

July 21, 2006



Acquisition

Procurement Procedures Used for C-17
Globemaster III Sustainment Partnership
Total System Support
(D-2006-101)

Department of Defense
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Acronyms

ALC	Air Logistics Center
BCA	Business Case Analysis
CBA	Cost Benefit Analysis
SAF/GC	Secretary of the Air Force/General Counsel



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July 21, 2006

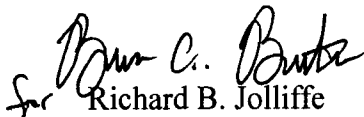
MEMORANDUM FOR ASSISTANT SECRETARY OF THE AIR FORCE
(FINANCIAL MANAGEMENT AND COMPTROLLER)

SUBJECT: Report on Procurement Procedures Used for C-17 Globemaster III
Sustainment Partnership Total System Support
(Report No. D-2006-101)

We are providing this report for information and use. We considered management comments on a draft of this report in preparing the final report.

Comments on the draft of this report conformed to the requirements of DoD Directive 7650.3 and left no unresolved issues. Therefore, no additional comments are required.

We appreciate the courtesies extended to the staff. Questions should be directed to Ms. Deborah L. Carros at (703) 604-9217 (DSN 664-9217) or Ms. Beth K. Schaefer at (703) 604-9232 (DSN 664-9232). See Appendix C for the report distribution. The team members are listed inside the back cover.


Richard B. Jolliffe
Assistant Inspector General
Acquisition and Contract Management

Department of Defense Office of Inspector General

Report No. D2006-101

July 21, 2006

(Project No. D2005-D000CK-0209.000)

Procurement Procedures Used for C-17 Globemaster III Sustainment Partnership Total System Support

Executive Summary

Who Should Read This Report and Why? Acquisition, contracting, and logistics personnel within DoD and the Military Departments should read this report because it concerns acquisition decisions that affect the long-term sustainment of the C-17 Globemaster III.

Background. The C-17 is a jet-powered strategic airlifter with a cabin offering large-volume capacity and a rear-loading assembly to accommodate wheeled or tracked vehicles. The aircraft was designed to airlift and airdrop loads, including armored vehicles, directly into a combat zone. The C-17 Globemaster III was developed by McDonnell Douglas Corporation, a wholly owned subsidiary of The Boeing Company (Boeing).

On October 1, 2003, the Air Force awarded McDonnell Douglas a letter contract (contract no. FA8614-04-C-2004) to provide sustainment for the C-17 through December 31, 2003, for an amount not to exceed \$259 million. The long-term sustainment contract was definitized on July 22, 2004, for \$871 million for FY 2004, and a potential value of almost \$5 billion (base year and four priced annual options). The contract, including the base year, four priced annual options, and three unpriced options, runs from FY 2004 through FY 2011. The Aeronautical Systems Center at Wright Patterson Air Force Base is the contracting activity.

Results. Air Force officials did not use an appropriate methodology for making the acquisition decision to procure contractor total system support for the C-17 aircraft. Specifically, the Air Force decision to award total system support responsibility was not based on a business case analysis. As a result, the Air Force awarded an \$871 million long-term contract (with a potential value of almost \$5 billion) without proper and necessary support and did not make fully informed sustainment strategy decisions. These decisions will impact future options for sustaining the C-17 when aircraft production is complete. Furthermore, unless the Air Force develops and completes a thorough business case analysis, the Air Force will increase the risk of implementing for the life of the aircraft a sustainment strategy that does not achieve best value. The business case analysis should be an objective analysis that thoroughly evaluates multiple sustainment options for the C-17 aircraft and ensures that the Government makes a knowledgeable best value decision for long-term sustainment (finding A).

Boeing invested in the Air Logistics Centers* through the C-17 Globemaster III Sustainment Partnership contract without an adequate legal basis to support the investment. Specifically, the contract requires Boeing to invest approximately

* The Air Logistics Centers include Oklahoma City, Warner Robins, and Ogden.

\$62 million in the Air Logistics Centers, primarily in the form of capital expenditures. As a result, the Air Force improperly augmented its congressional appropriation, potentially obscured true costs of the C-17 program, and potentially set a precedent for DoD contractors to make inappropriate financial investments at Government facilities. The Air Force needs to discontinue enforcing the requirements for investing in the C-17 Globemaster III Sustainment Partnership contract. In addition, the Air Force needs to determine what investment items have been delivered to the Air Logistics Centers, request the Defense Contract Audit Agency to validate the amount that Boeing has spent on investments in the Air Logistics Centers, make any necessary accounting corrections, and take other management actions as required (finding B). See the Finding sections for the detailed recommendations.

Management Comments and Audit Response. The Military Deputy, Office of the Assistant Secretary of the Air Force (Acquisition) concurred with the recommendation to conduct and complete a thorough business case analysis. The Air Force comments are responsive to the recommendation. As a result of management comments, we changed the requirement for a completed business case analysis to the second quarter FY 2009. On March 14, 2006, the Military Deputy nonconcurred with the recommendation to discontinue the investment requirement and the recommendation to identify, validate, and correct actions taken as a result of the investment; however, on July 13, 2006, the Military Deputy, Office of the Assistant Secretary of the Air Force (Acquisition) submitted additional comments stating that the Air Force will modify the current contractual arrangement to reflect sound management practices consistent with the recommendation. Specifically, the Air Force will develop new contract clauses and/or modify all appropriate C-17 Globemaster III Sustainment Partnership contract clauses to identify what core capability the investment will cover; specify the work to be performed at the Air Logistics Centers using the investment resources and track with appropriate metrics; and identify the connection between the investment resources and the core work being performed. The Military Deputy further stated that the Air Force will develop policy that will require future Air Force public-private partnership contracts to identify the resources being procured with private investment. The investments will be linked to the enhancement of specific core capabilities and the core work to be performed for contractors. The Military Deputy stated that the new policy will be in place within 6 months of the date of this report. The additional Air Force comments are responsive and meet the intent of the recommendation.

Although not required to comment, the Deputy General Counsel (Fiscal) provided comments in support of the Air Force legal opinion. The Deputy General Counsel (Fiscal) stated that under a public-private partnership agreement executed pursuant to section 2474(b)(2)(D), title 10, United States Code (10 U.S.C. 2474(b)(2)(D)), the Services may accept investments in the form of material, equipment, labor, and data from the private businesses, without impermissibly augmenting their appropriations. We disagreed with the DoD Office of the General Counsel comments. We contended that the meaning of 10 U.S.C. 2474(b)(2)(D) was clear in the context of the entire statute, that Congress was providing definite and limited tools whereby the Air Logistics Centers could sell their excess capacity to industry and thereby become centers of excellence and invest the funds received in plant, equipment, and commercial business ventures. However, the July 13, 2006 management comments satisfied our overall concerns, and therefore, we consider this issue closed.

A discussion of the management comments is in the Finding section of the report, and the complete text is in the Management Comments section.

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Background

The C-17 is a jet-powered strategic airlifter with a cabin offering large-volume capacity and a rear-loading assembly to accommodate wheeled or tracked vehicles. The aircraft was designed to airlift and airdrop loads, including armored vehicles, directly into a combat zone. It was developed by McDonnell Douglas Corporation, a wholly owned subsidiary of The Boeing Company (Boeing). See Figure below.

On October 1, 2003, the Air Force awarded McDonnell Douglas a letter contract (contract no. FA8614-04-C-2004) to provide sustainment for the C-17 through December 31, 2003, for an amount not to exceed \$259 million. The long-term sustainment contract was definitized on July 22, 2004, for \$871 million for FY 2004, and a potential value of almost \$5 billion (base year and four priced annual options). The contract, including the base year, four priced annual options, and three unpriced options, runs from FY 2004 through FY 2011. The Aeronautical Systems Center at Wright Patterson Air Force Base is the contracting activity.



C-17 Globemaster III Aircraft

Objectives

Our overall audit objective was to determine whether the C-17 Globemaster III Sustainment Partnership contract was procured in accordance with the Federal Acquisition Regulation. Specifically, we assessed whether Air Force officials used an appropriate methodology and rationale for making the acquisition decision to procure contractor total system support for the C-17. See Appendix A for a discussion of the scope and methodology and prior coverage related to the audit objectives.

A. Acquisition Decision for Total System Support Sustainment

Air Force officials did not use an appropriate methodology for making the acquisition decision to procure contractor total system support for the C-17 aircraft. Specifically, the Air Force decision to award total system support responsibility was not based on a business case analysis (BCA). This occurred because senior Air Force officials directed the C-17 Program Office to focus efforts solely on a partnership with Boeing without fully considering additional sustainment strategies. As a result, the Air Force awarded an \$871 million long-term contract (with a potential value of almost \$5 billion) without proper and necessary support and did not make fully informed sustainment strategy decisions. These decisions will impact future options for sustaining the C-17 when aircraft production is complete. Furthermore, unless the Air Force develops and completes a thorough BCA, the Air Force will increase the risk of implementing for the life of the aircraft a sustainment strategy that does not achieve best value.

C-17 Sustainment History

The Air Force originally planned to sustain the C-17 organically at San Antonio Air Logistics Center (ALC). However, in 1995, the Base Realignment and Closure Commission decided to close the San Antonio ALC. In 1996, in response to the closure, an Air Force General Officer Steering Group recommended implementing Flexible Sustainment Interim Contractor Logistics Support for the C-17 program and delaying the long-term sustainment decision until FY 2003, 2 years before the scheduled end of production of the aircraft.¹ The Flexible Sustainment strategy provided the Air Force near-term sustainment flexibility while preserving the options for establishing an organic depot, competing the contract in a contractor logistics support environment, or continuing the current contract strategy if it was determined to be the best value. In 1997, the Air Force Acquisition Strategy Panel approved the C-17 Flexible Sustainment strategy.

In its FY 1999 Report to Congress, the Air Force reported that it would evaluate the strengths of contractor and Government support and adopt an organic depot support strategy, competitively award a follow-on contract, or continue a long-term Flexible Sustainment contract with Boeing for C-17 long-term sustainment.

In 1999, the C-17 Program Office awarded a contract for the completion of a cost benefit analysis (CBA) that would demonstrate which sustainment approach for maintaining and supporting the C-17 weapon program would achieve the greatest cost savings and performance improvements. The CBA was to compare the costs for organic and contractor repair alternatives over the economic life of the system, including recurring and nonrecurring costs.

¹The scheduled end of production for the C-17 was later changed to FY 2008.

C-17 Sustainment Contract Decision

Air Force officials did not use an appropriate methodology or rationale for making the acquisition decision to procure contractor total system support for the C-17 aircraft. Specifically, the Air Force decision to award total system support responsibility to Boeing was not based on a BCA.

Business Case Analysis Guidance. The DoD “Performance-Based Logistics Program Manager’s Product Support Guide” (the Guide), November 10, 2004,² states that a BCA provides a best value analysis, considering not only cost, but also other quantifiable and nonquantifiable factors supporting an investment decision. According to the Guide, a BCA should be developed in an unbiased manner and not be constructed to justify a preordained decision. The BCA must be independent and able to withstand rigorous analysis and review by independent audit agencies. Specifically, the Guide explains that a BCA is an expanded CBA used in the initial decision to invest in a project. The BCA specifically guides the decision for selecting among alternative approaches. The BCA goes beyond cost benefit or economic analyses by linking each alternative to how it fulfills strategic objectives of the program. The Guide states that a BCA should determine the relative costs versus benefits of different support strategies.

In addition, Section 346 of Public Law 105-261, “Strom Thurmond National Defense Authorization Act for FY 1999,” October 17, 1998, as amended by Section 336 of Public Law 106-65, October 5, 1999, states that the Secretary of Defense or the head of a Military Department cannot enter a prime vendor contract for depot-level maintenance and repair of a weapon system, or other military equipment, before the end of a 30-day waiting period after submitting to Congress a report describing the nature, cost, impact, and competition procedures used to award the prime vendor support contract. The report should include an analysis of costs and benefits that demonstrates that using the prime vendor contract will result in savings to the Government over the life of the contract. In its FY 1999 Report to Congress, the Air Force stated that the Flexible Sustainment acquisition strategy preserved the three sustainment options pending the long-term depot support decision in FY 2003. However, the Air Force did not submit a report to Congress in accordance with the requirements of Section 346 of Public Law 105-261 when contracting officials awarded the total system support responsibility contract to Boeing in FY 2004.

C-17 Gatekeeper Reviews. The C-17 Program Office held periodic meetings for senior officials to discuss C-17 long-term sustainment direction and progress. The senior officials, called “Gatekeepers,” included the following offices: Office of the Assistant Secretary of the Air Force for Acquisition, Office of the Deputy Chief of Staff for Installations and Logistics, Headquarters Air Force Materiel Command, Headquarters Air Mobility Command, Program Executive Office for Airlift and Trainers, C-17 Program Office, and Boeing. Those meetings,

²The Guide supersedes DoD “Product Support for the 21st Century: A Program Manager’s Guide to Buying Performance,” November 6, 2001. The November 2001 guide recommended that program managers conduct a BCA to decide whether they should implement performance-based logistics for new and legacy systems.

subsequently referred to as Gatekeeper Reviews, were conducted approximately every 60 days to guide the program toward a mature FY 2003 long-term sustainment decision.

July 2001 Gatekeeper Review. During a July 31, 2001, Gatekeeper Review, the C-17 Program Director announced that Boeing would retain total system support responsibility for the C-17 life cycle. The C-17 Program Director further stated that Boeing would partner with the ALCs³ for a portion of the depot maintenance. At the same review, senior Air Force officials determined that the development of a C-17 CBA was no longer applicable because the CBA was creating a competitive environment between the ALCs and the contractor. Senior Air Force officials made these program decisions without a CBA and before the C-17 Program Office had completed a BCA. Senior Air Force officials also directed the C-17 Program Office to focus its efforts on a single strategy without fully considering additional sustainment options. This decision eliminated the opportunity to explore other sustainment approaches that may have produced greater cost savings.

Program Office Directed to Prepare BCA to Support Decision. The Air Force Principal Deputy Assistant Secretary for Acquisition and Management and the Deputy Chief of Staff for Installations and Logistics reiterated the July 31, 2001, decisions in a memorandum on January 31, 2002 (see Appendix B). The January 31, 2002, memorandum also directed the C-17 Program Office to prepare a BCA supporting the decision for Boeing to have total system support responsibility for the C-17 life cycle.

Long-Term Sustainment BCA. The C-17 Long-Term Sustainment BCA, dated June 6, 2003, documented the sustainment approach directed by Air Force officials and provided analysis supporting a performance-based partnership between the Air Force and Boeing. However, the BCA was incomplete because it focused on a Government-contractor sustainment partnership. The BCA did not compare C-17 sustainment costs with those of comparable aircraft, did not consider the assignment of noncore workload requirements that are essential to determining the relative costs versus benefits of different support strategies, and made no substantial evaluation of organic or contractor total sustainment capabilities.

Focus of the BCA. The BCA focused on a long-term Government-contractor sustainment partnership. The BCA summarized how the partnership was developed and described cost estimates associated with the partnership. The BCA stated that the objective of the partnership was to meet funded performance requirements issued by the Air Force while reducing currently planned and budgeted operating costs and providing value to the Air Force. One of the key topics excluded from the BCA was a CBA comparing costs for multiple sustainment options. A CBA should have compared the costs for organic and contractor repair alternatives over the economic life of the aircraft and included both recurring and nonrecurring costs.

³The ALCs include Oklahoma City, Warner Robins, and Ogden.

Comparison With Other Aircraft. The C-17 BCA did not compare estimated C-17 sustainment costs with sustainment costs of other comparable aircraft. However, in April 2005, the Air Force Cost Analysis Agency performed a comparison of the C-17 with comparable Air Force aircraft. The sum of cost per flying hour for the C-17 was reported to be much lower than that of the C-5 aircraft and higher than that of the C-141 aircraft when projected over an 11-year period. These results were based on full contractor logistics support for the C-17 and mostly organic support for the other two aircraft. The analysis concluded that C-17 contractor logistics support costs, when compared with the cost of other organically sustained aircraft, were reasonable with few exceptions.

Core Requirement Workload. Section 2464, title 10, United States Code requires DoD to maintain a core logistics capability of technical competencies and resources to meet national defense situations. The section states that core workloads include capabilities necessary to maintain and repair weapon systems and other military equipment identified as necessary to enable the Armed Forces to fulfill strategic and contingency plans. According to the Air Force Materiel Command Core Partnering Policy Implementation, noncore workloads are duties that do not satisfy a core capability and are managed or repaired at the depot level through a Government-contractor sustainment partnership agreement. The C-17 BCA states that core workloads are reserved for organic repair at the ALCs while all noncore depot maintenance workloads will be allocated in the future based on meeting performance requirements at best value.

According to the C-17 BCA, the C-17 Program Office restricted the initial partnership efforts to core workloads and did not discuss noncore workloads. According to the BCA, core capabilities will be transitioned to organic repair as they evolve at the ALCs and are biennially approved by the Secretary of the Air Force. Although approximately 95 percent of the C-17 workload is considered core, the C-17 Program Office should have evaluated both core and noncore workloads before making a long-term sustainment decision.

Conclusion

The Air Force awarded a long-term contract without proper and necessary support and did not make fully informed sustainment strategy decisions. These decisions will impact future options for sustaining the C-17 when aircraft production is complete. Without comparing C-17 sustainment costs with costs of comparable aircraft, thoroughly evaluating the option of organic sustainment, or including both core and noncore items in its analysis, the C-17 Program Office has no assurance that it selected the most suitable sustainment option. Furthermore, unless the Air Force develops and completes a thorough BCA, the Air Force will increase the risk of implementing for the life of the aircraft a sustainment strategy that may not achieve best value.

Recommendation, Management Comments, and Audit Response

Revised Recommendation. As a result of management comments, we revised draft Recommendation A. to change the completion date of the business case analysis to the second quarter FY 2009.

Recommendation A. We recommend that the Commander, Aeronautical Systems Center, Air Force Materiel Command direct the Program Director, C-17 Program Office to conduct and complete a thorough business case analysis before the end of second quarter FY 2009. The business case analysis should be an objective analysis that thoroughly evaluates multiple sustainment options for the C-17 aircraft and ensures that the Government makes a knowledgeable best value decision for long-term sustainment.

Management Comments. The Military Deputy, Office of the Assistant Secretary of the Air Force (Acquisition) concurred. However, the Military Deputy requested a revised completion date for the business case analysis. According to the Military Deputy, a key component of the business case analysis is a Post Production Support Plan. As the Air Force approaches a production shutdown decision, they plan to contract with Boeing to develop the Post Production Support Plan and complete the plan in the second quarter of FY 2008. The plan will address the production shutdown impact on Boeing's Long Beach facility and the post-production environment for its supplier team. The Military Deputy requested that we change the completion date requirement for the business case analysis to the second quarter FY 2009.

Audit Response. The comments are responsive, and no additional comments are required.

B. Contractor Investment in Partnering

Boeing invested in the ALCs through the Globemaster III Sustainment Partnership contract without an adequate legal basis to support the investment. Specifically, the contract requires Boeing to invest approximately \$62 million in the ALCs, primarily in the form of capital expenditures. This occurred because the former Secretary of the Air Force directed the C-17 Gatekeepers to construct an arrangement with Boeing to increase its efforts in the partnership through an investment into the ALCs. As a result, the Air Force improperly augmented its congressional appropriation, potentially obscured true costs of the C-17 program, and potentially set a precedent for DoD contractors to make inappropriate financial investments at Government facilities.

Contractor Investment

The Air Force required Boeing to invest in the ALCs through the Globemaster III Sustainment Partnership contract without an adequate legal basis to support the investment. Specifically, the contract requires Boeing to invest approximately \$62 million in the ALCs, primarily in the form of capital expenditures to increase organic capabilities related to C-17 sustainment.

Contract Requirement for Investment. The contracting office developed clause H-029 of the C-17 Globemaster III Sustainment Partnership contract requiring the contractor to make investments targeted at increasing ALC capabilities related to C-17 sustainment. The C-17 Program Office and Boeing agreed that Boeing would invest \$62 million over 5 years. The contract describes the investments as primarily capital expenditures, which may include material, labor, and data necessary to enhance C-17 organic maintenance at the ALCs. According to the contract clause, investment items come under the exclusive possession and control of the Government. The contractor is allowed to charge depreciation on the investments on this contract and other contracts. However, once fully depreciated, title to the investment passes to the Government.

Investment Equipment. According to Warner Robins ALC personnel, examples of equipment in which Boeing plans to invest include auxiliary power unit generators, landing gear repair equipment, and wing maintenance stands. As of October 31, 2005, Boeing had committed about \$29 million, of which it had spent \$5 million, in capital equipment and administrative costs for its investment into the ALCs.⁴ Boeing is required to segregate the commitments and costs for the investment items.

Depreciation of Equipment. Although the costs of the investments are not included in the price of the C-17 Globemaster III Sustainment Partnership contract, the contractor is allowed to indirectly charge the Government

⁴Amounts are contractor assertions; the Defense Contract Audit Agency has not verified the amounts with contractor accounting records.

depreciation expense for the capital investment items. The contract states that the Government will recognize depreciation expense for the investment items as indirect costs under this and other Government contracts to the extent those costs are otherwise allowable, allocable, and included in Boeing's overhead rates. However, Boeing has asserted that depreciation expenses referred to in contract clause H-029, computed using Boeing's established depreciation methods, will not be allocated to Government contracts but instead be recognized as a direct write-off to cost of sales for the contract. Boeing has also asserted that it cannot charge depreciation of the investment items to Government contracts because the capital investment items procured under clause H-029 are for the sole use of the ALCs performing C-17 sustainment activities and, therefore, are not allocable to other Boeing contracts. In addition, the allocation of depreciation for the capital investments to other contracts may result in a noncompliance with Cost Accounting Standard 418, "Allocation of Direct and Indirect Costs." Boeing stated that as of November 17, 2005, no capital investment items being built under the contract have been physically completed and placed into service at the ALCs.

Secretary of the Air Force/General Counsel Legal Opinion. On November 21, 2003, the Secretary of the Air Force/General Counsel (SAF/GC) issued a memorandum on the C-17 contractor investment in the ALCs. The SAF/GC found that the investment plan was consistent with applicable laws and policies. To determine compliance, SAF/GC reviewed three areas: core capability, fiscal law, and Office of the Secretary of Defense policy. SAF/GC found the investment items could be used to support the statutory requirement for a core capability. Additionally, SAF/GC stated that the Air Force did not improperly augment its appropriation because Boeing receives a benefit for its investment. Specifically, SAF/GC cited the ability to satisfy performance obligations and indirectly allocate depreciation expense to the Government as Boeing's benefits.

The SAF/GC memorandum also referenced a May 16, 2001, Under Secretary of Defense (Acquisition and Technology) memorandum that stated DoD contractors should not be encouraged or required to supplement DoD appropriations by bearing a portion of the contract cost for research and development contracts. SAF/GC stated that the policy was specifically related to contractor investment in research and development contracts, and while the policy could apply to the C-17 investment, it should not be applied because Boeing will benefit from the investment and associated depreciation costs.

Sufficiency of Legal Basis. SAF/GC found that the investment plan was consistent with applicable law and policy; however, we found that the investment was not legally sufficient. Under the Constitution, Congress provides funding for the activities of the Government. As a general rule, agencies may not accept funds from other sources without statutory authority. This policy prevents an agency from undercutting congressional power by exceeding the amount Congress has appropriated for a specific program. One such authority is the agency's authority to accept gifts. However, it is clear that the investments were not accepted as a gift under the Air Force's gift authority. The Air Force did not provide a statutory basis, authority, or exception as a basis for accepting the contractor investments. Without an appropriate legal basis for accepting the

investments, they would be deemed an improper augmentation of the Air Force appropriations.

Additionally, the Air Force potentially obscured true costs of the C-17 program by allowing Boeing to spread depreciation costs for the C-17 investment items as overhead to all of its Government contracts. By allowing costs for the C-17 investments to be spread across multiple contracts, the Air Force is potentially obscuring its true cost of the investment items from Congress and requiring other Government organizations to fund the ALC acquisition of capital equipment and other items for sustaining the C-17.

Lastly, the Air Force potentially set a precedent for DoD contractors to make inappropriate financial investments at Government facilities. According to Air Force personnel, the former Secretary of the Air Force planned to use the C-17 contractor investment as a precedent for other Government organizations.

Secretary of the Air Force Direction

The former Secretary of the Air Force directed the C-17 Gatekeepers to construct an arrangement with Boeing to increase Boeing efforts in the partnership through an investment into the ALCs. According to the C-17 contracting office, negotiations for the contract investment occurred at a senior level outside of the purview of the C-17 contracting office.

Secretary of the Air Force Briefing on C-17 Sustainment Decision. On September 22, 2003, the C-17 Program Office staff briefed the Secretary of the Air Force on the long-term sustainment decision for the aircraft. The C-17 Program Director recommended that the Air Force sustain the C-17 through contractor logistics support with total system support responsibility and implement partnerships between Boeing and the ALCs.

According to the C-17 Program Director, the former Secretary of the Air Force had concerns with the proposed C-17 long-term sustainment strategy and directed the C-17 Gatekeepers to revise the sustainment strategy. The former Secretary of the Air Force stated that long-term sustainment requires contractor investments into the partnership and that he expected Boeing to make investments into the ALCs. Further, the former Secretary of the Air Force anticipated that his suggested approach to partnering would be a model for other programs to follow.

Investment Negotiation. The former Secretary of the Air Force delayed the official long-term sustainment decision and directed the C-17 Gatekeepers to revise the long-term sustainment strategy to provide for an investment by Boeing into the ALCs. On November 18, 2003, the Deputy Chief of Staff for Installations and Logistics informed the former Secretary of the Air Force that the C-17 Program Office officials had negotiated an arrangement with Boeing to invest \$62 million into the ALCs over 5 years.

Other Matter of Interest

The Air Force has not incorporated into the C-17 Globemaster III Sustainment Partnership contract a Boeing core workload performance requirement to ensure the ALCs receive core items, nor has it incorporated contract metrics to track Boeing's compliance. The nonbinding preamble to the C-17 sustainment contract states that Boeing will be responsible, as a matter of contract, for ensuring that C-17 workload identified as core by Air Force Materiel Command is performed by the designated ALC. An attachment to the contract establishes core candidate workload for the ALCs. The C-17 Program Office stated that Boeing will be held responsible for ensuring the ALCs receive and perform core workload once the ALCs become qualified sources of repair for items listed in the attachment to the contract. The C-17 Program Office also stated that the Boeing performance requirement will be established in the contract by exercise of ALC Partnering Support Implementation Options.

Conclusion

Although the intent of Boeing's investment into the ALCs was to increase organic capabilities related to C-17 sustainment and increase Boeing's efforts in the partnership, the investment was not legally sufficient. Without sufficient legal basis for the contractor investment into the ALCs, the Air Force improperly augmented its congressional appropriation, potentially obscured true costs of the C-17 program, and potentially set a precedent for DoD contractors to make inappropriate financial investments at Government facilities.

Recommendations, Management Comments, and Audit Response

B. We recommend that the Assistant Secretary of the Air Force (Acquisition) direct the C-17 contracting office to:

1. Discontinue requirements of Clause H-029, "Boeing Investment in Partnering," of the C-17 Globemaster III Sustainment Partnership contract.

Management Comments. On March 14, 2006, the Military Deputy, Office of the Assistant Secretary of the Air Force (Acquisition) nonconcurred. The Military Deputy stated that the Air Force followed applicable guidance consistent with Public Law and DoD policy in formulating their long-term sustainment strategy. The Military Deputy cited section 2474, title 10, United States Code (10 U.S.C. 2474) as providing that the Secretary may authorize and encourage a Center of Industrial and Technical Excellence (i.e., designated Air Logistics Centers) to enter into a "public-private partnership" to achieve certain objectives. These objectives could include using private sector investment for plant and equipment recapitalization at a Center, or promoting commercial business ventures at a Center. The Military Deputy stated that the Air Force pursued and

achieved the investment encouraged by 10 U.S.C. 2474. In addition, the Military Deputy cited a Comptroller General ruling that there is no improper augmentation of an appropriation when the source providing the funds receives corresponding benefit. The Military Deputy stated because Boeing's investment provided a benefit to Boeing by aiding Boeing's ability to satisfy its performance obligation, the investment would not amount to an improper augmentation.

On July 13, 2006, the Military Deputy, Office of the Assistant Secretary of the Air Force (Acquisition) submitted additional comments stating that the Air Force will modify the current contractual arrangement to reflect sound management practices consistent with the recommendation. Specifically, the Air Force will develop new contract clauses and/or modify all appropriate C-17 Globemaster III Sustainment Partnership contract clauses to identify what core capability the investment will cover; specify the work to be performed at the Air Logistics Centers using the investment resources and track with appropriate metrics; and identify the connection between the investment resources and the core work being performed. The Military Deputy further stated that the Air Force will develop policy that will require future Air Force public-private partnership contracts to identify the resources being procured with private investment. The investments will be linked to the enhancement of specific core capabilities and the core work to be performed for contractors. The Military Deputy stated that the new policy will be in place within 6 months of the date of this report. For the full text of the Military Deputy, Office of the Assistant Secretary of the Air Force (Acquisition) comments, see the Management Comments section of the report.

Audit Response. The additional comments are responsive and meet the intent of the recommendation.

DoD Office of General Counsel Comments. Although not required to comment, the Deputy General Counsel (Fiscal) provided comments in support of the Air Force legal opinion. The Deputy General Counsel (Fiscal) stated that under a public-private partnership agreement executed pursuant to 10 U.S.C. 2474(b)(2)(D), the Services may accept investments in the form of material, equipment, labor, and data from the private businesses, without impermissibly augmenting their appropriations. The Deputy General Counsel (Fiscal) based this conclusion on the express terms of the cited subsection, the absence of any indication in the legislative history reflecting a contrary congressional intent, and the accepted cannon that remedial legislation, such as 10 U.S.C. 2474, should be construed liberally to accomplish its intended purpose (improvement of the industrial processes and business practices employed at DoD depot-level activities). Accordingly, the Deputy General Counsel (Fiscal) opinion is that Boeing's investment in the Air Logistics Centers does not constitute an improper augmentation of Air Force appropriations. For the full text of the DoD Office of General Counsel comments, see the Management Comments section of the report.

Audit Response. We disagreed with the DoD Office of the General Counsel comments. We contended that the meaning of 10 U.S.C. 2474(b)(2)(D) was clear in the context of the entire statute, that Congress was providing definite and limited tools whereby the Air Logistics Centers could sell their excess capacity to industry and thereby become centers of excellence and invest the funds received in plant, equipment, and commercial business ventures. We believed that if

Congress had intended that the Air Force could receive and retain “investment items,” and do so where no service is required to be performed by the Air Force, no such provision was made in the statute. However, the additional management comments on July 13, 2006 satisfied our overall concerns and we consider this issue to be closed.

2. Determine what investment items have been delivered to the Air Logistics Centers, request the Defense Contract Audit Agency to validate the amount that Boeing has spent on investments in the Air Logistics Centers, make any necessary accounting corrections, and take other management actions as required.

Management Comments. On March 14, 2006, the Military Deputy, Office of the Assistant Secretary of the Air Force (Acquisition) nonconcurred. The Military Deputy stated that the Air Force’s research into the history of the C-17 program and the policy in place at the time the strategy was formulated has reaffirmed the Air Force’s position that the investment Boeing brought to the partnership was appropriate at the time. On July 13, 2006 the Military Deputy responded with additional comments that were responsive and met the intent of the recommendation. See details of management comments to Recommendation B.1.

Audit Response. The additional comments are responsive and meet the intent of the recommendation.

Appendix A. Scope and Methodology

We evaluated whether Air Force officials used an appropriate methodology and rationale to award total system support responsibility for long-term sustainment of the C-17 Globemaster III to Boeing. Consequently, we focused the review on the strategy the Air Force used to make a long-term sustainment decision for the C-17 and the subsequent award of the C-17 Globemaster III Sustainment Partnership contract to Boeing.

We collected, reviewed, and analyzed documents dated from May 1996 through December 2005. Specifically, we evaluated acquisition and logistics documents that the Air Force used to support the long-term sustainment decision for the C-17. We also evaluated financial estimates for organic sustainment and contracting files for the C-17 Globemaster III Sustainment Partnership contract. We reviewed data the Defense Contract Audit Agency obtained from Boeing concerning cost and depreciation of investment items.

We interviewed contracting and logistics personnel at the C-17 Program Office at Wright Patterson Air Force Base. We also interviewed logistics and financial personnel at Warner Robins ALC. We interviewed personnel from the Air Force Cost Analysis Agency on sustainment costs for the C-17 compared with other Air Force aircraft.

We reviewed applicable contracting regulations including the Federal Acquisition Regulation, the Defense Federal Acquisition Regulation Supplement, and the Air Force Federal Acquisition Regulation Supplement. We also reviewed selected acquisition and logistics guidance on contractor logistics support and performance-based logistics.

We performed this audit from June 2005 through January 2006 in accordance with generally accepted government auditing standards. The audit scope was limited to the acquisition decision to award the C-17 Globemaster III Sustainment Partnership contract.

Use of Computer-Processed Data. We did not use computer-processed data to perform this audit.

Use of Technical Assistance. We did not require technical assistance for the execution of this audit.

Government Accountability Office High-Risk Area. The Government Accountability Office has identified several high-risk areas in DoD. This report provides coverage of the DoD Contract Management high-risk area.

Prior Coverage

During the last 5 years, the Air Force Audit Agency has issued three reports discussing C-17 sustainment. Unrestricted Air Force Audit Agency reports can be accessed at www.affa.hq.af.mil.

Air Force Audit Agency Report No. F2002-0002-C06400, "C-17 Integrated Product Team Participation-Phase IV," February 6, 2002

Air Force Audit Agency Report No. F2002-0001-C06400, "C-17 Integrated Product Team Participation-Phase III," December 7, 2001

Air Force Audit Agency Report No. 99064023, "C-17 Integrated Product Team Participation-Phase II," September 14, 2000

Appendix B. C-17 Sustainment Strategy Memorandum



DEPARTMENT OF THE AIR FORCE
WASHINGTON DC

JAN 31 2002

OFFICE OF THE ASSISTANT SECRETARY

MEMORANDUM FOR SEE DISTRIBUTION

SUBJECT: C-17 Sustainment Strategy

1. The Air Force strategy for future product support involves aggressively pursuing strong partnerships between the AF and its contractor counterparts. Our efforts on C-17 long-term sustainment, along with the associated FY03 CSAF/SECAF decision, have provided the AF and Boeing opportunities to capitalize on possible partnership solutions for C-17 sustainment requirements. This memo documents discussions and decisions made during past C-17 "Gatekeeper Meetings" (31 Jul 01, 17 Sep 01, and 20 Nov 01) that outline our path to C-17 sustainment.

a. Product support for the life cycle of the C-17 will be managed through a long-term performance-based partnership between Boeing and the AF. The objective of the partnership is to meet performance requirements while reducing operating costs. In this partnership, Boeing will retain Total System Support Responsibility (TSSR) for the C-17 life cycle and will commit to performance guarantees through a single contract. Partnerships with the Air Logistics Centers (ALCs) may include infrastructure investments at the ALCs. The AF reserves the option to transition all or portions of that responsibility to organic performance as circumstances dictate.

b. The C-17 Depot Support Strategy focus on performance-based partnerships is a change in the process flow, but the overall direction/intention is still unchanged. The timeframe for the long-term sustainment decision in FY03 and initial implementation in FY04 has not changed. Partnering transition can begin prior to FY04 if mutually agreed to by the ALCs and Boeing. These efforts must be within the context of current contract arrangements and offer the best value to the AF.

c. Depot Maintenance workload designated by the AF as "core" will be reserved for organic performance. All other depot maintenance workloads will be allocated based on meeting performance requirements at best value. As "core" requirements evolve and are approved by the CSAF and SECAF, they will be incorporated into the partnership agreements.

d. The C-17 System Program Director (SPD) and his counterparts will prepare a business case analysis (BCA) to support the SPD's final recommendation. The BCA will be based on a program office estimate and will be reviewed for sufficiency by SAF/FMC.

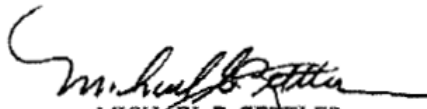
e. The C-17 SPD will comply with the processes as outlined in AFI 63-107, 29 May 01 (Integrated Product Support Planning and Assessment). The SPD will prepare the C-17 sustainment recommendation and coordinate with HQ AMC, HQ AETC, ALCs, and HQ AFMC/CC. The recommendation will be approved by SAF/AQ and AF/IL prior to submittal to

Appendix B. C-17 Sustainment Strategy Memorandum (cont'd)

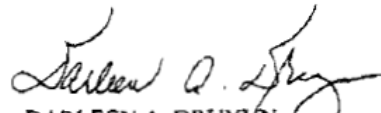
CSAF/SECAF in FY03. Interim heading checks, called "Gatekeeper Reviews," will be conducted approximately every 60 days with core players to include, but not limited to, the following offices: SAF/AQ, AF/IL, HQ AFMC, HQ AMC, AF PEO/AT, ASC/YC, WR-ALC, OC-ALC, OO-ALC, and Boeing. These interim checks will sort through issues and provide decisions as events evolve to guide the program toward the C-17 SPD's FY03 C-17 sustainment recommendation.

f. No specific pilot project status will be reported on the C-17 long-term sustainment effort. SAF/AQ and AF/IL will provide "top cover" for any innovative partnering, logistics concepts, and budgeting techniques proposed by the C-17 Gatekeeper Review Team.

2. The point of contact for C-17 sustainment direction is Col (S) Mike Carlson, ASC/YCL, DSN 785-1057. He is assisted by Ms. Edlene Flannery, ASC/YCL, DSN 785-1091; Lt Col Mike Then, ASC/YCLF, DSN 785-1495, and the C-17 Systems Support Manager, Lt Col Paul Dunbar, WR-ALC/LH, DSN 468-5411.



MICHAEL E. ZETTLER
Lieutenant General, USAF
DCS/Installations & Logistics



DARLEEN A. DRUYON
Principal Deputy Assistant Secretary
(Acquisition & Management)

cc:
SAF/AQC/AQQ/FM/FMC
HQ USAF/ILM/ILS

Appendix C. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition, Technology, and Logistics
Under Secretary of Defense (Comptroller)/Chief Financial Officer
 Deputy Chief Financial Officer
 Deputy Comptroller (Program/Budget)
Director, Program Analysis and Evaluation
Director, Defense Procurement and Acquisition Policy

Department of the Air Force

Assistant Secretary of the Air Force (Acquisition)
Assistant Secretary of the Air Force (Financial Management and Comptroller)
Auditor General, Department of the Air Force
Commander, Air Force Materiel Command
 Commander, Aeronautical Systems Center

Other Defense Organizations

Director, Defense Contract Audit Agency
Director, Defense Contract Management Agency

Non-Defense Federal Organization

Office of Management and Budget

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Homeland Security and Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Management, Finance, and Accountability,
 Committee on Government Reform
House Subcommittee on National Security, Emerging Threats, and International
 Relations, Committee on Government Reform

Department of the Air Force Comments

Final Report
Reference



DEPARTMENT OF THE AIR FORCE WASHINGTON DC

14 MAR 2006

OFFICE OF THE ASSISTANT SECRETARY

MEMORANDUM FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL
ATTN: DEPUTY INSPECTOR GENERAL FOR AUDITING

FROM: SAF/AQ

SUBJECT: Audit on Procurement Procedures Used for C-17 Globemaster III Sustainment
Partnership (GSP) Total System Support (Project No. D2005-D000CK-0209.000)

The Air Force appreciates the opportunity to review and comment on this draft DoD IG report. Air Force concurs to conduct and complete a thorough business case analysis (BCA) per DoD IG recommendation A, however, request your agreement on a revised completion date. We are planning to initiate the BCA in the 3rd quarter FY06. A key component of the BCA is a Post Production Support Plan (PPSP) and since we are getting closer to a production shutdown decision, we plan to contract with Boeing to develop the PPSP and complete the plan in the 2nd Quarter FY08. The PPSP will not only address the production shutdown impacts on Boeing's Long Beach facility (possible relocation, reduced sharing of overhead costs, calculation of new rates, etc.), but also the post-production environment for its supplier team (qualifying second sources, increased costs of spares and repairs, revising partnering Implementation Agreements, etc). Therefore, we would like you to reconsider the FY08 completion date and agree to 2nd quarter FY09.

Revised

The Air Force non-concurs with the recommendation (recommendation B.1) to discontinue requirements of Clause H-029 of the C-17 GSP contract. It is our opinion that we followed applicable guidance consistent with Public law and DoD policy in formulating our long-term sustainment strategy (the Globemaster III Sustainment Partnership).

We also non-concur with follow on recommendation (recommendation B.2) concerning investment. Our research into the history of the program and the policy in place at the time the strategy was formulated has reaffirmed our position that the investment Boeing brought to the partnership was appropriate at the time, and even more appropriate when considering today's vision of a true partnership. Attached is more detailed analysis that addresses our position.

My staff is ready to assist in any way to ensure all concerns are addressed prior to the final report publication. If you require further assistance, please contact my staff, Lt Col Joseph Wolfer at (703) 588-7737.

DONALD J. HOFFMAN, Lt Gen, USAF
Military Deputy, Office of the Assistant Secretary
of the Air Force (Acquisition)

Attachment:
Supporting analysis

Supporting Analysis for Response to Recommendation B:

DoD policy on Public-Private Partnerships for Depot Maintenance, 30 Jan 2002

Under Secretary of Defense (Logistics and Materiel Readiness) memorandum under "Policy", 2nd paragraph, 5th sub-bullet states, *"Where possible, partnerships should be structured in ways that encourage and justify private sector capital investment at the organic activity. In particular, this may involve multi-year arrangements."*

OSD Report on Public-Private Partnerships for Depot-Level Maintenance (July 2004)

Prepared for the Deputy Under Secretary of Defense (Logistics and Materiel Readiness) by The Joint Depot Maintenance Activities Group

Executive Summary

"...The desired end state is a dramatic increase in depot maintenance public-private partnerships, resulting in greater private sector investment in facilities and equipment, better facility utilization, reduced cost of ownership, workforce integration, and more efficient business processes."

The executive summary clearly states that the desired end state is to have greater private sector investment for depot level maintenance. In addition, on page II-13 there is a short paragraph and figure that depicts Actual Private and Public Sector Investment in Fiscal Year 2003 and earlier. The figure reflects \$8M in private sector investments for the Army, \$7.8M for the Air Force, and \$1.8M for the Navy. The second sentence states, *"Nine arrangements have actual investment from the private sector, and ten have actual investment from public sources."* Based on the information published in this DoD report it is apparent that private sector investment in the organic depot infrastructure was not only well known but encouraged by the DoD.

Excerpt from Appendix V of GAO Report "Depot Maintenance Public-Private Partnerships Have Increased, but Long-Term Growth and Results Are Uncertain", April 2003:

"Independent review and oversight provides an objective assessment of whether each partnership is achieving the expected benefits and that each partner performs as expected. Such a review also provides a basis for correcting or redirecting partnership efforts if expectations are not being met. To this end, OSD has begun a process to provide review and oversight of depot maintenance partnering efforts throughout the department. For example, OSD has directed its Joint Depot Maintenance Analysis Group to collect and maintain data on the conduct and performance of service partnerships. OSD plans to use these data to redirect and improve partnering efforts toward achieving DoD's goals and objectives."

Legal Determination:

DoD IG asserts that Boeing's agreement to make a \$62 million investment in the depots under the C-17 Globemaster III Sustainment Partnership (GSP) contract was legally insufficient. DoD IG states that agencies may not, as a general rule, accept funds from other sources without statutory authority. It points out, for example, that an agency can accept gifts under statutory authority; however, this particular investment was not treated as a gift. Finding no "appropriate legal basis for accepting the investments," DoD IG concluded that the investment was an improper augmentation of Air Force appropriations.

DoD IG's analysis ignores the circumstances of the investment, including the highly relevant facts that (1) there is a contractual relationship between the Government (the C-17 Systems Group) and Boeing as the prime contractor on the one hand for the sustainment of the C-17 aircraft, and (2) there is a partnership arrangement between the Government (the Air Logistics Centers (ALCs), including Warner-Robins ALC) and Boeing on the other hand to accomplish a portion of the work covered by the prime contract. In the latter arrangement, the depots can be viewed as a "subcontractor."

DSPA. In July 2002, the Air Force ALCs entered into a Direct Sales Partnering Agreement (DSPA) with Boeing. This DSPA was a public-private partnership concerning C-17 depot-level maintenance and repair, the legal authority for which included, *inter alia*, 10 U.S.C. § 2474. Under this agreement, Boeing is described as the "buyer" and the ALCs are referred to as the "sellers." The DSPA describes, among other things, the procedures by which Boeing places orders for work with the ALCs. These procedures expressly call out a "collaborative process" that includes Implementation Agreements and Direct Sales Ordering (DSO) Procedures. Article 11 of the DSPA provides coverage for the property administration and accountability requirements for Boeing property furnished for performance under a DSO.

Air Force and DoD Policy. This DSPA was entered into in furtherance of an Air Force memorandum, dated 15 April 2002, that emphasized the importance of partnerships in supporting weapon systems. This memorandum followed 30 January 2002 policy guidance to the Secretaries of the military departments from the Deputy Under Secretary of Defense for Logistics and Material Readiness, entitled "Public-Private Partnerships for Depot Maintenance." According to the DoD guidance, the specifically enumerated objectives of public-private partnerships include structuring the partnerships "in ways that encourage and justify private sector capital investments at [ALC] activities," and "leveraging private sector investments, such as facilities and equipment, to contribute to re-capitalization of depot maintenance activities."

10 U.S.C. § 2474. Section 2474 was amended by Section 341 of the National Defense Authorization Act, Fiscal Year 2001, Pub. L. No. 106-391, Oct. 30, 2000. One of the changes to § 2474 provided that the Secretary may authorize and encourage a Center of Industrial and Technical Excellence (*i.e.*, designated ALCs) to enter into a "public-private partnership" to achieve one or more of certain objectives, including "[t]o leverage private sector investment in – (i) such efforts as plant and equipment recapitalization for a Center; and (ii) the promotion of the

undertaking of commercial business ventures at a Center.” To its credit, the Air Force pursued, and achieved, the investment encouraged by Section 2474.

Comptroller General Decisions. Independent of Section 2474, the partnership investment is consistent with earlier Comptroller General decisions addressing appropriation augmentation issues. The general theory of “augmentation” stems from the constitutional requirement that “no money shall be drawn from the Treasury, but in Consequence of Appropriations made by Law . . .” U.S. CONST., Art. I, § 9. Thus, as a general proposition, the Air Force may not augment its appropriations from outside sources without specific statutory authority. An improper augmentation would occur if no benefit from the investment were available to Boeing. Conversely, so long as Boeing’s investment provides a benefit to Boeing (*e.g.*, the investment aids or facilitates Boeing’s ability to satisfy its performance obligations), the investment would not amount to an improper augmentation of an appropriation. The Comptroller General has ruled that there is no improper augmentation of funds when the source providing the funds receives a corresponding benefit. *See, e.g.*, 63 Comp. Gen. 459 (June 28, 1984) and 70 Comp. Gen. 597 (June 28, 1991). In both cited cases, the Comptroller General permitted the federal agency to accept a thing of value, so long as the provider was acting in its own best interest, and so long as the thing of value furthered the mission of the agency. Boeing’s investment in the ALCs clears both prongs.

DoD IG’s Legal Position. DoD IG’s legal position seems to place great emphasis on the role of the former Secretary in directing the C-17 Gatekeepers to negotiate Boeing investment in the depots. As discussed above, Secretarial direction to attempt such negotiations was consistent with DoD and Air Force policy to pursue public-private partnerships, as well as with Section 2474’s authority for the Secretaries of military departments to authorize and encourage public-private partnerships – all three of which include coverage for private sector investments. In short, the impetus for *how* the Air Force arrived at its negotiating position vis-à-vis Boeing is irrelevant.

What is important from a legal standpoint is that Boeing’s promise to invest in the depot was the result of a bargained-for exchange of consideration under circumstances where Boeing is the seller of C-17 sustainment effort to the Systems Group, as well as the buyer of a portion of that work from the ALCs. DoD IG’s position fails to recognize the fact that Boeing made such a promise in this larger contextual setting. In simple terms, the GSP contract requires Boeing to sustain C-17 aircraft. Boeing will perform the bulk of the work at Boeing facilities, using Boeing’s plant, equipment, and personnel. According to the DSPA, selected C-17 systems depot-level “core” maintenance and repair support requirements will be “subcontracted” by Boeing to ALCs. *See* 10 U.S.C. § 2464 for “core logistics capability.” Thus, it is in Boeing’s interest to ensure that the ALCs have the equipment necessary to perform required core work in a timely manner with high quality results.

Furthermore, as reflected in H-029 of the GSP contract, Boeing plays an integral role in determining what investment is made in the centers. Clause H-029, Contractor Investment in Air Logistics Center Capabilities, provides: “The contractor and the Air Force shall identify opportunities for investment, present them to the Depot Maintenance Activation Working Group (DMAWG), and execute those investments based on a mutual assessment of cost/benefit relative to other available C-17 investment opportunities as mutually agreed upon by Boeing and the

DMAWG.” Boeing’s investment in the C-17 GSP contract furthers the general objectives stated in the DSPA, which “represents the parties’ commitment to the common goals of implementing innovative, collaborative partnering and teaming to meet customer, contractual and statutory requirements.”

DoD IG’s conclusion misses the salient characteristics of the negotiations between contracting parties. Boeing made the investment as part of the give-and-take of the contracting process. Boeing’s investment in the C-17 GSP contract was fully supported by the exchange of consideration in this contract. The contract was freely negotiated between the parties, and the agreement binding. Most significantly, the arrangement was mutually beneficial to Boeing and the Air Force. The fact that the deal reflected in the GSP contract was mutually beneficial, as opposed to an Air Force directed action with no benefits for Boeing, undermines DoD IG’s conclusion that Boeing’s investment amounted to an improper augmentation of congressional appropriations.

Air Force General Counsel Opinion. As a final consideration, Boeing’s investment in the ALCs was supported by an opinion issued by the Air Force General Counsel. That opinion expressly considered the augmentation issue raised in the DoD IG report and concluded that “the contractor’s proposed investment plan is consistent with applicable law and policy.” DoD IG has not presented any law or facts that undermine the opinion expressed by the Air Force General Counsel.



DEPARTMENT OF THE AIR FORCE
WASHINGTON DC

OFFICE OF THE ASSISTANT SECRETARY

JUL 13 2006

MEMORANDUM FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL
ATTN: THE INSPECTOR GENERAL

FROM: SAF/AQ

SUBJECT: Audit on Procurement Procedures Used for C-17 Globemaster III Sustainment Partnership (GSP) Total System Support (Project No. D2005-D000CK-0209.000)

The Air Force (AF) appreciates the Department of Defense Inspector General's continued support and guidance regarding the C-17 GSP contract. To address your concerns with Boeing's \$62M investment in AF depots, the AF has decided to modify the current contractual arrangement to reflect sound management practices consistent with your recommendation B.1, and follow-on discussion with your office.

The AF will develop new, and/or modify all appropriate C-17 GSP contract clauses to: 1) identify what core capability the investment will cover, 2) specify the work to be performed at the Air Logistics Centers using the investment resources (track with appropriate metrics), and 3) identify the connection (link) between the investment resources and the core work being performed.

To ensure consistency with future AF contracts, the AF will develop policy that will require future AF public-private partnership contracts to identify the resources being procured with private investment and linking the investments to the enhancement of specific core capabilities and the core work to be performed for contractors. We plan to have this policy in place within 6 months after your final report is released.

Please feel free to contact Lt Col Keith Fletcher (703) 588-7743 if you have any further questions or concerns.

DONALD J. HOFFMAN, Lt Gen, USAF
Military Deputy, Office of the Assistant Secretary
Of the Air Force (Acquisition)

Department of Defense Office of General Counsel Comments



DEPARTMENT OF DEFENSE
OFFICE OF GENERAL COUNSEL
1600 DEFENSE PENTAGON
WASHINGTON, DC 20301-1600

MAY 11 2006

MEMORANDUM FOR OFFICE OF THE GENERAL COUNSEL, DEPARTMENT
OF THE AIR FORCE (ATTN: MR. DON FOX)

SUBJECT: Audit on Procurement Procedures Used for C-17 Globemaster III
Sustainment Partnership (GSP) Total System Support (Project No. D2005-D000CK-
0209.000)

This responds to your request for a legal opinion concerning the assertion in the referenced audit that Boeing's agreement to make a \$62 million investment in the depots under the C-17 Globemaster III Sustainment Partnership (GSP) contract improperly augmented Air Force appropriations.

This office has concluded that, under a public-private partnership agreement executed pursuant to title 10, United States Code, subsection 2474(b)(2)(D), the Services may accept investments in the forms of material, equipment, labor, and data from the private corporate parties to such agreements, without impermissibly augmenting their appropriations. We base this conclusion on the express terms of the cited subsection, the absence of any indication in the legislative history reflecting a contrary congressional intent, and the accepted canon that remedial legislation, such as 10 U.S.C. 2474, should be construed liberally to accomplish its intended purpose (here, improvement of the industrial processes and business practices employed at DoD's depot-level activities).

Accordingly, in our opinion, Boeing's investments in the Air Logistics Center (ALC), as described in the subject audit, do not constitute improper augmentations of Air Force appropriations.

Thank you for the opportunity to review the subject audit. Please let us know if we can provide further assistance in this matter.

A handwritten signature in black ink, appearing to read "E. Scott Castle".

E. Scott Castle
Deputy General Counsel
(Fiscal)

Team Members

The Department of Defense Office of the Deputy Inspector General for Auditing, Acquisition and Contract Management prepared this report. Personnel of the Department of Defense Office of Inspector General who contributed to the report are listed below.

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