were subsequently informed that Olin Mathieson had again refused to make any adjustment. On February 4, 1965, the Department of the Army notified Olin Mathieson that, in view of Olin Mathieson's refusal to enter into bona fide negotiations, this matter would be referred to the Department of Justice, the Army Contractor Performance Evaluation Group, and the Renegotiation Board for such action as those organizations deemed appropriate.

We believe that Olin Mathieson took unreasonable advantage of a sole-source procurement situation and established a price that resulted in profits greatly in excess of those considered normal in Government procurements. The fact that a contractor has not earned what it considers to be adequate profits on previous Government contracts does not justify its obtaining unreasonable profits on subsequent contracts. It is an established rule of Government procurement that each contract must "stand on its own" since contracts are sometimes intentionally undertaken at a loss to acquire production know-how, to obtain profitable follow-on contracts, or to broaden the contractor's production base on which to distribute fixed charges. However, in view of the actions already taken by the Department of the Army, we are making no further recommendations.

Both the Department of the Army and Remington Arms, Inc., disagreed with our conclusion that Remington Arms had not adequately protected the interests of the Government, pointing out that Remington Arms had initially attempted to obtain competition and had accepted Olin Mathieson's price quotation in good faith. However, our review disclosed that Remington Arms had information available to it indicating that the Government had previously purchased similar powder at a substantially lower price, yet took no action to have the Army look into the reasonableness of Olin Mathieson's price. In view of this, we do not believe that Remington Arms properly discharged its contractual responsibilities to protect the interests of the Government.

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We are reporting this matter to the Congress because it demonstrates the need for adequate price evaluation when there is no competition. Further, it also demonstrates a significant failure of contracting personnel to effectively discharge their responsibilities and protect the interests of the Government. The overpricing of negotiated contracts because of the submission of inaccurate cost data by contractors and the failure of Government procurement personnel to adequately review price proposals is a continuing problem. During the past several months we have issued a number of reports to the Congress pointing out significant overpricing of contracts, among which were overpricing of \$86,000 for amplifiers purchased by the Air Force, B-146954, December 28, 1964; and excessive costs of about \$1.5 million for gyroscopes procured by various Government contractors, B-146761, January 19, 1965.

Our numerous reports to the Congress disclosing the failure of Government contracting officials to obtain or fully evaluate cost information were the major factors which led to the enactment of Public Law 87-653. This law, which became effective December 1, 1962, provides that in negotiated procurements in excess of \$100,000, where competition is absent, contractors and subcontractors be required to submit cost or pricing data and that they certify to the currency, completeness, and correctness of such data. Also, the law provides that contract prices be adjusted in the event that such data are found to be inaccurate, incomplete, or noncurrent. To implement this law, the Armed Services Procurement Regulation was revised to furnish additional guidance to Government contracting officials and prime contractors and to place increased emphasis on the review and evaluation of cost and pricing data furnished by contractors and subcontractors. In our review of recent contract awards, we plan to examine into the manner in which agency officials are implementing the statute and current procurement instructions.

This report is also being sent today to the President of the Senate. Copies are being sent to the President of the United States, the Secretary of Defense, and the Secretary of the Army.

Sincerely yours,

Joseph Campbell

Comptroller General
of the United States

The Honorable John W. McCormack
Speaker of the House of Representatives