

Inspector General

United States
Department of Defense



Accountability Was Missing for Government Property
Procured on the Army's Services Contract for Logistics
Support of Stryker Vehicles

Report Documentation Page

*Form Approved
OMB No. 0704-0188*

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1. REPORT DATE 30 NOV 2012	2. REPORT TYPE	3. DATES COVERED 00-00-2012 to 00-00-2012			
4. TITLE AND SUBTITLE Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles		5a. CONTRACT NUMBER			
		5b. GRANT NUMBER			
		5c. PROGRAM ELEMENT NUMBER			
6. AUTHOR(S)		5d. PROJECT NUMBER			
		5e. TASK NUMBER			
		5f. WORK UNIT NUMBER			
7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES) Inspector General of the Department of Defense, 400 Army Navy Drive, Arlington, VA, 22202-4704		8. PERFORMING ORGANIZATION REPORT NUMBER			
9. SPONSORING/MONITORING AGENCY NAME(S) AND ADDRESS(ES)		10. SPONSOR/MONITOR'S ACRONYM(S)			
		11. SPONSOR/MONITOR'S REPORT NUMBER(S)			
12. DISTRIBUTION/AVAILABILITY STATEMENT Approved for public release; distribution unlimited					
13. SUPPLEMENTARY NOTES					
14. ABSTRACT					
15. SUBJECT TERMS					
16. SECURITY CLASSIFICATION OF:			17. LIMITATION OF ABSTRACT Same as Report (SAR)	18. NUMBER OF PAGES 90	19a. NAME OF RESPONSIBLE PERSON
a. REPORT unclassified	b. ABSTRACT unclassified	c. THIS PAGE unclassified			

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Acronyms

ASA(ALT)	Assistant Secretary of the Army (Acquisition, Logistics, and Technology)
ASA(FM&C)	Assistant Secretary of the Army (Financial Management and Comptroller)
BDAR	Battle Damage Assessments and Repairs
CAP	Contractor-Acquired Property
CDRL	Contract Data Requirements List
CLIN	Contract Line Item Number
CLS	Contractor Logistics Support
DCMA	Defense Contract Management Agency
DFARS PGI	Defense Federal Acquisition Regulation Supplement, Procedures, Guidance, and Information
DoD FMR	DoD Financial Management Regulation
DPAP	Defense Procurement and Acquisition Policy
FAR	Federal Acquisition Regulation
GOCO	Government-Owned, Contractor-Operated
LMP	Logistics Modernization Program
PMO	Project Management Office
USD(AT&L)	Under Secretary of Defense for Acquisition, Technology, and Logistics
USD(C)	Under Secretary of Defense (Comptroller)
USSGL	U.S. Government Standard General Ledger



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
4800 MARK CENTER DRIVE
ALEXANDRIA, VIRGINIA 22350-1500

November 30, 2012

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION,
TECHNOLOGY, AND LOGISTICS
AUDITOR GENERAL, DEPARTMENT OF THE ARMY

SUBJECT: Accountability Was Missing for Government Property Procured on the
Army's Services Contract for Logistics Support of Stryker Vehicles
(Report No. DODIG-2013-025)

We are providing this report for information and use. We identified Government property (Army-owned inventory), valued at roughly \$892.3 million, that was not being valued or tracked in Army property accountability systems or on the financial statements. Our review of 21 high-dollar parts, valued at \$85.1 million, showed that 16 parts had excess Stryker inventory of \$72.7 million that could be either disposed of (\$58.0 million) or potentially used on other contracts (\$14.7 million). During the audit, we found 170 empty engine containers, valued at \$1.1 million, that General Dynamics determined could be used to store a different engine, thereby reducing future requirements. This report is the second of three reports on the effectiveness of the contractor logistics support strategy for the Stryker family of vehicles.

We considered management comments on a draft of this report when preparing the final report. Comments from the Director, Defense Procurement and Acquisition Policy; Assistant Secretary of the Army (Acquisition, Logistics, and Technology), in coordination with Assistant Secretary of the Army (Financial Management and Comptroller); and Program Executive Officer, Ground Combat Systems, conformed to the requirements of DoD Directive 7650.3; therefore, additional comments were not required.

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 604-9077 (DSN 664-9077).

Jacqueline L. Wicecarver
Jacqueline L. Wicecarver
Assistant Inspector General
Acquisition and Contract Management



Results in Brief: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles

What We Did

We evaluated the effectiveness of the contractor logistics support strategy for the Stryker Family of Vehicles. The Project Management Office for Stryker Brigade Combat Team (PMO Stryker) entered into the contract with General Dynamics Land Systems with a singular focus to achieve an operational readiness rate goal of 90 percent and actually achieved a readiness rate in excess of 96 percent. This report is the second in a series of three reports and addresses controls over Government property (Army-owned Stryker inventory). The first report addressed contract type and performance metrics. The third report will address contractor billings.

What We Found

PMO Stryker officials did not properly account for Government property procured on the cost-reimbursable services contract for logistics support of Stryker vehicles. We identified 19,365 different items of Stryker inventory (spare and repair parts) being managed by General Dynamics at a Government-owned, contractor-operated (GOCO) warehouse that had not been assigned a value and recorded in appropriate Army property accountability and financial accounting systems. At our request, General Dynamics assigned a value to the Stryker inventory of about \$892.3 million.

Stryker inventory was not properly accounted for because PMO Stryker inappropriately treated the inventory as contractor-acquired property (CAP), while General Dynamics considered the inventory as Government

property, not CAP, once delivered to the GOCO warehouse. Consequently, neither PMO Stryker nor General Dynamics accounted for the Stryker inventory in appropriate property management systems. CAP business rules for cost-reimbursable contracts were generally designed to address "*property acquired, fabricated, or otherwise provided by the contractor*" that would eventually be delivered to the Government as part of a higher level end item, not as used by the Army on its logistics services contract with no end item deliverable. While Stryker inventory consumed during the contract periods of performance for the logistics services contract could possibly be considered CAP, most of the inventory identified in this report was from prior contract periods and needed to be delivered and accepted by the Army as Government property.

As a result of incorrectly classifying Stryker inventory as CAP, PMO Stryker did not:

- comply with multiple DoD and Army property regulations designed to provide good stewardship and fiduciary responsibility over Government property, support the Army goal of creating auditable financial statements, and correctly use the Army's system designed to integrate logistics and financial operations; and
- implement a comprehensive inventory management improvement plan that addressed overforecasting, total asset visibility, excess inventory, economic retention requirements, and aggressive potential reutilization and disposal reviews

to meet the intent of Public Law 111-84, “National Defense Authorization Act for FY 2010,” Section 328, “Improvement of Inventory Management Practices,” October 28, 2009.

Our review of 21 high-dollar parts, valued at \$85.1 million, showed that 16 parts had excess Stryker inventory of \$72.7 million that could be either disposed of (\$58.0 million) or potentially used on other contracts (\$14.7 million). General Dynamics initiated action to dispose of different obsolete parts identified during our review.

During our visit to the GOCO warehouse in Auburn, Washington, we identified 170 empty engine containers (part 10650112), valued at \$1.1 million, purchased to store an engine that was no longer being procured. General Dynamics determined that the empty containers could be used to store a newer engine, thereby reducing future requirements. (See Appendix F for details on potential monetary benefits.)

Figure 1. Excess Engine Container



Source: Photograph Provided by PMO Stryker.

What We Recommend

Among other recommendations, the Director, Defense Procurement and Acquisition Policy (DPAP) working with the Assistant Secretary of Defense for Logistics and Materiel Readiness, needs to issue additional guidance that clarifies the proper use of CAP business rules specifically for logistics services contracts with no end item deliverables and how to properly account for inventory on these contracts that is

not consumed during the contract period of performance.

Additionally, the Program Executive Officer, Ground Combat Systems, should require that the Stryker inventory be delivered and accepted on a contract line item, properly valued, recorded in an Army property accountability system, and stratified and classified in the proper logistics and financial accounts. Also, the Program Executive Officer, Ground Combat Systems, should require the PMO Stryker to implement a comprehensive inventory management improvement plan that addresses overforecasting, total asset visibility, excess inventory and economic retention requirements, and aggressive potential reutilization and disposal reviews.

Further, the Assistant Secretary of the Army (Acquisition, Logistics, and Technology) [ASA(ALT)], with support from the Assistant Secretary of the Army (Financial Management and Comptroller) [ASA(FM&C)], needs to establish a multifunctional support team to work with PMO Stryker to ensure that Stryker inventory has been assigned a value and recorded in appropriate Army property accountability and financial accounting systems.

Management Comments and Our Response

Management comments were responsive to the recommendations, and management was taking action to address Stryker inventory acceptance, accountability, and financial reporting issues. The Director, DPAP, planned to issue guidance during the second quarter of FY 2013 that clarifies the property accountability and financial valuation requirements for inventory that was not consumed during the period of performance on logistics services contracts. Additionally, ASA(ALT), with support from ASA(FM&C), established a multifunctional support team to assist PMO Stryker in properly valuing and recording Stryker inventory. See the Recommendations Table on the next page.

Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
Director, Defense Procurement and Acquisition Policy		1
Assistant Secretary of the Army (Acquisition, Logistics, and Technology)		4
Assistant Secretary of the Army (Financial Management and Comptroller)		4
Program Executive Officer, Ground Combat Systems		2.a, 2.b, 2.c, 2.d, 2.e, 2.f, 2.g, 2.h, 3, 5.a, and 5.b

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Introduction

Objectives

The overall objective of the audit was to evaluate the effectiveness of the contractor logistics support (CLS) sustainment strategy for Stryker vehicles. Specifically, we reviewed contract funding procedures, contract type, performance metrics, contractor billings, and controls over Government property that is being managed by the contractor. See Appendix A for a discussion of the scope and methodology and prior audit coverage.

This report is the second in a series of three reports and addresses controls over Government property (Army-owned Stryker inventory). The first report, DODIG-2012-102, “Better Cost-Control Measures Are Needed on the Army’s Cost-Reimbursable Services Contract for Logistics Support of Stryker Vehicles,” June 18, 2012, addressed contract type and performance metrics. The third report will address contractor billings.

We performed this audit pursuant to Public Law 110-417, “Duncan Hunter National Defense Authorization Act for Fiscal Year 2009,” Section 852, “Comprehensive Audit of Spare Parts Purchases and Depot Overhaul and Maintenance of Equipment for Operations in Iraq and Afghanistan,” October 14, 2008. Section 852 requires:

thorough audits to identify potential waste, fraud, and abuse in the performance of the following: (1) Department of Defense contracts, subcontracts, and task and delivery orders for—(A) depot overhaul and maintenance of equipment for the military in Iraq and Afghanistan; and (B) spare parts for military equipment used in Iraq and Afghanistan.

Background

U.S. Army TACOM Life Cycle Management Command

The U.S. Army TACOM¹ Life Cycle Management Command is headquartered in Warren, Michigan, and is a major subordinate command of the U.S. Army Materiel Command. According to the Army Web site,² the Life Cycle Management Command is a collaborative organization whose mission is to develop, acquire, field, and sustain soldier and ground systems for the warfighter through the integration of effective and timely acquisition, logistics, and cutting-edge technology. The Life Cycle Management Command facilitates partnerships between the Army Contracting Command and the collocated Program Executive Offices so that they can cooperatively provide the full range of life-cycle management services for the weapon systems that they support.

¹ TACOM was formerly known as the Tank-automotive and Armaments Command.

² The Web site source is <http://www.tacom.army.mil/main/index.html>.

Army Contracting Command

The Army Contracting Command-Warren, Michigan, previously referred to as TACOM Contracting Center, is at the TACOM Life Cycle Management Command. The contracting command is responsible for acquisition support and contracting for many of the Army's major weapon systems. The full range of services includes acquisition, fielding, contracting, business advisory, production support, and sustainment of TACOM Life Cycle Management Command systems.

Assistant Secretary of the Army (Financial Management and Comptroller)

The Assistant Secretary of the Army (Financial Management and Comptroller) [ASA(FM&C)], according to its Web site,³ is responsible for formulating, submitting, and defending the Army's budget to Congress and the American people and for overseeing the proper and effective use of the appropriated resources to accomplish the Army's assigned missions. ASA(FM&C) prepares and distributes both the Army Working Capital Fund and the Operation and Maintenance budgets. ASA(FM&C) also is responsible for preparing the Army's financial statements and ensuring that the Army is working toward obtaining auditable financial statements.

Project Management Office Stryker Brigade Combat Team

The Project Management Office, Stryker Brigade Combat Team (PMO Stryker), is a subsidiary office of the Program Executive Office, Ground Combat Systems, which is under the command of the Assistant Secretary of the Army (Acquisition, Logistics, and Technology) [ASA(ALT)]. According to the Army Web site,⁴ the mission of the PMO Stryker is to provide proven superior acquisition, development, and sustainment of the Stryker family of vehicles that afford the warfighter quick-response maneuvering, enhanced survivability and lethality, expanded fight versatility, and proven tactical agility.

General Dynamics Land Systems

General Dynamics Land Systems (General Dynamics), according to its Web site,⁵ is an international Defense contractor that offers a wide array of land and amphibious combat systems, subsystems, and components. General Dynamics produced the first Stryker vehicles in 2002. In addition to the Stryker, General Dynamics developed a variety of other combat vehicles, such as the Light-Armored Vehicle, M1 Abrams tank, Fox vehicle, Mine-Resistant Ambush-Protected vehicle, and Expeditionary Fighting vehicle.

³ The Web site source is <http://www.asafm.army.mil>.

⁴ The Web site source is <http://www.peogcs.army.mil/sbct.html>.

⁵ The Web site source is <http://www.gdls.com>.

The Stryker Family of Vehicles

The Stryker family of vehicles is a 19-ton, 8-wheeled, armored vehicle platform composed of 17 configurations (10 basic and 7 double-v hull configurations). The overall mission of the Stryker, originally named the “Interim Armored Vehicle,” is to enable soldiers to maneuver more easily in close quarters and urban terrain while providing protection in the open terrain. The Stryker family of vehicles consists of the:

1. Infantry Carrier Vehicle (see Figure 2)*
2. Reconnaissance Vehicle
3. Mortar Carrier Vehicle*
4. Commander’s Vehicle*
5. Fire Support Vehicle*
6. Engineer Squad Vehicle*
7. Medical Evacuation Vehicle*
8. Anti-Tank Guided Missile Vehicle*
9. Nuclear, Biological, Chemical, Reconnaissance Vehicle
10. Mobile Gun System Vehicle

*Vehicle also has a double-v hull configuration.

Figure 2. Stryker “Infantry Carrier Vehicle”



Source: www.sbct.army.mil.

The Stryker family of vehicles acquisition plan states that:

Comprehensive Contractor Logistics Support (CLS) is executed under a performance based contract supporting both garrison and deployment vehicles. The contractor is co-located with the units and provides National level maintenance and assists with field level maintenance. **They [General Dynamics] request, receive, store and issue all CLS items as well as document part consumption and vehicles repairs.** The contractor performs all scheduled services as well [as] repair services for all components or assemblies with the exception of defined Government Furnished items. CLS supports vehicles at all locations. Under CLS, GDLS [General Dynamics Land Systems] maintains the Stryker vehicles to a “fully mission capable” status. **[emphasis added]**

PMO Stryker Explanation of Operational Complexities

The Stryker family of vehicles acquisition program began before the events that would lead us to war in Iraq and Afghanistan. As a part of acquisition reform, the Stryker vehicle was a nondevelopmental item, lending itself to a performance-based logistics approach through the use of CLS because the technical data for the vehicle were not readily available. PMO Stryker stated that the pace of acquisition became an extremely rapid effort that took 31 months from contract award to the initial operational deployment in Iraq.

In addition to the rapid effort, the Army's deployment needs created complexities requiring concurrent development and production of a common chassis for the 10 original Stryker variants before completion of production verification testing. Additionally, the program had little operational tempo data from garrison deployments that could be used to identify performance-based logistics metrics for deployment, as well as the first brigade deployment to Iraq, which included CLS, that was in October 2003. This escalated to three Stryker brigades deployed to Iraq in 2006, that required sustainment for 2 years. As brigades were eventually redeploying from Iraq, other brigades were deploying to Afghanistan. The Stryker brigades were now spread across two operational theaters with differing environments, operational tempos, and threats.

Metrics gathered from one theater were not applicable to the new theater. The new threat in Afghanistan led to an urgent requirement to change the design of the flat-bottom Stryker vehicles to a more survivable double-v hull model. Design, test, production, and fielding were accelerated to get this new design into the hands of the soldier within 18 months. This added another new complexity to fleet support as both flat-bottom and double-v hull vehicles required support. The Army deployed a second Stryker brigade to Afghanistan, requiring additional CLS support. The double-v hull vehicles increased the variants to 17, which caused additional development, production, and sustainment complexities. The deployed fleet increased operational miles 10-fold from when fleets were in garrison/peacetime deployment. The operational environment, tempo, objectives, deployment, and utilization plans were all fluid as the threat would change in theater, creating a higher level of complexity for identifying performance-based logistics metrics.

A total of 17 Stryker Brigade Combat Teams were deployed across both theaters and accumulated an estimated 40 million miles. In addition, 80 brigade vehicles were lost in battle, 463 vehicles were damaged, and 3,464 vehicles were reset. Numerous retrofit applicable engineering change proposals and engineering change orders were developed since 2005, and 320 kits were developed or fielded to primarily address survivability issues in both Iraq and Afghanistan. As expected, the increased weight of these kits increased the failure rates of various drive-train and suspension components. Theater repair sites could not keep up with the volume of components requiring repair, so increased quantities of configuration spares were procured to meet operational vehicle readiness requirements. When newly designed/improved components were successfully tested and validated, they were incorporated into the supply system, either immediately replacing an existing part or replacing the part once it was totally depleted from the supply system, depending on the nature of the required design improvement.

Stryker/General Dynamics CLS Contracts

On December 21, 2006, the Army Contracting Command-Warren officials awarded General Dynamics a 6-year (base year and 5 option years), cost-plus-fixed-fee, CLS contract. As of March 2012, the contract was funded for about \$1.5 billion,⁶ including fees or profit of \$133.2 million (contract W56HZV-07-D-M112 delivery orders 0019, 0169, and 0269). As described in the acquisition plan, General Dynamics is responsible for performing scheduled and unscheduled maintenance; requesting, receiving, storing, and issuing all Stryker vehicle spares and repair parts; and documenting all part consumption and vehicle repairs. General Dynamics provides CLS to maintain all Stryker garrison and deployment⁷ vehicles at a fully mission-capable status. PMO Stryker entered into the contract with General Dynamics with a singular focus to achieve an operational readiness rate goal of 90 percent and actually achieved a readiness rate in excess of 96 percent. A follow-on Stryker logistics support contract is scheduled to be awarded in June 2013.

General Dynamics Manages the GOCO Facility Where Stryker Inventory Was Stored

General Dynamics has responsibility for managing both the wholesale and retail Stryker inventory. Wholesale distribution locations maintain bulk quantities of spare and repair parts, and the retail distribution locations store smaller quantities and provide the parts directly to the end users who maintain the vehicles. The principal wholesale distribution location is a Government-owned, contractor-operated (GOCO) warehouse in Auburn, Washington. The warehouse has about 700,000 square feet of internal storage space and 30,000 square feet of external storage space. General Dynamics' personnel receive, store, manage, and issue Stryker inventory for a variety of Stryker efforts, including CLS, battle damage assessments and repairs (BDAR), Reset, and retrofit.⁸ For purposes of this report, the Stryker inventory values, quantities, and demand information will incorporate data from the CLS, BDAR, and Reset efforts because the inventory for these three efforts are comingled and could be used interchangeably to fulfill requirements for any of the efforts as needed.

Figure 3 shows the inside of the GOCO warehouse in Auburn and the commander's seats (part LS1009617) that were stored in the warehouse.

⁶ Contract value of \$1.523 billion includes only CLS contract line items of more than \$40 million.

⁷ "Garrison" describes Stryker vehicles stationed at a permanent military post. "Deployment" describes Stryker vehicles that are deployed in theater to support a military operation.

⁸ Reset efforts are performed on Stryker vehicles returning from Iraq and Afghanistan to bring the vehicles back to a fully mission-capable condition. Retrofit efforts are also performed to add new part requirements to a Stryker vehicle that were not part of the original production requirements.

Figure 3. Interior of the GOCO Warehouse in Auburn



Source: Photograph provided by PMO Stryker.

General Dynamics also managed two other Stryker inventory wholesale warehouses at its London, Ontario Canada, facility and the GOCO European Distribution Center in Germersheim, Germany. The retail locations for the Stryker inventory are geographically dispersed to support Stryker mission requirements around the world.

Review of Internal Controls

DoD Instruction 5010.40, “Managers’ Internal Control Program (MICP) Procedures,” July 29, 2010, requires DoD organizations to implement a comprehensive system of internal controls that provide reasonable assurance that programs are operating as intended and to evaluate the effectiveness of the controls. We identified internal control weaknesses for ASA(ALT) and PMO Stryker officials. Specifically, PMO Stryker officials did not treat the Army-owned Stryker inventory as Government property, and as a result, the Stryker inventory was not properly valued and recorded in appropriate Army property accountability and financial accounting systems. Also, PMO Stryker officials did not implement a comprehensive inventory management improvement plan that complied with the DoD comprehensive plan for inventory management as required by Public Law 111-84, “National Defense Authorization Act for FY 2010,” Section 328, “Improvement of Inventory Management Practices,” October 28, 2009. We will provide a copy of the report to the senior Army officials responsible for internal controls.

Finding. Inadequate Controls Over Contractor-Managed Government Property

PMO Stryker officials did not properly account for Government property procured on the cost-reimbursable services contract for logistics support of Stryker vehicles. We identified 19,365 different items of Stryker inventory (spare and repair parts) managed by General Dynamics, primarily at a GOCO warehouse, that had not been assigned a value and recorded in appropriate Army property accountability and financial accounting systems. At our request, General Dynamics assigned a value to the Stryker inventory of about \$892.3 million. Stryker inventory was not properly accounted for because PMO Stryker inappropriately treated the inventory as contractor-acquired property (CAP), while General Dynamics considered the inventory as Government property, not CAP, once delivered to the GOCO warehouse. Consequently, neither PMO Stryker nor General Dynamics accounted for the Stryker inventory in appropriate property management systems. CAP business rules for cost-reimbursable contracts were generally designed to address “*property acquired, fabricated, or otherwise provided by the contractor*” that would eventually be delivered to the Government as part of a higher level end item, not as used by the Army on its logistics services contract with no end item deliverable. While Stryker inventory consumed during the contract period of performance for the logistics services contract could possibly be considered CAP, the inventory identified in this report had accumulated over many contract years and different periods of performance and needed to be officially delivered and accepted by the Army and accounted for as Government property. As a result of incorrectly classifying Stryker inventory as CAP, PMO Stryker did not:

- comply with multiple DoD and Army property regulations designed to provide good stewardship and fiduciary responsibility over Government property, support the Army goal of creating auditable financial statements, and correctly use the Army’s system designed to integrate logistics and financial operations; and
- implement a comprehensive inventory management improvement plan that addressed overforecasting, total asset visibility, excess inventory and economic retention requirements, and aggressive potential reutilization and disposal reviews to meet the intent of Public Law 111-84, “National Defense Authorization Act for FY 2010,” Section 328, “Improvement of Inventory Management Practices,” October 28, 2009.

We reviewed 21 high-dollar parts, valued at \$85.1 million, and found 16 parts had excess Stryker inventory of \$72.7 million that could be either disposed of (\$58.0 million) or potentially used on other contracts (\$14.7 million). For example, we found 170 empty engine containers, valued at \$1.1 million, that General Dynamics determined could be used to store a different engine, thereby reducing future costs. General Dynamics also initiated action to dispose of four different obsolete parts identified during our review.

Stryker Inventory Was Not Assigned a Value and Recorded in Appropriate Army Accountability and Financial Accounting Systems

We identified 19,365 different items of Army-owned Stryker inventory (spare and repair parts) being managed by General Dynamics, primarily at a GOCO warehouse in Auburn that were not assigned a value and recorded in appropriate Army property accountability and financial accounting systems. At our request, General Dynamics used several sources to assign a value of about \$892.3 million to 16,344 parts (\$676.2 million related to CLS Stryker inventory and \$216.1 million related to Reset, BDAR, and Retrofit efforts) but was unable to determine a value for the remaining 3,021 parts for various reasons. General Dynamics also provided the following disclaimer to the assigned inventory value.

DISCLAIMER: The information contained in this document has been prepared solely for information purposes in response to specific DOD Inspector General requests regarding **existing government owned inventory**. The information as presented herein is not an official record or deliverable of General Dynamics or any of its subsidiaries and should not be relied upon for any decision, analysis or evaluation regarding government owned inventory valuation. **The data herein has not been verified or validated for accuracy, particularly with respect to dollar valuations. [emphasis added]**

Table 1 shows a breakdown of the Stryker inventory that was not recorded or assigned a value in an Army property accountability system.

Table 1. Stryker Inventory Valued by General Dynamics (as of January 30, 2012)

Description	Number of Different Items	Total Parts	Dollar Value
<i>Wholesale</i>			
Garrison- Auburn	3,525	219,684	\$39,926,300
Deployment-Auburn	13,695	6,233,794	425,574,909
BDAR-Auburn	7,279	4,062,424	43,977,586
Reset-Auburn	8,129	2,600,444	93,607,969
Retrofit-Auburn	852	802,916	18,657,186
Subtotal (Auburn Warehouse)		13,919,262	\$621,743,950
London Warehouse	156	7,484	2,515,651
European Distribution Center	1,593	47,806	57,809,672
Total Wholesale Inventory		13,974,552	\$682,069,273
<i>Retail Inventory</i>	7,566	496,578	210,224,417
Subtotal Inventory*	16,344	14,471,130	\$892,293,690
<i>Inventory without an assigned value</i>	3,021	436,054	
Total Inventory*	19,365	14,907,184	\$892,293,690

Note: Because of rounding, the dollar value in columns may not sum.

* The total represents the number of different parts.

According to General Dynamics contracting officials, General Dynamics managed Stryker inventory in its Oracle system; however, it did not assign the inventory a value in its system or report the inventory on its financial statements because it considered the

General Dynamics managed Stryker inventory in its Oracle system; however, it did not assign the inventory a value in its system or report the inventory on its financial statements because it considered the Stryker inventory to be Government property.

Stryker inventory to be Government property. Therefore, General Dynamics did not account for the Stryker inventory according to Federal Acquisition Regulation (FAR) Government property guidance for CAP. Specifically, FAR 52.245-1, "Government Property," requires that the contractor create and maintain records of all Government

property accountable to the contract, including Government-furnished property and CAP, and requires accounting for the quantity received, issued, balance on hand, and unit acquisition cost.

Stryker Inventory Was Incorrectly Classified as CAP

While General Dynamics officials classified Stryker inventory delivered to the GOCO warehouse as Government property, PMO Stryker officials incorrectly classified the inventory as CAP. Consequently, the Stryker inventory was not reported on either the contractor's or the Army's financial statements, resulting in no visibility of the Army assets (parts and value). PMO Stryker relied on the CAP definition in FAR Part 45, "Government Property," which defines CAP as "*property acquired, fabricated, or otherwise provided by the contractor for performing a contract to which the Government has title.*" CAP business rules for cost-reimbursable contracts were generally designed to address "*property acquired, fabricated, or otherwise provided by the contractor*" that would eventually be delivered to the Government as part of a higher level end item, not as used by the Army on its logistics services contract with no end item deliverable. While Stryker inventory consumed during the contract period of performance for the logistics services contract could possibly be considered CAP, the inventory identified in this report was from prior-year periods and needed to be officially delivered and accepted by the Army and accounted for as Government property. In regards to BDAR and Reset efforts, the situation was basically the same because both efforts had specific periods of performance so inventory not consumed during periods of performance needed to be officially delivered and accepted by the Army and accounted for as Government property.

CAP business rules were established to prevent an inefficient practice of recording CAP on DoD accountability records when it was acquired by the contractor and then recording

CAP business rules were established to prevent duplicate accountability records, not to prevent proper accountability of Government property.

the end item on DoD accountability records once it was delivered, which would result in duplicate accountability records. The CAP business rules were established to prevent duplicate accountability records, not to prevent

proper accountability of Government property. By classifying the Stryker inventory as

CAP, PMO Stryker officials were able to bypass the accountability and financial reporting requirements for Government property after the Stryker inventory was delivered to the GOCO warehouse.

Stryker inventory consists of spare parts that General Dynamics procured from its vendors, which were delivered directly to the GOCO warehouse and material or parts that were used to manufacture higher level assembly parts that were then delivered to the GOCO warehouse. For example, the commander's seat assembly consisted of several brackets, a seat guard, and a seat that were assembled by General Dynamics and delivered to the GOCO warehouse.

DoD Guidance on CAP

In December 2007, the Under Secretary of Defense for Acquisition, Technology, and Logistics (USD[AT&L]) and Under Secretary of Defense (Comptroller) [USD(C)]

Upon delivery to the Government, contractor acquired property should be recorded in the appropriate property accountability system.

developed guidance to address questions and issues being raised by DoD Components regarding financial accounting and property accountability of CAP. The joint USD(AT&L) and USD(C) memorandum, "Military Equipment Valuation Contractor

Acquired Property Business Rule," December 22, 2007, states that:

. . . while title passes to DoD when the property is obtained by the contractor, the property will not be recorded on DoD financial statements (as other than construction in process) or in accountability systems until the property is delivered to DoD. . . .

The purpose of this paper is to provide the requirements for **accounting for Contractor Acquired Property (CAP) in accordance with the provisions of Statement of Federal Financial Accounting Standards (SFFAS) No. 6, *Accounting for Property, Plant, and Equipment***. . . .

Statement of Federal Financial Accounting Standards (SFFAS) No.6, *Accounting for Property, Plant, and Equipment*, requires that Property, Plant and Equipment (PP&E) shall be recognized when title passes to the acquiring entity or when the PP&E is delivered to the entity or to an agent of the entity. In the case of constructed PP&E, the PP&E shall be recorded as construction-in-progress until it is placed in service, at which time the balance shall be transferred to general PP&E. . . .

DoD policies, processes, and practices are structured on delivery, receipt, and acceptance of property. . . Although the DoD may have title to some property, e.g., property acquired, fabricated or otherwise provided by the contractor for performing a contract, **such property has not yet been delivered.** . . .

Upon delivery to the Government, contractor acquired property should be recorded in the appropriate property accountability system. [emphasis added]

Additionally, in a subsequent USD(AT&L) memorandum, “Contractor Acquired Property (CAP) Under Cost Reimbursement Contracts and Line Items,” January 11, 2010, the Director, Defense Procurement and Acquisition Policy (DPAP), issued more guidance to clarify business rules for CAP.

Historically, **some DoD Components sought to establish accountable property records for CAP – an inefficient practice that resulted in duplicate accountability records.** In a joint memorandum entitled “Military Equipment Valuation Contractor Acquired Policy Business Rule,” dated December 22, 2007, the Office of the Under Secretary of Defense (Comptroller) and Under Secretary of Defense (Acquisition, Technology & Logistics) clarified the Department’s policy (attached). The business rule states that although title passes to DoD when the property is obtained by the contractor, **the property will not be recorded on DoD financial statements (as other than construction in process) or in accountability systems until the property is delivered to DoD.**

Given the many on-going audits and Congressional interest in Government Property, it is imperative that DoD Components understand the business rules for CAP, as well as the aforementioned change in accountability and financial record keeping, and that they **ensure that accountable property records are established for CAP only upon delivery to the Government on a contract line item number (CLIN).** [emphasis added]

Appendix B provides the complete USD(AT&L) and USD(C) memoranda.

PMO Stryker Inappropriately Applied DoD Guidance on CAP

PMO Stryker inappropriately applied the USD(AT&L) memorandum on CAP business rules and, therefore, did not establish adequate controls over Government property on the Stryker CLS contract. We asked the former Deputy Project Manager for Stryker⁹ who owned the inventory at the Auburn warehouse. The former Deputy Project Manager replied in a letter to us, dated February 18, 2011, that “. . . *material that is used in the performance of CLS is treated as Contractor Acquired Property.*” The former Deputy Project Manager also stated that the Stryker inventory was considered CAP until the inventory was placed on a Stryker vehicle; the position was reiterated by the Defense Contract Management Agency (DCMA).¹⁰ Specifically, in response to our statement that a Government official was not accepting inventory at the Auburn warehouse, a Lead Program Integrator for Team Stryker, DCMA, stated in an e-mail, dated March 15, 2011, that:

There are NOT approximately 15,000 line items in the CLS contract. There are no individual piece parts in the CLS contract (perhaps less [than] a dozen). And the Government did not purchase 15,000 piece

⁹ The former Deputy Project Manager for Stryker was reassigned in August 2011.

¹⁰ The Stryker CLS contract is administered by DCMA.

parts between 2006 and 2013. . . We have not purchased parts, nor a stockpile of parts, nor a warehouse to store them in. . . **Technically, when a cost voucher is paid the material belongs to the Government, but under the CAP program (AT&L Memo dated January 11, 2010) the Government takes delivery of these parts when we take delivery of the vehicles. We have never taken delivery of the parts in the warehouse-the CLS contract does not require a DD-250. [emphasis added]**

However, the Stryker inventory stored at the GOCO warehouse does not support the production of Stryker vehicles that are later delivered to the Army and accepted by DCMA. Instead, the Stryker inventory consists of spare parts that are used to sustain fielded Stryker vehicles for which the Army had already taken delivery. Therefore, based on the interpretation of the CAP guidance by PMO Stryker and DCMA officials, the Army will never take delivery of the Stryker inventory, assign the inventory a value, record it in an appropriate Army property accountability system, and recognize the inventory on the Army's financial statements. See Appendix C for the process being used by the Stryker CLS program to account for Stryker inventory being procured on the cost-reimbursable services contract.

PMO Stryker Did Not Follow CAP Guidance and Accept Delivery or Transfer Excess Material Costs to Follow-On Contracts

Although PMO Stryker and Army Contracting Command officials classified the Stryker inventory as CAP, the officials did not require General Dynamics to account for the

When excess CAP on the losing contract is required on a follow-on contract, then the inventory cost should be reduced on the losing contract and added on the gaining contract.

[DFARS PGI 245.402-70(6)]

inventory as CAP, follow guidance and accept delivery of CAP by contract line item where the material then becomes Government property, or identify the actual cost of the CAP inventory acquired on previous contracts and transfer the inventory cost to the current Stryker CLS contract. Defense Federal Acquisition Regulation Supplement, Procedures, Guidance, and

Information (DFARS PGI) 245.4, "Title to Government Property," states that when excess CAP on the losing contract is required on a follow-on contract, then the inventory cost should be reduced on the losing contract and added on the gaining contract.

DFARS PGI 245.402-70, "Policy," states:

(1) Title vests in the Government for all property acquired or fabricated by the contractor in accordance with specific requirements for passage of title in the contract. Oversight and visibility of this Government property, therefore, is limited to reviews and audits of contractor accounting and property management systems. Ad-hoc contractor generated reports of contractor-acquired property used by government personnel for "property accountability" can result in duplicate accountability records, inefficient operations, and increased program costs, and are discouraged.

(2) Contractor-acquired property items not anticipated at time of contract award, or not otherwise specified for delivery on an existing line item, shall be delivered to the Government on a contract line item. The value of that item shall be recorded at the original purchase cost or best estimate. Unless otherwise noted by the contractor at the time of delivery to the Government, the placed-in-service date shall be the date of acquisition or completed manufacture, if fabricated.

(3) Upon delivery and acceptance by the Government of contractor-acquired property items, and when retained by the contractor for continued use under a successor contract, these items become Government-furnished property (GFP). The items shall be added to the successor contract as GFP by contract modification.

(4) Individual contractor-acquired property items should be recorded in the contractor's property management system at the contractor's original purchase cost or best estimate.

(5) Financial/accounting treatment shall be in accordance with DoD Financial Management Regulations, DoD 7000.14-R, volume 4, chapter 6.

(6) To the extent that contractor-acquired material that is excess to the needs of the accountable contract is required on follow-on or other contracts, the costs of such property shall be credited to the losing contract; the gaining contract shall be debited accordingly. This supports the FAR 31.205-26 policy that material costs should be borne by the contract that consumes material when materials are required for specific contracts. This also complies with the requirements of DFARS clause 252.242-7004, Material Management Accounting Systems, requiring a material management and accounting system. This process applies only to contractor-acquired material. It does not apply to other contractor-acquired property, i.e., equipment, special tooling or special test equipment, or GFP.

(7) Contractor "credit-debit" systems and material management accounting systems do not involve or require contractual modifications for the transfer of material by credit as they are internal contractor accounting transactions. However, such systems should be reviewed for efficacy and efficiency by the DoD component responsible for contract administration. **[emphasis added]**

PMO Stryker personnel never accepted delivery or planned to accept delivery of the CAP inventory on a contract line item nor did they transfer the costs of the inventory to the gaining contracts and credited or reduced costs on the losing contracts (although transferring costs from contract to contract at this point is probably not feasible due to the substantial cost of the Stryker inventory accumulated over many contract years). After extensive discussions with PMO Stryker officials, we were unable to reach agreement that the Stryker inventory was not CAP and should be treated as Government property managed and recorded in appropriate Army accountability and financial accounting systems.

Clarification Needed on the CAP Business Rules for Logistics Services Contracts

CAP can be material not intended to be incorporated into a higher level end item. It can also be material used in the performance of services. However, the CAP business rules for cost-reimbursable contracts were generally designed to address “*property acquired, fabricated, or otherwise provided by the contractor*” that would eventually be delivered to the Government as part of a higher level end item, not for logistics services contracts that provide only the service as a deliverable.

In July and August 2012, we met with senior officials responsible for Government property and CAP policy from the Assistant Secretary of Defense for Logistics and Material Readiness and the DPAP and Acquisition Resources, and Analysis directorates within USD(AT&L). Representatives from the ASA(FM&C), PMO Stryker, Army Contracting Command-Warren, and U.S. Army TACOM Life Cycle Management Command Legal office were also present to discuss the proper classification of the Stryker inventory.

The DoD CAP and Government property policy experts stated that inventory procured on the cost-reimbursable logistics services contract and consumed during the contract period of performance may be considered CAP. However, inventory not consumed during the period of performance and transferred to a new contract represented a delivery and acceptance action, thereby changing the status from CAP to Government property.

Additionally, there could be instances where the CAP inventory does not become Government property if the contractor bought back the CAP or the Army transferred the costs of the CAP to a gaining contract with a credit to the losing contract. However, these instances were not likely to occur on a logistics services contract because of the large amount of CAP inventory that could be involved in performing the contract.

The Director, DPAP, working with the Assistant Secretary of Defense for Logistics and Materiel Readiness, needs to issue additional guidance that further clarifies the proper use of CAP business rules specifically for logistics services contracts with no end item deliverables and how to properly account for and value the inventory on these contracts that is not consumed during the contract period of performance.

The Program Executive Officer, Ground Combat Systems, needs to require the Project Manager, Stryker, to accept delivery of all CAP inventory that was not consumed during the contract period of performance on a contract line item in accordance with DFARS PGI 245.402-70. Consequently, the Stryker inventory identified in this report will need to be delivered and accepted as Government property before award of the follow-on Stryker CLS contract scheduled in FY 2013.

The Program Executive Officer, Ground Combat Systems, needs to require the Project Manager, Stryker, to require General Dynamics to accept responsibility and create and maintain appropriate accountability records in accordance with FAR 52.245-1 for any inventory considered CAP. If General Dynamics is unwilling to accept responsibility for

inventory delivered to the GOCO warehouse as CAP, then PMO Stryker must accept delivery of the inventory as Government property.

PMO Stryker Officials Did Not Comply With Multiple DoD and Army Property Regulations

PMO Stryker officials inappropriately categorized all Stryker inventory as CAP and did not recognize the inventory at the GOCO warehouse as Government property, which could include CAP, that was managed in the contractor's inventory management system. As a result, PMO Stryker officials did not comply with multiple DoD and Army property regulations designed to provide good stewardship and fiduciary responsibility over Government property and support the Army goal of creating auditable financial statements. PMO Stryker officials also did not correctly use the Army's Logistics Modernization Program (LMP) system designed to integrate logistics and financial operations. The guidance provides detailed procedures on how inventory should be valued, accounted for, and reported in DoD and Army financial accounting systems.

DoD Financial Management Regulation (DoD FMR) 7000.14-R, Volume 4, "Accounting Policy and Procedures," Chapter 4, "Inventory and Related Property," prescribes the accounting policy and related requirements necessary to establish financial control over DoD inventory and operating materials and supplies held for use or sale.

DoD Regulation 4140.1-R (DoD 4140.1-R), "DoD Supply Chain Materiel Management Regulation," May 23, 2003, provides detailed material management guidance that promulgates best business practices and meets all material management statutory requirements.

Army Regulation 735-5, "Policies and Procedures for Property Accountability," February, 28, 2005, identifies how Army property should be accounted for and who is responsible for ensuring the property is properly used and cared for. It also requires detailed accounting records and financial accounting records of Army property. Chapter 2, "Property Accounting Requirements," section I, "Basic Principles," 2-2.c, "Accounting for Army property," states that:

All property or material, except real and contractor-acquired property, acquired in any manner will be properly accounted for on item detail accounting records and financial (dollar) item accounting records. Responsibility will be fixed as prescribed by this regulation or other Army policy. The local commander may direct more stringent controls for expendable material.

Army Regulation 735-5, Chapter 10, "Loans, Bonding, and Other Accounting Procedures," Section II, "Other Accounting Procedures," 10-5, "Financial Inventory Accounting," states that:

A financial inventory accounting system will be established and maintained for inventories of Army material held on records of accountability within the Army supply system. It will be the formal

accounting system used to integrate the required quantitative and monetary accounting of Army property.

Stryker Inventory Needed to Be Properly Valued

PMO Stryker did not capitalize and properly value the Army-owned inventory being managed by General Dynamics. By not properly valuing the Stryker inventory, PMO Stryker did not comply with the DoD FMR 7000.14-R, volume 4, chapter 4, which requires that inventory be valued at historical cost using a moving average cost. USD(AT&L) and USD(C) issued a memorandum, “Baseline Valuation and Certification for Department of Defense (DoD) Inventory and Operating Materials and Supplies,” November 8, 2005, that outlines a 13-step approach for valuing inventory, including establishing the baseline value for on-hand inventory if historical acquisition data were not available. (See Appendix D for the complete memorandum.)

The Program Executive Officer, Ground Combat Systems, needs to require the Project Manager, Stryker, to follow DoD guidance and develop procedures to properly value the Stryker inventory.

Stryker Inventory Was Not Recorded in an Army Property Accountability System

PMO Stryker did not properly record Army-owned inventory in an Army property accountability system. As a result, PMO Stryker did not maintain detailed transaction histories related to the inventory, categorize the inventory into proper logistics categories, validate inventory levels, and take appropriate action to dispose of excess or obsolete inventory in a timely manner. Both DoD 4140.1-R and Army Regulation 735-5 state that Government property should be accounted for on property accounting records until it is either consumed or disposed of.

Government property should be accounted for on property accounting records until it is either consumed or disposed of.

Specifically, DoD 4140.1-R states that property should be classified into four categories to establish mechanisms for the proper retention, distribution, and disposal of the property. Those four categories are:

- Approved Acquisition Objective—the quantity of an item authorized for peacetime and wartime requirements.
- Economic Retention Stock—stock above the approved acquisition objective that is more economical to retain than to dispose of.
- Contingency Retention Stock—stock above the approved acquisition objective and economic retention stock that is held to support specific contingencies.

- Potential Reutilization Stock—stock above the approved acquisition objective, economic retention stock, and contingency retention stock that should be reviewed for transfer to the Defense Reutilization and Marketing Group as soon as practicable.

Additionally, DoD 4140.1-R and Army Regulation 735-5 state that a detailed transaction history is to be maintained, providing a complete audit trail of all transactions affecting the total item property records for a minimum of 2 years. At a minimum, the accounting records should include quantity on hand at wholesale storage activities, quantity on hand at retail activities, condition, dollar value, quantity due-in, quantity in-transit to another location, quantity in a repair facility, and whether the item is in the contractor's custody. Also, Army Regulation 735-5 states that accounting records should include any gains or losses for an item.

The Program Executive Officer, Ground Combat Systems, needs to require the Project Manager, Stryker, to perform a thorough review of the Stryker inventory, record the inventory in an Army property accountability system, and properly stratify the inventory as approved acquisition objective, economic retention stock, contingency retention stock, or potential reutilization stock.

The Program Executive Officer, Ground Combat Systems, needs to require the Project Manager, Stryker, to establish a detailed transaction history for the Stryker inventory that records anticipated receipts of inventory as material due-ins, material received, or material transferred out.

Stryker Inventory Needed to Be Recognized in Army Financial Accounting Systems

PMO Stryker did not recognize Stryker inventory on the Army financial statements to support the Army goal of creating auditable financial statements. Specifically, Stryker inventory, valued at \$892.3 million, was not recognized and properly valued in appropriate inventory general ledger accounts or in any Army financial accounting systems. DoD FMR 7000.14-R, volume 4, chapter 4, describes the different U.S. Government Standard General Ledger (USSGL) accounts that should be used to account for the types of inventory. Additionally, DoD FMR 7000.14-R, volume 4, chapter 4, states that inventory included in the financial records should also be identified in logistics records.

Table 2 illustrates the relationship between the logistics inventory categories and the USSGL accounts.

**Table 2. Logistics Inventory Categories
Compared to USSGL Accounts**

Category	Inventory Accounts
Approved Acquisition Objective	USSGL 1521
Economic Retention Stock	USSGL 1522
Contingency Retention Stock	USSGL 1522
Potential Reutilization Stock (Excess)	USSGL 1524

DoD FMR 7000.14-R, volume 4, chapter 4, defines the USSGL accounts displayed in Table 2 as:

- USSGL Account 1521 - inventory purchased for resale that is in usable condition and available for immediate resale.
- USSGL Account 1522 – inventory held in reserve for future sale.
- USSGL Account 1524 - inventory that exceeds the amount expected to be used for normal operations and does not meet the criteria to be held in reserve for future use.

Congress established an FY 2017 goal for DoD to have auditable financial statements in Public Law 111-84, Section 1003, “Audit Readiness of Financial Statements of the Department of Defense.” USD(C) assigned a high priority for the Departments to focus on improving audit readiness on information essential to effectively manage DoD mission-critical assets, which include operating inventory, so that DoD would achieve the goal of auditable financial statements by FY 2017. The Army started to implement several controls to guarantee compliance from all Army personnel whose work directly impacts the financial statements. ASA(FM&C) stated in “FY 2011 Army Audit Readiness Strategy” (undated) that:

One important audit readiness concept the Army must understand is that the auditors will be looking for evidence or proof of how the Army conducts business to include obligations recorded are supported by sufficient documentation assets recorded in the Army’s property systems depict a complete and accurate picture of the Army’s physical inventory.

For the Army to achieve its financial improvement goals, every person in the Army managing or executing resources must accept responsibility for sustaining an auditable business environment. [emphasis added]

Additionally, the Secretary for the Army stated in a memorandum, "Army Audit Readiness Efforts," February 18, 2011, that:

Army leaders shall be held accountable in their performance plans for transacting the Army's business in an audit compliant manner. Specifically, financial, logistics, facilities, human resources, contracting, and other personnel will be held accountable for ensuring management controls and business processes comply with financial audit standards. [emphasis added]

PMO Stryker should recognize, value, and classify the Stryker inventory in the appropriate USSGL accounts to make certain the inventory is reported in the Army and DoD financial statements and to support the Army's goal to have auditable financial statements to comply with Public Law 111-84, section 1003.

The Program Executive Officer, Ground Combat Systems, needs to develop performance standards for appropriate PMO Stryker personnel that address proper accountability and financial controls over all Government property.

The Program Executive Officer, Ground Combat Systems, needs to require the Project Manager, Stryker, to report the Stryker inventory on Army financial statements in the appropriate general ledger accounts.

Logistics Modernization Program Was Not Used

In February 1998, the Army began to replace its existing material management systems with the LMP system, at a cost of over \$1 billion. As of April 2011, LMP was fully implemented in the Army Materiel Command community and fielded to approximately 25,000 users at more than 50 Army and DoD locations and interfaced with more than 70 different DoD systems. LMP manages approximately \$22 billion in inventory with tens of thousands of contractors. The system is among the world's largest fully integrated supply chain demand planning and execution solutions. Additionally, LMP integrates financial and logistics operations into one system.

As of August 2012, the Army did not have visibility over the \$892.3 million of Stryker inventory (parts and value). Starting in October 2011, a portion of the Stryker inventory was being tracked by quantity within LMP; however, it was not valued in the system. Additionally, in October 2011, the Army started charging the Stryker brigades for parts issued from inventory that were previously purchased with Stryker brigade Operation and Maintenance or Procurement funds. Even though the inventory was loaded in LMP at no value, the Stryker brigades were charged a price that was determined by PMO Stryker, using pricing data from the contract data requirement lists provided by General Dynamics. In October 2011, PMO Stryker began using Army Working Capital Funding to purchase inventory to backfill the inventory that had been ordered from LMP. The inventory bought with Army Working Capital Funding was also recorded in LMP at no value.

Although a portion of the Stryker inventory was recorded in LMP, it was still not properly valued, and therefore, PMO Stryker was not in compliance with DoD FMR 7000.14-R, volume 4, chapter 4, which requires that inventory be valued at historical cost using a moving average cost. The USD(AT&L) and USD(C) memorandum, “Baseline Valuation and Certification for Department of Defense (DoD) Inventory and Operating Materials and Supplies,” November 8, 2005, provides best practices for valuing inventory that PMO Stryker could use to value the Stryker inventory. A multifunctional support team is needed with the necessary knowledge, technical expertise, and credibility to support PMO Stryker to properly value and input Stryker inventory into LMP so the Stryker brigades are correctly charged.

The Program Executive Officer, Ground Combat Systems, needs to require the Project Manager, Stryker, to accept delivery of Stryker inventory as Government property and value the inventory in LMP before parts are requisitioned and charged to the Stryker brigades.

ASA(ALT), with support from ASA(FM&C), needs to establish a multifunctional support team with necessary knowledge, technical expertise, and creditability to properly account for the Government property procured on the cost-reimbursable services contract for Stryker vehicles. This team should work with PMO Stryker personnel to ensure that Stryker inventory has been assigned a value and recorded in appropriate Army property accountability and financial accounting systems.

PMO Stryker Officials Should Implement a Comprehensive Plan for Improving Inventory Management

Public Law 111-84, section 328, requires DoD to develop a plan to provide for total asset visibility. Specifically, the Secretary of Defense is to develop a comprehensive plan for improving the inventory management systems of the military, with the goal of reducing acquisition and storage of excess secondary inventory. The plan should focus on:

- reviewing demand-forecasting procedures and developing metrics to identify a bias toward overforecasting;
- accelerating the efforts to achieve total asset visibility;
- reducing the average level of on-order secondary inventory that exceeds requirements;
- reviewing and validating methods to establish economic and contingency retention requirements; and
- reviewing on-hand inventory items that have no demand, developing metrics to track years of no demand, and developing procedures for ensuring the potential reutilization or disposal of the no-demand inventory.

In October 2010, the Assistant Secretary of Defense for Logistics and Materiel Readiness issued the “Department of Defense Comprehensive Inventory Management Improvement Plan,” requiring Military Departments to implement the plan’s policies, procedures, and metrics for inventory management that address the requirements in Public Law 111-84, section 328. PMO Stryker officials should comply with DoD and Army property accountability regulations so that they can start tracking the inventory and compiling the necessary data to comply with the DoD comprehensive plan for inventory management that addresses overforecasting, total asset visibility, excess inventory, economic retention requirements, and aggressive potential reutilization and disposal reviews to meet the intent of Public Law 111-84, section 328.

The Program Executive Officer, Ground Combat Systems, needs to require the Project Manager, Stryker, to implement a comprehensive inventory management improvement plan that complies with the DoD inventory management plan and addresses overforecasting, total asset visibility, excess inventory, economic retention requirements, and aggressive potential reutilization and disposal reviews to meet the intent of Public Law 111-84, section 328.

Obsolete and Excess Stryker Inventory for High-Dollar Review Parts

Our review of 21 high-dollar parts, valued at \$85.1 million, showed that 16 parts had excess Stryker inventory of \$72.7 million that could be either disposed of (\$58.0 million) or potentially used on other contracts (\$14.7 million). For example, we found 170 empty engine containers (part 10650112), valued at \$1.1 million, that General Dynamics determined could be used to store a different engine, thereby reducing future costs. General Dynamics also initiated action to dispose of different obsolete parts we identified during the audit.

During our audit, we classified the 21 parts in our sample in the appropriate accounts as described in DoD FMR 7000.14-R, volume 4, chapter 4. According to DoD 4140.1-R, the approved acquisition objective is the quantity of parts needed to meet peacetime and wartime requirements. Additionally, DoD 4140.1-R states that active inventory consists of “Materiel that is expected to be consumed within the budget year (2 years) and materiel that has been purchased to meet specific war reserve requirements.”

Therefore, we calculated a 2-year demand using data provided by General Dynamics to establish the quantity for the “Inventory Held for Resale” (Account 1521). For the “Inventory Held in Reserve for Future Sale” (Account 1522), we also used a 2-year demand to determine the quantity for that account. For the “Excess, Obsolete, and Unserviceable Inventory” (Account 1524), we calculated the quantity remaining after subtracting the quantity placed in accounts 1521 and 1522 from the quantity on hand that was available for issuance. Table 3 shows a summary of our classifications of the 21 review parts in the appropriate DoD accounts (DoD FMR 7000.14-R, volume 4, chapter 4). For details on specific parts, see Appendix E.

Table 3. OIG Review of Stryker CLS Inventory for the 21 Sample Parts
(millions)

Category	Parts	Requirements (Account 1521)	Contingency/ Economic Retention (Account 1522)	Excess/Obsolete (Account 1524)	Total
Obsolescence	5	0.0	0.0	\$58.0	\$58.0
Potential Use Outside CLS	5	\$0.9	\$0.9	9.0	10.8
Excess Inventory	6	0.2	0.2	5.6	6.0
Acceptable	5	8.8	1.6	0.0	10.4
Total	21	\$9.8	\$2.6	\$72.7	\$85.1

Note: Because of rounding, columns may not sum. Values on hand as of January 30, 2012.

Action Needed to Be Taken to Dispose of Obsolete Inventory

During the audit, we identified five parts, valued at \$58.0 million, that were considered obsolete because of the changing configurations on the Stryker vehicles. However, PMO Stryker personnel did not take timely action to dispose of the obsolete inventory. According to DoD 4140.1-R, section C2.8.1.1.4,

Personnel involved in wholesale materiel management functions should seek to eliminate wasteful retention practices and achieve cost savings in the retaining stock where possible. In particular, the DoD Components should ensure that item managers and distribution system managers process disposals in a timely manner. Generally, **potential reutilization stock shall not be held by an IMM [integrated materiel manager] longer than 12 months after stratification**, or by the distribution system longer than 6 months after a disposal release order is received from the IMM. **[emphasis added]**

The following section provides information on the obsolete parts.

Review Part 1 – Thermal Imaging Module

The thermal imaging module became obsolete on September 29, 2005 (engineering change order BCT00039 R1), for new production vehicles and parts that failed on fielded Stryker vehicles. Then on June 18, 2007, according to engineering change order GDV6293, all Stryker vehicles were to be retrofitted with the newer thermal imaging module (part 68112518-01) making all inventory of the old part (part 1310010-501) obsolete. As of January 30, 2012, PMO Stryker had 768 units of the obsolete thermal imaging module in inventory, valued at about \$57.0 million, or \$74,086.00 each. The large amount of inventory for the obsolete thermal imaging module was a result of removing the part from the Stryker vehicles and replacing it with the newer thermal imaging module. On April 5, 2012, General Dynamics received approval from PMO Stryker to dispose of 765 units, which accounted for \$56.7 million of the total obsolescence value of \$58.0 million identified in Table 3.

Review Parts 2, 3, and 4 – Commander’s Seat Assembly

On April 15, 2009, these three variations of the commander’s seat assembly became obsolete and were replaced with new, ceiling-mounted, energy-attenuating seats. The new seats provided additional protection against roadside improvised explosive devices by limiting the energy transferred by the explosives. Between February 2011 and August 2011, General Dynamics requested and received confirmation to dispose of the three obsolete commander’s seat assemblies, for a total of 1,210 units, valued at \$9.9 million.¹¹ Although the Army approved disposal of a majority of the units for these three parts, as of January 30, 2012, the cumulative total of the three obsolete commander’s seat assemblies remaining in inventory was 135 units, valued at \$1.1 million.

Review Part 5 – Ramp Manifold

The ramp manifold was a component of the actuation system that was used to open and close the rear ramp on the Stryker vehicle. In October 2004, the ramp manifold (part 10626152) became obsolete in production vehicles and was replaced by part 10660046-001. By April 2007, the old ramp manifold became obsolete for both production and fielded vehicles. As of January 30, 2012, General Dynamics reported that seven units, valued at \$9,608, or \$1,372.61 each, remained in inventory. However, we found that another 659 units, valued at \$904,549, were still being stored and managed at the GOCO warehouse and awaiting disposition approval from PMO Stryker officials. These 659 units along with several other obsolete and excess parts were not reported to us because General Dynamics coded them as nonissuable inventory. General Dynamics indicated that they reported nonissuable and issuable inventory daily to PMO Stryker personnel.

The Program Executive Officer, Ground Combat Systems, needs to require, the Project Manager, Stryker, to perform a thorough review of the Stryker spare parts inventory and take appropriate action to dispose of obsolete parts.

Excess Stryker Inventory Could Be Used in Production or on a Higher Level Assembly

During the audit, we identified excess Stryker spare part inventory relating to five parts, valued at \$10.8 million, that could be used for production of Stryker vehicles or on a higher level assembly part. One of the issues preventing General Dynamics from using excess Stryker spare part inventory to meet production requirements was a 23.4-percent buyback charge that PMO Stryker would charge General Dynamics to buy back the part and use it on another Stryker contract. According to PMO Stryker officials, the 23.4-percent buyback charge was equivalent to the FY 2007 cost recovery rate that TACOM developed and adjusts each fiscal year. PMO Stryker officials decided to use the TACOM surcharge rate to recover the fee and procurement rates that General

¹¹ The value of the review parts was based on the pricing data that General Dynamics provided us instead of the pricing data listed in the DCMA’s Plant Clearance Automated Reutilization Screening System.

Dynamics already charged when it sold PMO Stryker the part. However, the buyback charge provides a disincentive for General Dynamics to use the excess Stryker spare part inventory for other applications. The following section provides detailed information on the parts that had potential use outside the CLS contract.

Review Part 6 – Netting Material

The netting material was used to hold equipment on Stryker vehicles and was issued with all new production vehicles. As of January 30, 2012, PMO Stryker had 7,568 units, valued at \$892,896, or \$117.98 each. General Dynamics' records showed no spares demand for the netting; however, its purchase order history for this part indicated that it continued to buy the netting for use on new production vehicles. General Dynamics was unable to transfer the spare netting (see Figure 4) to the production contract without obtaining prior approval from PMO Stryker officials and paying the 23.4-percent buyback charge on the material cost.

Figure 4. Excess Netting Material



Source: Photograph provided by PMO Stryker.

Review Part 7 – Collapsing Sign Stand

The collapsing sign stand was used to mark contaminated areas during field missions and training exercises and was issued with new production vehicles. As of January 30, 2012, PMO Stryker had 2,938 units on hand, valued at \$81,242, or \$27.65 each.¹² General Dynamics' records show no spares demand for the collapsing sign stand, but its purchase order history indicated it still buys the collapsing sign stand for other Stryker efforts.

¹² General Dynamics was unable to determine an exact price for this part, so we calculated the price using its purchase order history and applying a 17.92-percent burden rate because the part was purchased by General Dynamics-U.S.

Review Part 8 – Drive Assembly Elevation

The drive assembly elevation was used to elevate and depress a target acquisition housing assembly on the Stryker vehicle and was procured to meet spares and new production requirements (see Figure 5). As of January 30, 2012, PMO Stryker had 97 units on hand, valued at \$2.1 million, or \$21,287.69 each. General Dynamics' records showed that for the next 2 years, it anticipated a demand of five spares; therefore, PMO Stryker had about 32.3 years' worth of inventory for this part. General Dynamics was unable to transfer the spare drive assembly elevation to the production contract without obtaining prior approval from PMO Stryker officials and paying the 23.4-percent buyback charge on the material cost.

Figure 5. Drive Assembly Elevation



Source: Photograph provided by PMO Stryker.

Review Part 9 – Power Electronics Assembly

The power electronics assembly was a motor controller that powered the drive system (see Figure 6). As of January 30, 2012, PMO Stryker had 56 units, valued at \$7.2 million, or \$127,734.15 each. General Dynamics was required to maintain four units in inventory for flyaway deployment packages, which left 52 units available for use as spares for the Stryker vehicles. General Dynamics' records showed a 2-year demand of five units for this part; therefore, PMO Stryker had 17.3 years' worth of inventory for the power electronics assembly. General Dynamics was unable to transfer the spare power electronics assembly to the production contract without obtaining prior approval from PMO Stryker officials and paying the 23.4-percent buyback charge on the material cost.

Figure 6. Power Electronics Assembly



Source: Illustration provided by General Dynamics.

Review Part 10 – Engine Container

The engine container (part 10650112; see Figure 1) was originally procured to store a specific Stryker engine; however, in December 2006, the supplier notified General Dynamics that it would no longer be producing that engine. Therefore, PMO Stryker officials allowed General Dynamics to do a “last-chance” buy to procure additional engines and containers. Over the past several years, General Dynamics procured newer engines with new engine containers; therefore, there was no longer a requirement for the older engine containers in inventory.

During the audit, we identified the excess containers, and in July 2011, General Dynamics took action to change the buy requirements for the new engines to purchase only the engine and then store it in the old containers until the existing inventory was depleted. Over the next 2 years, the demand for the engine containers increased from 0 to 20 engine containers. We commend General Dynamics for finding a use for the 170 engine containers on hand, valued at \$1.1 million, or \$6,470.24 each. See Appendix F for details on potential monetary benefits.

Excess Inventory Needed to Be Addressed

During the audit, we identified excess Stryker spare part inventory relating to six parts, valued at \$6.0 million, that had a reduced demand or excessive procurement quantities. The following section provides detailed information on the parts whose demand requirements significantly decreased or for which General Dynamics made excessive procurements.

Review Parts Related to the Wheel Drive and Suspension System

Review parts 11-16 were all components of the wheel drive and suspension system that experienced a high level of field failures between 2007 and mid-2009 (see Table 4).

However, starting in 2010, General Dynamics' consumption for these parts decreased because of changes in mission execution and the installation of a heavyweight driveshaft, which led to a decrease in failures. Table 4 shows a significant reduction in parts consumption in 2011 from earlier years.

Table 4. Consumption History for Parts With Reduced Demand or Excess Procurement Quantities, by Fiscal Year

Review Part	Number	Total Consumption					
		2006	2007	2008	2009	2010	2011
11-Planet Pinion	10650815	828	1,204	2,117	1,940	1,054	72
12-Left Hand Brake Assembly	10663271-001	324	216	718	986	539	0
13-Right Hand Brake Assembly	10663270-001	213	356	680	1,178	487	0
14-Ring Gear Carrier	10650813	539	1,156	1,162	2,499	1,323	17
15-Wheel Hub	10650817	179	1,036	1,603	1,136	601	16
16-Wheel Bearing Flange	10664080-001	77	2,571	1,857	1,508	782	24

Table 5 shows that PMO Stryker had between 32 and 1,147 years of inventory for review parts 11-16.

Table 5. Quantity On Hand and Demand for Review Parts 11-16

Review Part	Quantity On Hand ¹	Unit Price	Total Price (in millions)	2-Year Demand ²	Years of Inventory
11-Planet Pinion	9,179	\$62.32	\$0.6	15	1,147
12-Left Hand Brake Assembly	1,845	705.99	1.3	3	923
13-Right Hand Brake Assembly	1,783	705.99	1.3	11	297
14-Ring Gear Carrier	2,581	390.18	1.0	98	53
15-Wheel Hub	1,741	283.66	0.5	91	38
16-Wheel Bearing Flange	1,831	719.12	1.3	113	32

¹Quantity on hand as of January 30, 2012.

²General Dynamics 2-year forecasted demand as of September 1, 2011.

Further, General Dynamics purchased 7,197 units of review part 11, the planet pinion, in May 2009, when actual consumption for the previous year (2008) was only 2,117 units. As of September 2011, forecasted 2-year demand for the planet pinion was only 15 units. This bias toward overforecasting resulted in the Army's owning 9,179 planet pinions, valued at over \$572,000, when 2-year demand for the part was only 15 units.

This bias toward overforecasting resulted in the Army owning 9,179 planet pinions, valued at over \$572,000, when 2-year demand for the part was only 15 units.

The Program Executive Officer, Ground Combat Systems, needs to require the Project Manager, Stryker, to perform a thorough review of excess Stryker inventory and

determine whether the parts can be used to meet other related Stryker requirements and ensure any material buy-back provisions do not provide a disincentive for the contractor to fully use the excess inventory.

Management Comments on the Finding and Our Response

The Deputy Program Executive Officer, Ground Combat Systems (Deputy PEO), disagreed with aspects of the finding, but agreed with the recommendations.

Department of the Army Comments

The Deputy PEO stated that the finding and conclusion that PMO Stryker inappropriately treated and classified Stryker inventory as CAP was factually incorrect. He stated that during earlier periods of performance in the contract, PMO Stryker required the contractor to account for CAP in accordance with FAR 45 and FAR 52.245-1 guidance on Government property. The Deputy PEO also stated that the Stryker CLS contract included contract data requirements list (CDRL) reports, which provided PMO Stryker with the necessary oversight of the Government property in the possession of the contractor. As part of the CDRL reports, General Dynamics provided details about the parts purchased and repaired, including costs, consumption, and on-hand inventory.

Additionally, the Deputy PEO stated that the requirement for delivery and Government acceptance of excess CAP at the end of a contract was not incorporated in DFARS PGI 245.4 until January 2011, which was during the fourth year of the Stryker CLS contract. He stated that the Stryker inventory was never delivered to the Army because the material was not an end product deliverable under a CLIN on the Stryker CLS contract; therefore, PMO Stryker was not required to account for the inventory per the USD(AT&L) memorandum, "Contractor Acquired Property (CAP) Under Cost Reimbursement Contracts and Line Items," January 11, 2010.

Our Response

We acknowledge that PMO Stryker and Army Contracting Command-Warren included FAR clause 52.245-1 in the contract; however, PMO Stryker and Army Contracting Command-Warren did not provide sufficient oversight to confirm that General Dynamics was complying with the FAR requirements. FAR clause 52.245-1 requires the contractor to maintain accountable records for CAP, including quantity and unit acquisition cost. However, we identified that General Dynamics had at least 3,021 Army-owned Stryker parts recorded in its Oracle system with no assigned value. We also identified that the CDRL reports contained inaccurate data, including the costs associated with some of the parts.

This report primarily focused on the Stryker inventory that had accumulated from the expired base year and four option years,¹³ not inventory that was acquired during an active contract period of performance. We agree that stronger guidance was needed to clarify when delivery and Government acceptance of inventory should occur for inventory that was acquired but not consumed by the end of the contract period of performance. Further, the clarifying guidance should specify how to record the delivered inventory in DoD property accountability and financial accounting systems. Therefore, we recommended that the Director, DPAP, working with the Assistant Secretary of Defense for Logistics and Materiel Readiness issue the necessary guidance (Recommendation 1). The Director, DPAP, stated that the guidance would be issued during the second quarter of FY 2013.

The facts of the findings were still accurate in that at least \$892.3 million of Army-owned Stryker inventory was not assigned a value and recorded in the Army's property accountability and financial accounting records. PMO Stryker inappropriately classified and treated the entire Stryker inventory as CAP based on the FAR definition. FAR Subpart 45.1 defines CAP as property acquired, fabricated, or otherwise provided by the contractor *for performing a contract*, and to which the Government has title. However, General Dynamics did not acquire nor use a majority of the Stryker inventory to perform CLS services during the fifth contract year (option year 4). In fact, the Stryker inventory, as of January 2012, was accumulated over at least five contract years (the expired base year and four option years). For example, the average annual value of the CLS contract was about \$290.6 million,¹⁴ yet the accumulated Stryker inventory procured for garrison and deployment CLS was valued at about \$676.2 million.

While General Dynamics may have acquired Stryker inventory as CAP to perform logistics support services during previous contract periods of performance, a majority of the Stryker inventory was not used during the performance of previous contracts based on the accumulation of inventory. Therefore, any Stryker inventory that was classified as CAP during an active contract period of performance should no longer be classified as CAP once the contract period of performance has expired. At the end of the contract period of performance, the Stryker inventory not otherwise specified for delivery during the performance of the contract, should be delivered to and accepted by the Army in accordance with DFARS PGI 245.402-70. Further, the joint USD(AT&L) and USD(C) memorandum, "Military Equipment Valuation Contractor Acquired Property Business Rule," December 22, 2007, requires that upon delivery to the Government, CAP must be recorded in the appropriate Government property accountability systems.

¹³ The Stryker CLS contract included a base year and five option years with successive annual periods of performance from March through February. The fourth option year ended in February 2012. Each option year represented a new separate and distinct contract in accordance with DoD FMR 7000.14-R, Volume 3, Chapter 8, "Standards for Recording and Reviewing Commitments and Obligations."

¹⁴ The annual average contract value was calculated by dividing the CLS contract value of \$1.5 billion (material and labor cost) over 5 years. The CLS contract value of \$1.5 billion only included CLS contract line items of more than \$40 million.

Recommendations, Management Comments, and Our Response

Revised Recommendation

As a result of management comments, we revised draft Recommendation 4 to clarify that the Assistant Secretary of the Army for Acquisition, Logistics, and Technology was the single office responsible for implementing the corrective action and should have support from the Assistant Secretary of the Army (Financial Management and Comptroller).

1. We recommend that the Director, Defense Procurement and Acquisition Policy, working with the Assistant Secretary of Defense for Logistics and Materiel Readiness, issue additional policy that clarifies the Under Secretary of Defense for Acquisition, Technology, and Logistics memorandum, “Contractor Acquired Property (CAP) Under Cost Reimbursement Contracts and Line Items,” January 11, 2010, specifically for logistics services contracts with no end-item deliverables and how to properly account for and value the inventory on these contracts that is not consumed during the period of performance.

Defense Procurement and Acquisition Policy Comments

The Director, DPAP, agreed with the recommendation and stated that additional guidance would be issued during the second quarter of FY 2013.

Our Response

The Director, DPAP, comments were responsive and met the intent of the recommendation. No further comments were required.

2. We recommend that the Program Executive Officer, Ground Combat Systems, require the Project Manager for the Stryker Brigade Combat Team, to:

a. Accept delivery of all contractor-acquired property that was not consumed during the contract period of performance on a contract line item in accordance with Defense Federal Acquisition Regulation Supplement, Procedures, Guidance, and Information 245.402-70. Additionally, all Stryker inventory identified in this report needs to be officially delivered and accepted as Government property before the award of the follow-on Stryker contractor logistics support contract scheduled in FY 2013.

Department of the Army Comments

The Deputy PEO partially agreed with the recommendation and stated that Stryker inventory in excess of the CLS contract requirements would be accepted in accordance with DFARS PGI 245.402-70. However, he stated that because of the volume of material procured in support of other contracts, the acceptance of these materials would not be completed before the award of the next CLS contract planned for December 2012. The

Deputy PEO stated that the Army would complete the acceptance of all Stryker material by September 30, 2013.

b. Require General Dynamics to accept responsibility and create and maintain appropriate accountability records in accordance with Federal Acquisition Regulation 52.245-1 for any inventory considered contractor-acquired property or Project Management Office, Stryker Brigade Combat Team needs to accept delivery of the inventory at the Government-owned, contractor-operated warehouse as Government property.

Department of the Army Comments

The Deputy PEO agreed with the recommendation and stated that General Dynamics would continue to maintain appropriate property accountability records in accordance with FAR 52.245-1, which began with the first Stryker CLS contract awarded in May 2002. Additionally, he stated that a procurement contracting officer letter would be issued in November 2012 that would remind General Dynamics of its obligation to comply with FAR 52.245-1. Further, he stated that PMO Stryker would perform oversight in accordance with the contract surveillance plan to verify the contractor's compliance with FAR 52.245-1.

c. Develop procedures to properly value the Stryker inventory, as required by DoD Financial Management Regulation 7000.14-R, volume 4, chapter 4, or follow the best practices outlined in the Under Secretary of Defense for Acquisition, Technology, and Logistics and Under Secretary of Defense (Comptroller) memorandum, "Baseline Valuation and Certification for Department of Defense (DoD) Inventory and Operating Materials and Supplies," November 8, 2005.

Department of the Army Comments

The Deputy PEO agreed with the recommendation and stated that the contractor would value CAP at the original purchase cost or best estimate in accordance with DFARS PGI 245.402-70. Additionally, he stated that Stryker inventory that was acquired by the Government and furnished to the contractor to perform the CLS contract, would be valued at historical moving average cost in accordance with DoD FMR 7000-14-R, volume 4, chapter 4. Further, the Deputy PEO stated that the effort to value the Stryker inventory started on October 1, 2011, and was scheduled to be completed by March 1, 2014.

d. Perform a thorough review of the Stryker inventory, record the inventory in an Army property accountability system, and properly stratify the inventory as approved acquisition objective, economic retention stock, contingency retention stock, or potential reutilization stock, as required by DoD Regulation 4140.1-R and Army Regulation 735-5.

Department of the Army Comments

The Deputy PEO agreed with the recommendation and stated that as of October 1, 2012, Government-accepted Stryker inventory was being recorded, valued, and properly stratified in the LMP system.

e. Establish a detailed transaction history for Stryker inventory that records anticipated receipts of inventory as material due-ins, material received, or material transferred out, as required by DoD Regulation 4140.1-R and Army Regulation 735-5.

Department of the Army Comments

The Deputy PEO agreed with the recommendation and stated that FAR 52.245-1 and DFARS PGI Subpart 245 require the contractor to establish a detailed transaction history for CAP. Additionally, he stated that PMO Stryker will maintain a detailed transaction history for all Government property in accordance with the DoD and Army regulations.

f. Adhere to DoD Financial Management Regulation 7000.14-R, volume 4, chapter 4, and report the Stryker inventory on Army Financial Statements in the appropriate general ledger accounts to support the Army's goal of having auditable financial statements to comply with Public Law 111-84, section 1003.

Department of the Army Comments

The Deputy PEO agreed with the recommendation and stated that the Stryker inventory that was procured and accepted on completed contracts would be recorded in the LMP system for reporting on the Army financial statements. He stated that this process began on October 1, 2011, and would be completed by March 1, 2014. However, he stated that Stryker inventory classified as CAP would not be recorded on Army financial statements.

g. Accept delivery of Stryker inventory as Government property and value the inventory in Logistics Modernization Program before parts are requisitioned and charged to the Stryker brigades.

Department of the Army Comments

The Deputy PEO partially agreed with the recommendation and stated that the acceptance and valuation of all Stryker inventory procured under previous contract periods of performance would be completed by March 1, 2014. He stated that the acceptance and valuation process could not be completed before parts were requisitioned and charged to the Stryker brigades; however, the proposed transition period would allow time for the implementation of the recommendation while maintaining Stryker vehicle readiness.

h. Implement a comprehensive inventory management improvement plan that complies with the DoD comprehensive inventory management plan and addresses overforecasting, total asset visibility, excess inventory, economic retention requirements, and aggressive potential reutilization and disposal reviews to meet the intent of Public Law 111-84 section 328.

Department of the Army Comments

The Deputy PEO agreed with the recommendation and stated that the following inventory performance metrics were established for the contract as of October 1, 2011: requisition fill time; inventory turns; inventory accuracy; and first-pass stock availability. Additionally, he stated that PMO Stryker would routinely analyze worldwide requirements for other potential applications of excess parts. Further, the Deputy PEO stated that in May 2012, PMO Stryker developed a formal excess and obsolete inventory review process and added a contract requirement that requires General Dynamics to report excess and obsolete Stryker inventory to the Army for disposition. He stated that PMO Stryker would continue to review General Dynamics' requests for material disposition.

3. We recommend that the Program Executive Officer, Ground Combat Systems, develop performance standards for or Project Management Office, Stryker Brigade Combat Team personnel that address proper accountability and financial controls over all Government property.

Department of the Army Comments

The Deputy PEO agreed with the recommendation and stated that PEO Ground Combat Systems has performance standards for PMO Stryker personnel that address proper accountability and financial controls over all Government property.

Our Response

The Deputy PEO comments on Recommendations 2 and 3 were responsive and met the intent of the recommendations. No further comments were required.

4. We recommend that the Assistant Secretary of the Army (Acquisition, Logistics, and Technology), with support from the Assistant Secretary of the Army (Financial Management and Comptroller), establish a multifunctional support team with necessary knowledge, technical expertise, and creditability to properly account for the Government property procured on the cost-reimbursable services contract for Stryker vehicles and work with Project Management Office, Stryker Brigade Combat Team, to ensure that Stryker inventory has been assigned a value and recorded in appropriate Army accountability and financial accounting systems.

Department of the Army Comments

The Deputy for Acquisition and System Management, ASA(ALT), in coordination with ASA(FM&C), agreed with the recommendation and stated that the process for coordinating the multifunctional support team began in August 2009. Further, he stated that, during the most recent meeting in October 2012, the ASA(FM&C) committed to providing support to the multifunctional support team on an "as needed/as requested basis."

Our Response

The Deputy for Acquisition and System Management comments were responsive and met the intent of the recommendation. No further comments were required.

5. We recommend that the Program Executive Officer, Ground Combat Systems, require the Project Manager for the Stryker Brigade Combat Team to:

a. Perform a thorough review of all Stryker spare part inventory and take appropriate action to dispose of obsolete parts.

Department of the Army Comments

The Deputy PEO agreed with the recommendation and stated that, as of March 1, 2012, the CLS contract was modified to require General Dynamics to properly monitor and manage Stryker excess inventory. Specifically, he stated that the contractor was required to routinely report excess and obsolete inventory to the Army for disposition. In addition, he stated that, as a result of the new requirement, PMO Stryker identified \$5 million in unusable inventory from May 2012 through October 2012.

b. Perform a thorough review of excess Stryker inventory and determine whether the parts can be used to meet other related Stryker requirements and ensure any material buy-back provisions do not provide a disincentive for the contractor to fully use the excess inventory.

Department of the Army Comments

The Deputy PEO agreed with the recommendation and stated that PMO Stryker continuously reviews excess and obsolete inventory reports submitted by the contractor and analyzes world-wide requirements for other potential uses. Additionally, he stated that the excess inventory identified could be provided as Government-furnished material to the contractor if other requirements exist for non-CLS Stryker or other Government programs. Further, he stated that the next CLS contract, planned for award in December 2012, would include incentives to encourage General Dynamics to buy back excess Stryker inventory to support non-CLS requirements.

Our Response

The Deputy PEO comments were responsive and met the intent of the recommendation. No further comments were required.

Appendix A. Scope and Methodology

We conducted this performance audit from October 2010 through November 2012 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Interviews and Documentation

We met with representatives from ASA(FM&C); Acting Executive Director, Army Contracting Command, Warren, Michigan; Program Executive Office, Ground Combat Systems; and Project Manager, PMO Stryker.

We interviewed personnel from the Army Contracting Command, Warren, Michigan; PMO Stryker, Warren, Michigan; DCMA, Warren, Michigan, and Auburn, Washington; Defense Contract Audit Agency, Sterling Heights, Michigan; General Dynamics Land Systems, Sterling Heights, Michigan; Auburn, Washington; and London, Ontario Canada.

We reviewed copies of three Stryker contractor logistics support contracts (W56HZV-07-D-M112, DAAE07-02-C-B001, and W56HZV-06-C-B003) and acquisition planning documentation from PMO Stryker, dated from May 2002 to March 2012. For contract W56HZV-07-D-M112, we reviewed CLS contract line items of more than \$40 million on delivery orders 0019, 0169, and 0269, which totaled \$1.5 billion. Additionally, we reviewed inventory quantities, unit prices, purchase order and work-in-process histories, invoices, demand forecasts, and engineering change orders provided by General Dynamics. We also analyzed documentation from PMO Stryker, including inventory disposition schedules that were extracted from the DCMA's Plant Clearance Automated Reutilization Screening System and procurement contracting officer letters related to configuration changes. Additionally, PMO Stryker and General Dynamics personnel provided us with pictures and illustration of the spare parts.

We reviewed the public laws, FAR, DoD Regulations, and Army Regulations for guidance related to the accountability for and financial accounting of Government property. We also reviewed Government property valuation guidance from the DoD FMR 7000.14-R and USD(AT&L) and USD(C). Additionally, we reviewed criteria related to contractor-acquired property, including memorandum guidance from USD(AT&L).

Sample Selection

As of September 2010, General Dynamics managed 15,422 different Stryker parts. From the universe of 15,422 different parts, using professional judgment, we selected a nonstatistical sample of 28 parts with anomalies, such as large amounts of inventory with limited demand. For 23 of the sample parts, General Dynamics was able to provide a unit price; however 5 of the 28 parts did not have a unit price.

In March 2011, General Dynamics provided updated quantities on hand at the Auburn warehouse and in June 2011, General Dynamics provided purchase order and work-in-process histories for the 28 parts. For the five parts with no unit price, we used the latest purchase order or work-in-process cost and added a burden rate of either 17.92 percent for General Dynamics-U.S.-procured or -manufactured part or 23.68 percent for General Dynamics-Canada-procured or -manufactured part. The burden rate includes General Dynamics' costs of doing business, such as overhead, general and administrative, and procurement costs, and a profit of 9.50 percent.* We then excluded any parts from our sample that had an inventory value of less than \$20,000. Therefore, we removed 7 parts from the sample, leaving 21 parts in the final sample.

In January 2012, General Dynamics provided an updated Stryker inventory list that included 19,365 different parts, including 16,344 parts valued at \$892.3 million and 3,021 parts that were not assigned a value.

Obsolete and Excess Inventory Analysis

To determine whether excess inventory existed for our nonstatistical sample of 21 parts, we reviewed the total inventory of on-hand quantities as of January 30, 2012, and 2-year demand data as of September 1, 2011, that General Dynamics provided us. The inventory of on-hand quantities and demand data incorporated data for the CLS, BDAR, and Reset efforts because the comingled inventory for these three efforts could be used interchangeably to fulfill requirements for any of the efforts as needed. However, we excluded on-hand quantities designated as "flyaway packages" (mandatory parts that travel with the vehicles during missions) and anticipated authorized stockage list requirements (parts that are inventoried for the brigades) from the inventory on hand. For example, according to General Dynamics' records, part 10080435-01, "SEM Scanner," had a quantity on hand of 28 units. However, 12 units were dedicated to "flyaway packages," and 8 units were expected to be added to the authorized stockage list. Therefore, only eight units were available for consumption under CLS efforts.

We stratified inventory quantities to meet a 2-year demand for operational requirements and retention requirements, respectively. The operational inventory was classified as "Inventory Held for Resale" (Account 1521), and the retention inventory was classified as "Inventory Held in Reserve for Future Sale" (Account 1522). Any remaining quantity on hand for a particular part was classified as "Excess, Obsolete, and Unserviceable Inventory," (Account 1524). For example, for part 10650813, "Ring Gear Carrier," General Dynamics' records indicated the inventory on hand to be 2,581 units, valued at \$1.0 million, or \$390.18 each. The 2-year demand for this part was 98 units, valued at

* For a majority of the CLS years, General Dynamics earned a higher fixed fee (9.50 percent) for deployment CLINs as opposed to the garrison CLINs (9.25 percent). The deployment CLINs have a higher fixed fee because those Stryker vehicles require more scheduled and unscheduled maintenance than garrison vehicles. The deployment CLINs represent about 73.3 percent of the CLS costs. Therefore for the purposes of this report, we used the deployment CLINs fixed fee of 9.50 percent whenever we fully burdened unit prices for our sample parts.

\$38,237. Therefore, we populated both Accounts 1521 and 1522 with a value of \$38,237 to represent the dollar value of the 2-year demand requirement. The remaining 2,385 units, valued at \$930,574, were placed in Account 1524 because they potentially exceeded requirements.

Additionally, we determined the years of inventory by dividing in half the 2-year demand requirement to determine the annual demand for a given part. We then divided the inventory on-hand quantity available for CLS consumption by the annual demand requirement to determine how many years of inventory were available for future consumption given the current annual demand. For example, part 10650813, "Ring Gear Carrier," General Dynamics indicated quantity on hand of 2,581 units and a 2-year demand of 98 units for this part. We divided the 2-year demand of 98 units by 2 to determine an annual demand of 49 units. Then we divided the quantity on hand of 2,581 units by 49 units to determine that the Army had 52.7 years' worth of inventory that General Dynamics managed.

We determined that parts with less than 4 years of inventory on hand were acceptable to manage, while parts with more than 4 years of inventory exceeded requirements.

Use of Computer-Processed Data

We relied on the total inventory value of about \$892.3 million provided by General Dynamics for 16,344 different items for CLS, BDAR, retrofit, and Reset efforts. General Dynamics calculated the inventory value and quantities from various sources: Oracle, Data Management Information System, last purchase order price, a contractor data requirements list that provided moving-average prices, and contractor support team estimates. General Dynamics provided the following disclaimer with the data:

The information in this document has been prepared solely for information purposes in response to specific DoD Inspector General requests regarding government owned inventory. The information as presented herein is not an official record or deliverable of General Dynamics or any of its subsidiaries and should not be relied upon for any decision, analysis or evaluation regarding government owned inventory valuation. The data herein has not been verified or validated for accuracy particularly with respect to dollar valuations.

Although the inventory pricing data provided by General Dynamics was incomplete and we were unable to verify its accuracy, the exactness of the total inventory valuation is not material to the report finding and conclusions.

In April 2012, DCMA personnel reviewed and found no material deficiencies in General Dynamics' 100-percent physical inventory counts. Therefore, we determined the inventory quantities reported by General Dynamics to be sufficient and complete.

We also relied on purchase order histories and work-in-process reports generated by General Dynamics' Oracle system. We used the purchase order history and work-in-process reports to determine whether any parts were procured or manufactured after the

part became obsolete or if a part could be used for another effort (for example, production of the Stryker vehicles) or in a higher level assembly. We also used General Dynamics' purchase order and work-in-process histories to help calculate the unit prices for 2 of the 21 sample parts that General Dynamics was not able to value. We verified the accuracy of the purchase order or work-in-process job numbers, quantities ordered or completed, and unit prices indicated in the purchase order and work-in-process histories by comparing them to the actual purchase orders and work-in-process discrete job value reports. We also verified the completeness of the purchase order and work-in-process histories by observing General Dynamics extract the histories from its Oracle system.

We determined that the purchase order histories and work in-process reports obtained from General Dynamics provided sufficient evidence to identify parts that were potentially procured by General Dynamics and subsequently billed to the Army after the part went obsolete and to determine whether existing excess Stryker inventory could be used on different efforts to draw down the inventory.

We relied on computer-processed data from the Electronic Document Access system to identify the period of performance and total obligated amount for each contract line item number (CLIN) under contract W56HZV-07-D-M112 delivery orders 0019, 0169, and 0269. The Electronic Document Access system is a Web-based system that provides secure online access, storage, and retrieval of contracts and contract modifications to authorized users throughout DoD. To assess the reliability of contract modifications extracted from the Electronic Document Access system, we compared the contract modifications to PMO Stryker contract files and determined that the contract modifications extracted from the Electronic Document Access system presented no errors. Therefore, we determined that the contract modifications extracted from the Electronic Document Access system provided sufficient and complete evidence that was reliable for the purposes of this report.

Overall, we did not find errors that would preclude the use of the computer-processed data to meet the audit objectives or that would change the conclusions we reached.

Prior Coverage

During the last 5 years, the Government Accountability Office (GAO) and the DoD Inspector General (DoD IG) have issued three reports related to the Army logistics support contract for the Stryker vehicle with General Dynamics. Unrestricted GAO reports can be accessed over the Internet at <http://www.gao.gov/>. Unrestricted DoD IG reports can be accessed at <http://www.dodig.osd.mil/audit/reports>.

GAO

Report No. GAO-11-240R, "DoD's 2010 Comprehensive Inventory Management Improvement Plan Addressed Statutory Requirements, But Faces Implementation Challenges," January 7, 2011

Report No. GAO-12-493, "Defense Inventory: Actions Underway to Implement Improvement Plan, but Steps Needed to Enhance Efforts," May 3, 2012

DoD IG

Report No. DODIG-2012-102, "Better Cost-Control Measures Are Needed on the Army's Cost-Reimbursable Services Contract for Logistics Support of Stryker Vehicles," June 18, 2012

Appendix B. DoD Guidance Memorandum on Contractor-Acquired Property



ACQUISITION,
TECHNOLOGY
AND LOGISTICS

OFFICE OF THE UNDER SECRETARY OF DEFENSE
3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000

JAN 11 2010

MEMORANDUM FOR COMMANDER, UNITED STATES SPECIAL OPERATIONS
COMMAND (ATTN: ACQUISITION EXECUTIVE)
COMMANDER, UNITED STATES TRANSPORTATION
COMMAND (ATTN: ACQUISITION EXECUTIVE)
DEPUTY ASSISTANT SECRETARY OF THE ARMY
(PROCUREMENT), DASA(P)
DEPUTY ASSISTANT SECRETARY OF THE NAVY
(ACQUISITION AND LOGISTICS MANAGEMENT),
ASN (RDA)
DEPUTY ASSISTANT SECRETARY OF THE AIR FORCE
(CONTRACTING), SAF/AQC
ASSISTANT SECRETARY OF DEFENSE (LOGISTICS AND
MATERIEL READINESS)
DIRECTORS, DEFENSE AGENCIES
DIRECTORS, DOD FIELD ACTIVITIES

SUBJECT: Contractor Acquired Property (CAP) under Cost Reimbursement Contracts
and Line Items

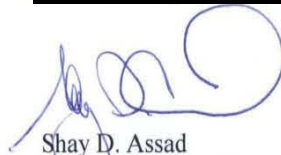
This memorandum is issued to clarify Department of Defense (DoD) business rules for Contractor Acquired Property (CAP). CAP, as defined by the Federal Acquisition Regulation (FAR) 45.101, is property acquired, fabricated, or otherwise provided by the contractor for performing a contract and to which the Government has title. Business rules relative to CAP are exclusive to cost-reimbursement contracts as well as cost reimbursement line items under mixed type contracts and cost reimbursement delivery orders under indefinite delivery contracts or basic ordering agreements.

Historically, some DoD Components sought to establish accountable property records for CAP — an inefficient practice that resulted in duplicate accountability records. In a joint memorandum entitled “Military Equipment Valuation Contractor Acquired Property Business Rule,” dated December 22, 2007, the Office of the Under Secretary of Defense (Comptroller) and Under Secretary of Defense (Acquisition, Technology & Logistics) clarified the Department’s policy (attached). The business rule states that although title passes to DoD when the property is obtained by the contractor, the property will not be recorded on DoD financial statements (as other than construction in process) or in accountability systems until the property is delivered to DoD.

Given the many ongoing audits and Congressional interest in Government Property, it is imperative that DoD Components understand the business rules for CAP, as well as the aforementioned change in accountability and financial record keeping, and that they ensure that accountable property records are established for CAP only upon delivery to the Government on a contract line item number (CLIN).

The procedures and guidance in the attachment for formulation and valuation of CLINs for CAP delivery shall be published as PGI 245.401, Contractor Acquired Property, within 90 days from the date of this memorandum.

My point of contact for this matter is [REDACTED]



Shay D. Assad
Director, Defense Procurement
and Acquisition Policy

Attachment:
As stated

ATTACHMENT

SUBJECT: Business Rules for Establishing Accountable Property Records for
Contractor Acquired Property (CAP)

1. Title.

a. The Government has title to CAP (under cost reimbursement contracts).

b. Title to property acquired by contractors under fixed price contracts is dependent on the contract terms and conditions as follows:

1) Fixed price contracts. The contractor retains title to all property acquired, except for property identified and ultimately delivered and accepted as a deliverable end-items on CLINs.

2) Fixed price contracts with contract financing provisions. The Government obtains title to property acquired by the contractor under financing clause(s), up until the point the property is accepted as a deliverable end-item, and all payments have been liquidated. This property is not considered CAP.

c. Government furnished property (GFP). The Government retains title to all GFP until ultimately disposed of by authorized means as specified in Federal Acquisition Regulation (FAR) Part 45. CAP items subsequently delivered on a CLIN are considered GFP when retained by the contractor for continued use under a contract. In such cases, and in accordance with the requirements of FAR 45.102, the items shall be added to the contract as GFP by contract modification.

2. General CAP Business Rules

a. The Requiring Activity, in partnership with the contracting specialists, should determine the CAP items that are required to be delivered. The following procedure acknowledges that CAP may not be anticipated at the time of contract award.

1) A CLIN, included at contract award, shall include a Contract Data Requirements List (CDRL) for the contractor to deliver a list of all CAP items (as required). The delivery date for that list should be at the discretion of the Requiring Activity, but no later than contract performance completion.

2) When CAP items are selected for delivery to the Government, a CLIN should be structured for CAP delivery and an Exhibit established in accordance with FAR Procedures, Guidance and Instructions (PGI) 204.7105. This will allow identification of CAP and enable the contractor to establish the property acquisition value and date placed in service upon delivery of the items in that Exhibit.

a) Separate CLINs should be established for material, equipment, special tooling, and special test equipment.

b) CLINs should be identified as "Not Separately Priced", unless an equitable adjustment is necessary, as determined by the Contracting Officer (CO).

b. CAP items meeting the Item Unique Identification (IUID) criteria of DFARS 211.274-2 should be marked and reported to the DoD UID registry upon delivery in accordance with the clause at DFARS 252.211-7003. Requiring activities should update paragraph (c)(1)(ii) of that clause, as required to insert the Exhibit Line Item Numbers (ELINs) of those items.

c. Oversight and visibility of CAP not designated for delivery to the Government is limited to reviews and audits of contractor accounting and property management systems. Property management systems are maintained in accordance with the requirements of FAR 52.245-1(b)(1).

3. Business Rules for Establishing Property Accountability

a. Consistent with the FAR required order of disposition precedence, once the contractor determines that the CAP is no longer needed for contract performance, the contractor may purchase that item at original acquisition cost (See FAR 52.245-1(j)(2)). If the contractor does not use this option, then the contractor should notify the CO if use of the property in the performance of other Government contracts is practical.

b. GFP items shall be added to and/or removed from the contract by contract modification(s) to both the losing and gaining contracts, and recorded via submission of a Property Transfer action through Wide Area Work Flow.

c. Excess contractor inventory (See FAR 45.101), including CAP, is disposed of in accordance with FAR Clause 52.245-1, Government Property; 52.245-2 or 52.245-5, as applicable, i.e., reported on Inventory Disposal Schedules (SF 1428) or to the Plant Clearance Automated Reutilization Screening System. The Inventory Disposal Schedule is suitable for the CDRL data description (paragraph 2.a.1).

4. GFP Business Rules

a. If required, CAP items may be delivered in place of the acquisition contract. The property is then considered GFP and meets the reporting criteria of DFARS 211.211-7007, and must be reported to the UID registry, once rule 3 b actions are complete.

b. Provided the requirements of FAR Part 45.102 are met, CAP may be retained for continued contract performance. If the requirements of FAR Part 45.102 do not apply, the items may be declared excess.



OFFICE OF THE SECRETARY OF DEFENSE

WASHINGTON, DC 20301

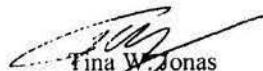
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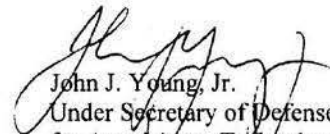
MEMORANDUM FOR SECRETARIES OF THE MILITARY DEPARTMENTS
COMMANDER, U.S. SPECIAL OPERATIONS COMMAND
DIRECTORS OF THE DEFENSE AGENCIES
DIRECTORS OF THE DEPARTMENT OF DEFENSE
FIELD ACTIVITIES
ASSISTANT TO THE SECRETARY OF DEFENSE
(NUCLEAR, CHEMICAL AND BIOLOGICAL DEFENSE
PROGRAMS)

SUBJECT: Military Equipment Valuation Contractor Acquired Property Business Rule

The attached business rule was developed in response to questions and issues raised by the DoD Components regarding financial accounting and property accountability for Contractor Acquired Property (CAP). The rule states that while title passes to DoD when the property is obtained by the contractor, the property will not be recorded on DoD financial statements (as other than construction in process) or in accountability systems until the property is delivered to DoD. This business rule will be incorporated into the DoD Financial Management Regulation.

Questions concerning this memorandum and the attached business rule should be directed to [REDACTED]


Tina W. Jonas
Under Secretary of Defense
(Comptroller)


John J. Young, Jr.
Under Secretary of Defense
for Acquisition, Technology and Logistics

Attachment:
As stated



Business Rule: Accounting for and Accountability of Contractor Acquired Property

DESCRIPTION OF ISSUE

The purpose of this paper is to provide the requirements for accounting for Contractor Acquired Property (CAP) in accordance with the provisions of Statement of Federal Financial Accounting Standards (SFFAS) No. 6, *Accounting for Property, Plant, and Equipment*. It also addresses how CAP should be managed in the Government's accountability systems.

BACKGROUND

Statement of Federal Financial Accounting Standards (SFFAS) No. 6, *Accounting for Property, Plant, and Equipment*, requires that Property, Plant and Equipment (PP&E) shall be recognized when title passes to the acquiring entity or when the PP&E is delivered to the entity or to an agent of the entity. In the case of constructed PP&E, the PP&E shall be recorded as construction-in-progress until it is placed in service, at which time the balance shall be transferred to general PP&E.

Contractor acquired property (CAP) is property obtained or otherwise provided by the contractor for performing a contract. Contractors may acquire property, as a direct cost to the Government, to fulfill the contract's requirements. When this occurs, the Government takes title to the property under the terms and conditions of the Government property clause.

DoD policies, processes, and practices are structured on delivery, receipt and acceptance of property. This aligns and is consistent with other DoD processes and practices, e.g., Wide-Area Work Flow, Unique Item identification. Although the DoD may have title to some property, e.g., property acquired, fabricated, or otherwise provided by the contractor for performing a contract, such property has not yet been delivered.

ACCOUNTING TREATMENT

The cost of contractor acquired property and other reimbursed costs should be accumulated in the construction-in-progress (CIP) general ledger account for posting to the applicable General Property, Plant, and Equipment account when construction or manufacturing is completed. For General and Military Equipment, construction-in-progress is transferred to the applicable General Property, Plant,

and Equipment account on the date the asset is placed in service¹ and recorded in the appropriate property accountability system.

With respect to contractor acquired property, upon completion of the construction or manufacture of end items for which the contractor acquired property was used and delivery of the contractor acquired property to the Government, contractor acquired property should either be capitalized in the appropriate Property, Plant, and Equipment account or if the contractor acquired property does not meet the capitalization threshold, such items should be recorded in the appropriate expense account. The amount transferred from CIP will be the Contractor's estimated fully burdened unit cost of contractor acquired property at the time of delivery to the Government.²

ACCOUNTABILITY TREATMENT

Upon delivery to the Government, contractor acquired property should be recorded in the appropriate property accountability system. Consistent with DoDI 5000.64, there is no requirement for accountability by DoD Components for such property prior to delivery to the Government. Third parties (to include contractors) have stewardship responsibility, to include creating and maintaining records of all Government property accountable to the contract, consistent with the terms and conditions of the contract or third party agreement, for the Government property in their care.

AUTHORITATIVE GUIDANCE

Statement of Federal Financial Accounting Standards No. 6, "*Accounting for Property, Plant, and Equipment*"

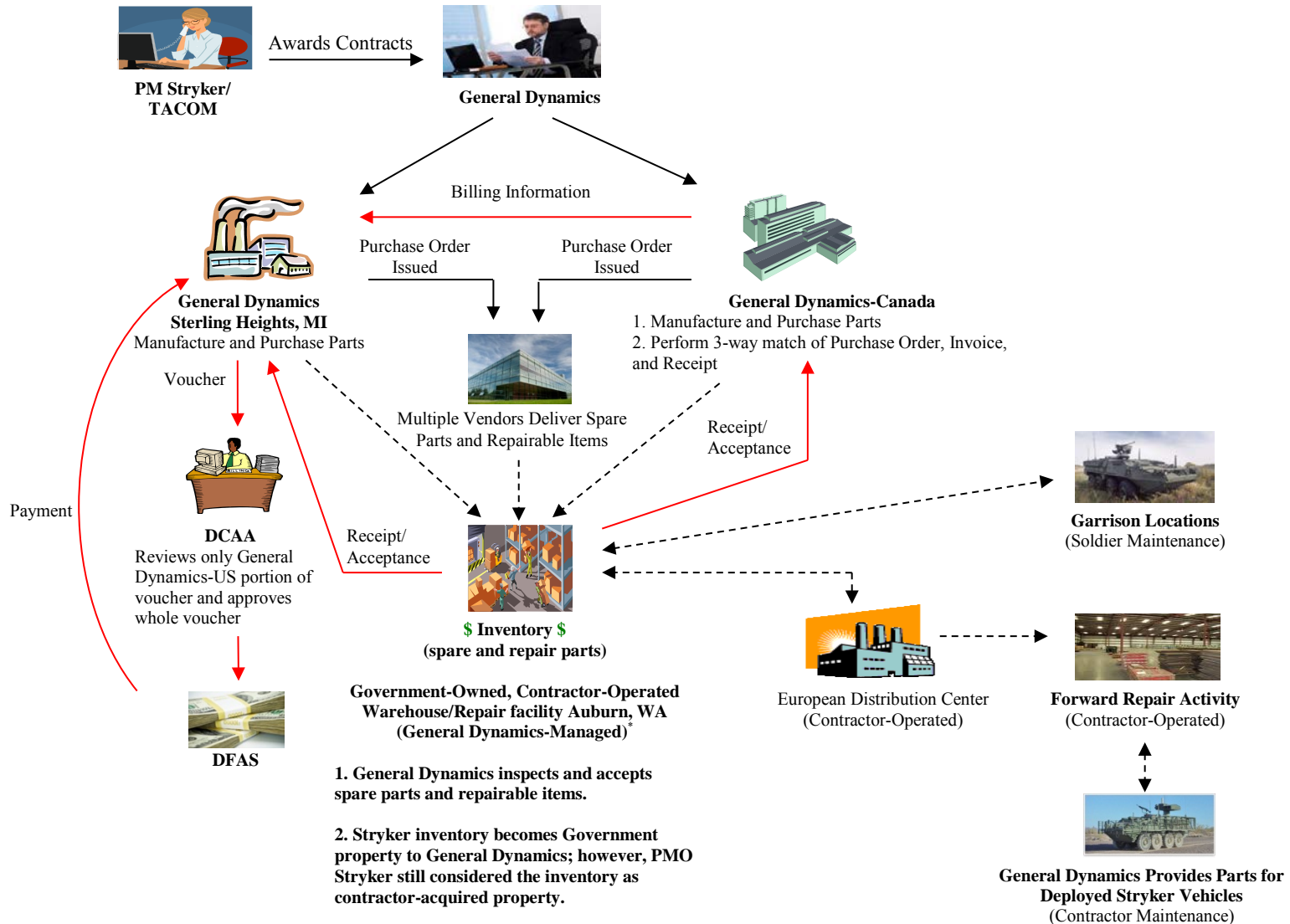
DoDI 5000.64, "*Accountability and Management of DoD-Owned Equipment and Other Accountable Property*"

DoD Financial Management Regulation, Volume 4, Chapter 6 (now under revision)

¹ DoD Financial Management Regulation (FMR), DoD 7000.14-R, Volume 4, Chapter 6, "Property, Plant and Equipment," (paragraph 060105) defines recognition for Military Equipment as "normally be the date shown on Block 22, Receiver's Use, of the "Material Inspection and Receiving Report" (DD Form 250) or the equivalent date source under Wide Area Work Flow."

² Defense Federal Acquisition Regulation Supplement (DFARS) 211.274-3 Policy for valuation.

Appendix C. Stryker Inventory Was Not Recorded or Assigned a Value in a DoD Accountability System



----- Indicates movement of parts
 _____ Indicates billing, voucher, and payment process
 *Repair & Overhaul parts are repaired by General Dynamics or sent to original vendor for repair.

Appendix D. Baseline Valuation for DoD Inventory and Operating Materials and Supplies



OFFICE OF THE SECRETARY OF DEFENSE
WASHINGTON, DC 20301



NOV - 8 2005

MEMORANDUM FOR UNDER SECRETARY OF THE ARMY
UNDER SECRETARY OF THE NAVY
UNDER SECRETARY OF THE AIR FORCE
DIRECTOR, DEFENSE LOGISTICS AGENCY


SUBJECT: Baseline Valuation and Certification for Department of Defense (DoD)
Inventory and Operating Materials and Supplies

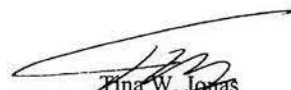
The Under Secretary of Defense (Comptroller) (OUSD(C)) established an Inventory and Operating Materials and Supplies (I&OM&S) Working Group with representatives from the OUSD(C), the Office of the Under Secretary of Defense (Acquisition, Technology and Logistics), the DoD Military Components, and the Office of the Inspector General, DoD. The Working Group reviewed valuation methodologies and criteria and determined which ones would lead to an auditable historical I&OM&S baseline cost for the more than \$200 billion reported in DoD's financial statements.

The Deputy Chief Financial Officer issued a memorandum, dated July 6, 2001, directing the use of moving average cost as the approved historical cost method for DoD. There are several ongoing initiatives to modify existing systems or migrate to commercial systems to calculate historical cost and one of the most critical elements to achieving success is to determine and establish the initial baseline value for on-hand inventories.

Attachments 1 through 3 provide summary and general criteria for addressing I&OM&S baseline valuations, to include the proof-of-principle valuation methods report developed by the Working Group. Attachment 4 summarizes I&OM&S systems that are currently capable of computing moving average cost or are in the process of being implemented at scheduled Component activities. Attachment 5 is the required baseline certification template which must be completed in accordance with the policies stated in Attachments 1 through 3.

If you have questions, you may contact [REDACTED]


Kenneth J. Kueg
Under Secretary of Defense
(Acquisition, Technology and Logistics)


Tina W. Jones
Under Secretary of Defense
(Comptroller)

Attachments:
As stated



Attachments 3 through 5 omitted due to length. Copies will be provided upon request.

Policies and Requirements

- All DoD Components and activities reporting material amounts of I&OM&S on their audited financial statements must take action to establish historical moving average cost (MAC) baseline valuations in line with a process that parallels Attachments 2 and 3, verify the physical existence of quantities used in baseline computations, and certify the work completed and the values computed as outlined in Attachment 5.
- All Components and activities must integrate the baselining procedures within their long range plans to provide I&OM&S line item assertions - and within their Enterprise Resource Planning tools or other systems design schedules to compute and maintain moving average cost.
- Components and activities may not continue to convert baseline valuations from one non-compliant value to another non-compliant value, e.g., from latest acquisition cost (LAC) to LAC without completing a reasonable and exhaustive baselining process.

In addition, Attachment 4 lists I&OM&S systems which can currently compute moving average cost, or are in the process of being implemented with or migrated to MAC functionality. Some systems include conversions which have already taken place, but which did not establish acceptable or auditable baselines. These systems represent the first priority for acceptable baseline conversions since they should provide the capability to sustain MAC values. Systems which have been converted from LAC to LAC must be rebaselined as the most immediate priority.

Systems which cannot currently maintain MAC, or which will not have MAC functionality in the near future, represent potential risk and cost in terms of baseline sustainment. For these systems, or for these categories of I&OM&S, addressees should consider possible sustainment alternatives and costs in their action plans. Alternatives may include parallel automated software applications or personal computer based off-line systems. In some instances, where there is a low volume of procurements and issues such as high-dollar, low transactions items, manual based sustainment may be possible. Sustainment alternatives and plans may also be impacted by the potential length of time required for maintenance.

Addressees should review the Attachments to this memorandum and the policies stated above and provide this office with your Plan of Action and Milestones for conducting baseline valuations for all material I&OM&S systems and for your I&OM&S financial statement line item values. Your plans should consider the requirement to:

- Follow the attached baselining process prior to or in conjunction with all MAC systems conversions.

Attachment 1
Page 1 of 2

- Include the process as a part of your Financial Improvement Business Rules for corrective actions, validations, and assertions.
- Take priority action to perform baseline valuations for those systems addressed in Attachment 4 and to re-baseline those systems that were not originally converted in accordance with this policy.
- Determine baseline sustainment alternatives and estimated costs for systems which cannot maintain moving average cost as discussed above.
- Provide evidence and your certification of supported and estimated values, to include verification of the physical existence of quantities used, as outlined in Attachment 2 and in Attachment 5. Baseline certifications must be signed by addressees' Assistant Secretaries or Deputy Assistant Secretaries for Financial Management or Component Comptrollers or Deputy Comptrollers.

Critical Steps for Inventory and Operating Materials & Supplies **Baseline Valuation**

Verification of Physical Existence of Quantities. The following baseline valuation steps are primarily predicated on an iterative and information gathering process utilizing data in stock control, logistics, and inventory accounting systems which support and maintain reportable on-hand quantities for Inventories and Operating Materials and Supplies (I&OM&S). However, in order for baseline valuations to have audit credibility, quantities used in the baseline valuation process must be verifiable to actual physical existence. The actual physical existence and verification of quantities should be performed at the beginning stage of the process, e.g., in conjunction with or after Steps 1 or 2. Early verification is necessary in order to preclude the potential for expending significant resources going to the end of the process utilizing unsupported quantities.

Step 1 - Review all managed or held I&OM&S items with National Stock Numbers, Manufacture's Part Numbers or other identifying item numbers in supporting I&OM&S stock/logistics systems. Determine items which have quantities reported as "on-hand" by the supporting system(s). Verify the accuracy and integrity of supporting systems that compute and maintain quantities. Establish a workable database for all items being baselined which had reported on-hand quantities.

Step 2 - Determine and include in the database all available acquisition histories related to items being baselined which had reported on-hand quantities. (Acquisition history includes information and data elements in supporting logistics or management systems indicating procurement action, such as last representative buy quantity and price.)

Step 3 - Determine initial baseline historical values for those items with reported on-hand quantities using quantities for the most recent acquisition histories. Use the next most recent acquisition data (and etc.) until all reported on-hand quantities being baselined have been identified to an initial historical baseline value.

Step 4 - Validate reported on-hand quantities with acquisition histories to supporting source documentation, e.g., hardcopy contracts, contract data repositories, contract data databases, or other supporting documentation such as delivery orders, purchase orders, and receipt documentation.

Step 5 - Validate reported on-hand quantities with acquisition histories, but with no supporting contract information, to corroborative information such as commercial sources (for example, the IHS Corporation Federal Logistics Information System HAYSTACK web-based database or other commercial pricing sources) or other similar and multiple acquisition histories (e.g., with similar dollar values).

Step 6 - For reported on-hand quantities with acquisition histories, but no supporting contract information and no acceptable corroborative information, determine the availability of corroborative information for like items (for example, items classified as interchangeable items and substitutable items).

Step 7 - For reported on-hand quantities with no acquisition histories and no supporting contract information or corroborative information, determine alternative corroborative correlations, e.g., standard price (less surcharges) comparisons to commercial price catalogs.

Step 8 - For reported on-hand quantities with no acquisition histories and no supporting contract information or corroborative or alternative corroborative information, determine values of like items as defined by item managers. Use values for like items when like items have supporting documentation or corroborative information.

Step 9 - For reported on-hand quantities with no acquisition histories and no acceptable supporting contract or corroborative information, determine actual repair costs incurred for on-hand quantities with repair histories as alternative corroborative information or as an alternative item valuation. Validate repair costs to supporting documentation for repair costs, e.g., depot maintenance work orders and commercial repair contracts.

Step 10 - For reported on-hand reparable item quantities found in Step 9 above (with no acquisition histories and no procurement or corroborative information) that cannot be corroborated to repair cost, use systems repair data as the alternative baseline valuation.

Step 11 - Determine the materiality to the financial statements of any reported on-hand quantities which have not been assigned a supportable or corroborative baseline value subsequent to completion of Steps 1 through 10. (In general, if materiality relative to the total financial statement values is not significant, use the current catalog price for Step 11 items minus surcharges.)

Step 12 - Assess the demand history or the probability of items being sold or issued for use. Items which have no demand history, support obsolete and retired weapons systems, or which have an otherwise remote chance of sale or issue should be baselined to a net realizable value unless item managers can provide reasonable evidence to the contrary.

Step 13 - For items which represent material values, and which will potentially have continued demand, determine alternative valuations for any items not valued subsequent to Steps 1 through 12. Alternative valuations include information based on expertise of item managers, Program Management Offices, budget programs for items in question, cost or engineering estimates, price deflators, or alternative data bases. All alternative baseline valuations should be documented for audit purposes.

Appendix E. DoD OIG Classification of Stryker Inventory (\$ millions)

		Inventory On Hand ¹		Requirements (Account 1521) ²		Contingency/Economic Retention (Account 1522) ²		Excess, Obsolete, Unserviceable (Account 1524) ²			
Review Part #	Part Number	Qty	Value	Qty	Value	Qty	Value	Qty	Value	Annual Demand Qty ³	Years of Inventory
Excess Inventory – Obsolescence											
1	1310010-501	768	\$56.898	0	0.000	0	0.000	768	\$56.898	0	∞
2	10655605-001	85	0.691	0	0.000	0	0.000	85	0.691	0	∞
3	10657371-001	24	0.242	0	0.000	0	0.000	24	0.242	0	∞
4	LS1009617	26	0.165	0	0.000	0	0.000	26	0.165	0	∞
5	10626152	7	0.001	0	0.000	0	0.000	7	0.001	0	∞
	Subtotal (5)	910	\$58.006	0	0.000	0	0.000	910	\$58.006		
Excess Inventory – Parts Can Be Used in Production or on a Higher Level Assembly											
6	10655317-001	7,568	\$0.893	0	0.000	0	0.000	7,568	\$0.893	0	∞
7	6600077-200	2,938	0.081	0	0.000	0	0.000	2,938	0.081	0	∞
8	16102788-011	97	2.065	5	\$0.106	5	\$0.106	87	1.852	3	32.3
9	7578478-061	52	6.642	5	0.639	5	0.639	42	5.365	3	17.3
10	10650112	170	1.100	20	0.129	20	0.129	130	0.841	10	17.0
	Subtotal (5)	10,825	\$10.781	30	\$0.875	30	\$0.875	10,765	\$9.032		

Note: Because of rounding, columns may not sum.

¹ Quantity (Qty) as of January 30, 2012; excludes any quantities required to be held for the authorized stock list or flyways.

² The DoD FMR 7000.14-R, volume 4, chapter 4, describes Account 1521 as “Inventory Purchased for Resale,” Account 1522 as “Inventory Held in Reserve for Future Sale,” and Account 1524 as “Excess, Obsolete, and Unserviceable Inventory.”

³ Annual demand quantities based on General Dynamics’ 2-year demand forecasts, as of September 1, 2011.

∞ Parts with no demand requirements; therefore, the years of inventory are infinite.

		Inventory On Hand ¹		Requirements (Account 1521) ²		Contingency/ Economic Retention (Account 1522) ²		Excess, Obsolete, Unserviceable (Account 1524) ²			
Review Part #	Part Number	Qty	Value	Qty	Value	Qty	Value	Qty	Value	Annual Demand Qty ³	Years of Inventory
Excess Inventory – Reduced Demand and/or Excessive Procurement Quantity											
11	10650815	9,179	\$0.572	15	\$0.001	15	\$0.001	9,149	\$0.570	8	1,147.4
12	10663271-001	1,845	1.303	3	0.002	3	0.002	1,839	1.298	2	922.5
13	10663270-001	1,783	1.259	11	0.008	11	0.008	1,761	1.243	6	297.2
14	10650813	2,581	1.007	98	0.038	98	0.038	2,385	0.931	49	52.7
15	10650817	1,741	0.494	91	0.026	91	0.026	1,559	0.442	46	37.8
16	10664080-001	1,831	1.317	113	0.081	113	0.081	1,605	1.154	57	32.1
	Subtotal (6)	18,960	\$5.951	331	\$0.156	331	\$0.156	18,298	\$5.639		
Acceptable Inventory											
17	10080344	35	\$1.928	21	\$1.157	14	\$0.771	0	0.000	11	3.2
18	10080435-01	8	3.241	6	2.431	2	0.810	0	0.000	3	2.7
19	LS1048040-305	16	2.996	16	2.996	0	0.000	0	0.000	18	0.9
20	10683033-001	3	0.041	3	0.041	0	0.000	0	0.000	9	0.3
21	10650344-011	22	2.180	22	2.180	0	0.000	0	0.000	183	0.1
	Subtotal (5)	84	10.386	68	8.805	16	1.582	0	0.000		
	Total (21)	30,779	\$85.125	429	\$9.835	377	\$2.612	29,973	\$72.677		

Note: Because of rounding, columns may not sum.

¹ Quantity (Qty) as of January 30, 2012; excludes any quantities required to be held for the authorized stock list or flyways.

² The DoD FMR 7000.14-R, volume 4, chapter 4, describes Account 1521 as “Inventory Purchased for Resale,” Account 1522 as “Inventory Held in Reserve for Future Sale,” and Account 1524 as “Excess, Obsolete, and Unserviceable Inventory.”

³ Annual demand quantities based on General Dynamics’ 2-year demand forecasts, as of September 1, 2011.

Appendix F. Summary of Potential Monetary Benefits

Recommendation	Type of Benefit	Amount of Benefit	Account
5.b	Economy and Efficiency. Reduces costs for future requirements by using current inventory to meet demand.	\$1.1 million of funds put to better use by reusing existing engine containers instead of purchasing new engine containers.	Army Working Capital Fund – 97X4930.001

Note: Potential monetary benefits are funds put to better use or questioned costs.

Defense Procurement and Acquisition Policy Comments



ACQUISITION,
TECHNOLOGY
AND LOGISTICS

OFFICE OF THE UNDER SECRETARY OF DEFENSE
3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000

OCT 15 2012

MEMORANDUM FOR DIRECTOR OF PRICING AND LOGISTICS ACQUISITION
OFFICE OF THE INSPECTOR GENERAL

THROUGH: DIRECTOR, ACQUISITION RESOURCES AND ANALYSIS

*NS
10/15/12*

SUBJECT: Response to DoDIG Draft Report D2011-D000CH-0032.001

As requested, I am providing responses to the general content and recommendations contained in the subject report.

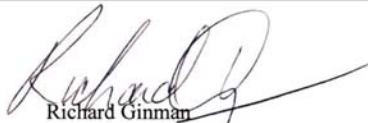
Recommendation:

The Director, Defense Procurement and Acquisition Policy working with the Assistant Secretary of Defense for Logistics and Materiel Readiness, needs to issue additional guidance that clarifies the proper use of CAP business rules specifically for logistics services contracts with no end item deliverables and how to properly account for inventory on these contracts that is not consumed during the contract period of performance.

Response:

Concur. Additional guidance will be published in 2nd Quarter of Fiscal Year 2013.

Please contact [REDACTED] if additional information is required.


Richard Ginman
Director, Defense Procurement
and Acquisition Policy

Department of the Army Comments



DEPARTMENT OF THE ARMY
OFFICE OF THE ASSISTANT SECRETARY OF THE ARMY
ACQUISITION LOGISTICS AND TECHNOLOGY
103 ARMY PENTAGON
WASHINGTON DC 20310

SAAL-SMS

05 NOV 2012

MEMORANDUM FOR UNITED STATES ARMY AUDIT AGENCY, 3101 PARK-CENTER DRIVE, ALEXANDRIA, VA 22302

SUBJECT: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles (Project Number D2011-D000CH-0032-001)

1. Pursuant to the Department of Defense Inspector General's (DoDIG's) memorandum, dated 17 Sep 12, the following information is provided to the DoDIG request for comments to their subject draft report.
2. The DoDIG recommendation two. We recommend the Program Executive Officer, Ground Combat Systems (PEO, GCS), require the Project Manager (PM) for the Stryker Brigade Combat Team to:
 - a. Accept delivery of all contractor-acquired property that was not consumed during the contract period of performance on a contract line item in accordance with the Defense Federal Acquisition Regulation Supplement, Procedures, Guidance, and Information 245.402.70. Additionally, all Stryker inventory identified in this report needs to be officially delivered and accepted as government property before the award of the follow-on Stryker contractor logistics support contract scheduled in Fiscal Year 2013.
 - b. Require General Dynamics to accept responsibility and create and maintain appropriate accountability records in accordance with Federal Acquisition Regulation 52.245-1 for any inventory considered contractor-acquired property or Project Management Office (PMO), Stryker Brigade Combat Team needs to accept delivery of the inventory at the government-owned, contractor-operated warehouse as government property.
 - c. Develop procedures to properly value the Stryker inventory, as required by the Department of Defense (DoD) Financial Management Regulation 7000.14-R, Volume 4, Chapter 4, or the follow the best practices outlined in the Under Secretary of Defense (USD) (Acquisition, Technology and Logistics) and the USD (Comptroller) memorandum, "Baseline Valuation and Certification for the DoD Inventory and Operating Materials and Supplies," dated 8 Nov 05.
 - d. Perform a thorough review of the Stryker inventory, record the inventory in an Army property accountability system and properly stratify the inventory as approved acquisition objective, economic retention stock, contingency retention stock, or potential

SAAL-SMS

SUBJECT: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles (Project Number: D2011-D000CH-0032-001)

reutilization stock, as required by the DoD Regulation 4140.1-R and Army Regulation (AR) 735-5.

e. Establish a detailed transaction history for Stryker inventory that records anticipated receipts of inventory as material due-ins, material received, or material transferred out, as required by the DoD Regulation 4140.1-R and AR 735-5.

f. Adhere to the DoD Financial Management Regulation 7000.14-R, Volume 4, Chapter 4, and report the Stryker inventory on Army Financial Statements in the appropriate general ledger accounts to support the Army's goal of having auditable financial statements to comply with Public Law 111-84, Section 1003.

g. Accept delivery of Stryker inventory as government property and value the inventory in Logistics Modernization Program before parts are requisitioned and charged to the Stryker brigades.

h. Implement a comprehensive inventory management improvement plan that complies with the DoD comprehensive inventory management plan and addresses overforecasting, total asset visibility, excess inventory, economic retention requirements, and aggressive potential reutilization and disposal reviews to meet the intent of Public Law 111-84, Section 328.

i. U.S. Army Management Action. See enclosure: AMSTA-CSC-J, subject: Draft Report: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles (Project Number: D2011-D000CH-0032.001), dated 17 Oct 12.

3. The DoDIG Recommendation three:

a. We recommend that the PEO, GCS develop performance standards for PMO, Stryker Brigade Combat Team personnel that address proper accountability and financial controls over all government property.

b. U.S. Army Management Action. See enclosure: AMSTA-CSC-J, subject: Draft Report: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles (Project Number: D2011-D000CH-0032.001), dated 17 Oct 12.

4. The DoDIG Recommendation four.

SAAL-SMS

SUBJECT: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles (Project Number. D2011-D000CH-0032-001)

a. We recommend that the Assistant Secretary of the Army (ASA) (Acquisition, Logistics, and Technology) and the ASA (Financial Management and Comptroller) (FMC) establish a multifunctional support team with necessary knowledge, technical expertise and creditability to properly account for the government property procured on the cost-reimbursable services contract for the Stryker vehicles and work with or PMO, Stryker Brigade Combat Team, to ensure that Stryker inventory has been assigned a value and recorded in appropriate Army accountability and financial accounting systems.

Revised

b. U.S. Army Management Action. The Army concurs and began the process in Aug 09, to establish a multi-functional team to properly account for the government property procured on the cost-reimbursable services contract for the Stryker vehicles and ensure that Stryker inventory will be assigned a value and recorded in the appropriate Army property accountability and financial accounting systems. The team has met as recently as 1 and 17 Oct 12. At the 17 Oct 12 meeting, the ASA(FMC) committed to assist and support the multifunctional team on a "as needed/as requested basis." This response has been coordinated with the appropriate personnel within ASA(FMC).

5. The DoDIG recommendation five. We recommend that the PEO, GCS, require the PM for the Stryker Brigade Combat Team to:

a. Perform a thorough review of all Stryker spare part inventory and take appropriate action to dispose of obsolete parts.

b. Perform a thorough review of excess the Stryker inventory and determine whether the parts can be used to meet other related Stryker requirements and ensure any material buy-back provisions do not provide a disincentive for the contractor to fully use the excess inventory.

c. U.S. Army Management Action. See enclosure: AMSTA-CSC-J, subject: Draft Report: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles (Project Number: D2011-D000CH-0032.001), dated 17 Oct 12.

SAAL-SMS

SUBJECT: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles (Project Number. D2011-D000CH-0032-001)

6. Additional comments from the PEO, GCS are included in the enclosure to assist in providing greater accuracy and clarity for the final report.

Encl



Harold J. Greene
Major General, GS
Deputy for Acquisition
And System Management



DEPARTMENT OF THE ARMY
PROGRAM EXECUTIVE OFFICE
GROUND COMBAT SYSTEMS
6501 E. ELEVEN MILE ROAD
WARREN, MICHIGAN 48397-5000

REPLY TO

AMSTA-CSC-J

17 Oct 2012

MEMORANDUM FOR Director of Pricing and Logistics Acquisition – Acquisition and Contract Management, Department of Defense Office of the Inspector General, 4800 Mark Center Drive, Alexandria, Virginia 22302-1500

SUBJECT: Draft Report: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles (Project No: D2011-D000CH-0032.001)

1. Reference memorandum, DODIG, dated 17 September 2012, subject as above.
2. We have reviewed subject DODIG Draft Report. In general, we do not agree with the findings. The PEO for Ground Combat Systems position is that the PMO Stryker Brigade Combat Team did have accounting for Government property procured on the Army Services Contract for logistics support of Stryker Vehicles. This contract adhered to the FAR, DFARs and guidance relative to accounting of Government Property in existence at the time of contract award. Further, modifications to this contract were reviewed, prior to award, to ensure compliance with current regulatory and legal requirements.
3. With regard to the recommendations in the report, although we did not agree with the findings, we do agree with recommendations 2.b, 2c, 2d, 2e, 2f, 2h, 3, 5a, 5b, and related potential monetary benefit. In addition, we concur in part to recommendations 2a. and 2g. Our specific comments are contained in the enclosed reply.
4. While the subject report focuses on the accountability of the Contractor Acquired Property (CAP) versus Government Furnished Property (GFP) items in question, the bigger issue is that the United States Government (USG) assumes increased liability when ownership of the material is transferred from contractor to Government and subsequently back to the contractor as GFP. When complying with the transfer of CAP under the existing contract to GFP under the follow on contract, the USG will assume additional risk with regard to items that are found defective after acceptance. This will be mitigated by a detailed review of the items being transferred, as well as by a quality check of complex, high dollar items. This risk could also be eliminated by deferring the transfer accountability until the contractual relationship ends with the prime contractor.
5. The TACOM Internal Review and Audit Compliance Office will track the status of the corrective actions through completion and perform a follow-up review to verify implementation.

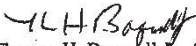
AMSTA-CSC-J

SUBJECT: Draft Report: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles (Project No: D2011-D000CH-0032.001)

6. Point of contact for this reply is

[REDACTED]

Encl


Thomas H. Bagwell Jr., SES
Deputy Program Executive Officer
Ground Combat Systems

DRAFT Response to DoDIG's Report #2, Project No. D2011-D000CH-0032.001, Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles

Objective: DoDIG's overall objective was to evaluate the effectiveness of the contractor logistics support sustainment strategy for Stryker vehicles. This report is the second in a series of three reports and reviews the contracting funding procedures, contract type, performance metrics, contractor billings, and controls over Government property that is being managed by the contractor.

DoDIG Conclusion: PMO Stryker officials did not properly account for Government property procured on the cost-reimbursable services contract for logistics support of Stryker vehicles.

ADDITIONAL FACTS: Response on DoD-IG Conclusion and related findings:

- I. Government property procured by a contractor in the performance of a cost-reimbursable logistic support contract is Contractor-Acquired Property (CAP) pursuant to the definition in Federal Acquisition Regulation 52.245-1 Government Property. Therefore, the conclusion and related factual findings providing PMO-Stryker inappropriately treated the inventory as CAP and incorrectly classified the Stryker inventory as CAP are factually incorrect.

The auditors' support the conclusion above by claiming that the Government property in inventory¹ "was not accounted for because PMO Stryker inappropriately treated the inventory as contractor-acquired property (CAP), while General Dynamics considered the inventory as Government property, not CAP, once delivered to the GOCO warehouse." Audit Report p. 8. The remainder of the audit report (pp. 9-28) goes on to point to all the policies and regulations that the Army failed to comply with, purportedly because it had improperly treated the property as CAP.

In order to properly classify the property at issue, one must have an understanding of Government Property, in general. The term "Government Property" is defined, in pertinent part, in FAR 52.245-1 as "all property owned or leased by the Government. Government property includes both Government-furnished and Contractor-acquired property." In other words, the term "Government Property" includes both Government-furnished property (GFP) and CAP.

Government-furnished property is defined as "property in the possession of, or directly acquired by, the Government and subsequently furnished to the Contractor for performance of a contract. Government-furnished property includes, but is not limited to, spares and property furnished for repair, maintenance, overhaul, or modification. Government-furnished property also includes contractor-acquired property if the contractor-acquired property is a deliverable under a cost contract when accepted by the Government for continued use under the contract." FAR 52.245-1.²

¹ The terms part(s), material, property, and inventory are used interchangeably, depending on how the term was used in the audit report or in other various references used throughout this response.

² This definition is from the April 2012 version of FAR 52.245-1. The applicable Government Property clause at the time of award was FAR 52.245-5 (Cost-Reimbursement, Time-and-Material, or Labor Hour Contracts) (Deviation, per DAR Tracking Number 99-00008, 13 July 1999).

CAP is defined as "property acquired, fabricated, or otherwise provided by the Contractor for performing a contract, and to which the Government has title." Id.

Under the CLS effort, the contractor was required to deliver Contractor Logistic Support ("CLS") services to the Government. That service was the end item deliverable under the contract. There was no separate deliverable in the contract for spare parts or material. In order for the contractor to deliver the contractually required service (i.e. CLS), the contract scope of work expressly mandated that it was the contractor's responsibility to decide what parts/material were needed and when, in order to successfully perform the contract. This is consistent with FAR 45.102 (a) which states that "[c]ontractors are ordinarily required to furnish all property necessary to perform Government contracts." The Government takes title to that property in accordance with FAR 52.245-1(e) and at that point in the acquisition process the property becomes CAP. Based on the FAR definition of CAP, and the facts of this procurement, the property procured and held inventory was in fact properly treated as CAP.

As will be discussed in more detail later, the report acknowledges the Stryker inventory is CAP in a couple of instances. The report finds GD did not account for the inventory in accordance with FAR 52.245-1 Government property guidance for CAP. Audit report pg 10. The report also acknowledges its uncertainty on the issue in other instances, finding the Stryker inventory "could possibly be considered CAP." Audit report pgs. 8, 10, and 15. It further acknowledges that DoD CAP and Government property policy experts opined, "inventory procured on the cost-reimbursement logistics services contract and consumed during the period the contract period of performance may be considered CAP."³ The report also makes specific findings that PMO Stryker incorrectly classified the Stryker inventory as CAP so additional analysis is provided to help clarify this issue.

The inventory was not delivered to the Army, it was delivered to the contractor in the course of the contractor acquiring property in the performance of its CLS contract. In order for the inventory to be "delivered to the Army" it would have to have been an end product deliverable under the contract, which would have been evidenced by a contract line item number (CLIN) on the contract. FAR 2.101 defines an end product, in pertinent part, as "supplies delivered under a line item of a Government contract." There are no such line items (i.e. CLINs) for parts and materials as end products on the CLS contract.

Also, any property that would have been deliverable under the contract would have to have identified a Free on Board ("F.O.B") point in order to determine, among other things, the responsibility and basis for payment of freight charges. See FAR 2.101, Definitions. The contract at issue, per the "Delivery Schedule for Delivery Orders" clause, 52.242-4457(b)(2) describes the two different types of F.O.B. points (origin and destination) and sets forth the specific FAR clauses that govern the different F.O.B. points ("F.O.B. Origin" - FAR 52.247-29

The contract was later modified to incorporate the Government Property clause FAR 52.245-1 (June/2007) "Government Property (Deviation) DARS Tracking #2007-0012." This clause defines GFP as "property in the possession of, or directly acquired by, the Government and subsequently furnished to the Contractor for performance of a contract." The contract has not been modified to incorporate the April 2012 as permitted by FAR 1.108(d)(3). However, the April 2012 version is analyzed here for simplicity as it tracks with the regulations cited in the audit report.

³ As will be discussed further below, it is PMO Stryker's position that the DoD CAP and Government property policy experts said the property was CAP, not that it "may be considered CAP" as indicated in the report.

and "F.O.B Destination" - FAR 52.247-34), to the extent there would be an F.O.B. point. Had the parties intended for the parts to be delivered to the Government under the contract, the contract would have to identify the property and the associated F.O.B. point(s). There are no F.O.B. points in the contract, because the contractor was providing a service, not an end item or product.

Further, a necessary element of "delivery" is acceptance of that delivery. Acceptance of property is defined in the DoDI 5400.64 glossary as a "formal certification that the goods or services have been received and that they conform to the terms of the contract." In order to properly "accept" this property, the Government would have to have had language in the contract that would enable it to determine whether the goods conformed to the terms of the contract (e.g. part numbers, performance spec, scope of work, etc.). There were no such terms in the contract because the parties had not contemplated delivery or acceptance of the property. In addition, there was no "formal certification" that would evidence acceptance of the property (e.g. form DD250, "Material Inspection and Receiving Report"). Therefore, it is improper to state that the government took delivery of this property.

In fact, without a CLIN in the contract, had the Army treated the property as a end product deliverable and begun accounting for such property it would have violated the direction in the USD(AT&L) memorandum, entitled "Contractor Acquired Property (CAP) under Cost Reimbursement Contracts and Line Items," dated January 11, 2010 (hereinafter the "January 2010 memo). That memorandum requires "DoD components ... ensure that accountable property records are established for CAP only upon delivery to the Government on a contract line item number (CLIN)."

Under the CLS contract, GD acquired certain property from its supplier and accepted that property for use under the CLS contract. As discussed previously, once the Government took title to the property the property became CAP. There would have been no basis for the Government to accept this property, since it was not a party to the contract(s) between GD and its supplier(s).

Accordingly, as the property procured and held in inventory was CAP by definition, the findings that PMO Stryker "inappropriately treated the inventory as contractor-acquired property," "incorrectly classified as CAP," and "could possibly be considered CAP" are factually inaccurate as they are contrary to the FAR definitions and the facts presented. The report should be revised to correct these findings. If not, the report should be revised to provide the supporting analysis for the determination that the property was inappropriately and incorrectly classified as CAP and how the property should been classified during the period of performance.

II. The audit report should provide additional facts to support its finding and conclusion and should analyze all of the facts utilizing FAR 52.245-1.

PMO Stryker asserts the facts to be added are the Stryker CLS contract incorporated all of the applicable Government property clauses at the time it was awarded in December 2006. Pursuant to the clauses in the contract and FAR 45 at the time, PMO Stryker correctly treated the Stryker inventory procured in the performance of the CLS contract as CAP. As such, GD was

responsible for accounting for it.⁴ This requirement continued and was reinforced when PMO Stryker officials modified the contract to incorporate FAR 52.245-1 Government property clause in July 2008. The policy change requiring delivery of excess CAP at the end of the contract for Government acceptance was not incorporated into the DFARs PGI 245.4 until January 2011. In May 2011, the DFAR PGI was again modified to clarify the transfer of the delivered excess property to the Government applied to orders on the same contract. These facts are missing from the report.

Applying FAR 52.245-1 (and other regulatory and policy guidance referenced throughout the report) to the findings in the report reveals it contains insufficient facts to perform a proper analysis of the regulations, the regulations contradict the findings and/or factual statements that are provided, and inconsistencies between the findings and supporting factual statements.⁵

The following are examples of the impact applying FAR 52.245-1 has on the findings in the report to illustrate this point:

- Bottom pg. 7, “Specifically, PMO Stryker officials did not treat the Army-owned Stryker inventory as [GP], and as a result, the Stryker inventory was not properly valued and recorded in appropriate Army property accountability and financial accounting systems.”

Response: The definition of GP in FAR 52.245-1 includes both CAP and GFP. The definition of CAP includes property acquired by a contractor in the performance of a contract to which the Government has title (i.e., ownership). The definition of GFP is property acquired by the Government and furnished to the contractor in the performance of the contract. FAR 52.245-1 further mandates that the contractor has stewardship responsibility over all GP accountable under the contract to include maintaining records of the value of the property in its property management system. The obligation to value and record the inventory in the appropriate Army property accountability and financial accounting systems does not attach to the PMO until after it accepts delivery of the inventory from the contractor.

The above finding is clearly at odds with FAR 52.245-1. By treating Army-owned Stryker inventory in the contractor’s possession, PMO Stryker is treating the property as GP. Further, as CAP, the obligation to properly value the property was imposed on the contractor by the

⁴ The FAR 45 re-write kept the same definition of CAP and incorporated it into FAR 52.245-1 (June 2007).

⁵ The Federal Acquisition Regulations (FAR) has the “force and effect of law.” As such, any of the examples that are inconsistent with the plain language of the FAR definition are incorrect as a matter of law. Put differently, the various findings cited in the following examples that treat GP differently than CAP are incorrect as a matter of law. See Paul v. United States, 371 US 245, 9 L Ed 2d 292, 83 S Ct 426 (1963). For additional discussion of this concept, see Chrysler Corp. v. Brown, 441 US 281, 60 L Ed 2d 208, 99 S Ct 1705 (1979); Labat-Anderson, Inc. v. United States, 42 Fed Cl 806 (1999) (citing Hamlet v. United States, 63 F3d 1097 (CA FC 1995)). Under the Supreme Court’s Chrysler decision, interpretive rules, general statements of policy or rules of agency organization, procedure or practice will not have the force of law. 5 U.S.C.A. § 553(b), (d); Reynolds Associates v. United States, 31 Fed Cl 335 (1994).

inclusion of FAR 52.245-1 in the contract. Therefore, contrary to the above finding, it was proper for the PMO Stryker not to value and record the property in Army property accountability and financial accounting systems.

- Top and middle pg. 8. "PMO Stryker officials did not properly account for Government property procured on the cost-reimbursable contract for logistics support of Stryker vehicles...Stryker inventory was not properly accounted for because PMO Stryker inappropriately treated the inventory as contractor-acquired property (CAP), while [GD] considered the inventory as Government property, not CAP, once delivered to the GOCO warehouse."

Response: This is similar to the example above. As previously noted, GP in the possession of the contractor is GFP and/or CAP pursuant to FAR 52.245-1. As such, if GP is not CAP as alleged, it can only be GFP. If the property is not GFP, it can only be CAP. Applying the following step-by-step analysis of FAR 52.245-1 to the facts helps to resolve this question: 1) Is it GP in the possession of the contractor? 2) If yes, is it (a) GFP or (b) CAP? Per the finding, the answer to (1) is yes. Step (2) is to determine if it's either (a) or (b). The audit report does not find or allege the property was GFP. Nevertheless, the test is whether GD or another supplier delivered the Stryker inventory to the Government, the inventory was accepted by the Government and furnished it to GD for performance of the CLS contract. The facts in this regard are missing so reasonable inferences could be made either way. The reader could infer the inventory must be GFP, based on the finding the GP was not CAP. But, this inference is contrary to the finding the inventory was procured in performance of the Stryker CLS contract. This finding meets the definition of meets the definition of CAP, not GFP. In other words, the logical inference from this is the inventory is CAP, not GFP. The problem is this is contrary to the finding the GP is not CAP. The circular nature of these arguments only proves more facts are needed in order to properly analyze FAR 52.245-1.

There is also a problem with the portion of the finding providing GD was not accounting for the inventory delivered to the GOCO warehouse because it was treating it as GP, not CAP. Pursuant to FAR 52.245-1(f)(1)(iii), the contractor is accountable for all government property, GFP or CAP, on the contract. This means GD was contractually obligated to account for the inventory simply by characterizing it as GP so the fact GD did not consider the inventory as CAP is immaterial. This finding could also be attributable to misunderstanding and/or inconsistent use of the term GP in general and throughout the report. Further, the finding seems to be at odds with some of the findings in Appendix A of the report about reviewing reports the contractor generated from its Oracle system regarding the property. Audit report pgs 31-34. The fact the contractor was able to generate reports related to over 16,000 items worth over \$800 million dollars suggests it was accounting for the property absent specific findings or discussion to the contrary.

It is also worth noting that if GD was procuring the parts in the performance of the CLS contract, then the parts were CAP pursuant to the definition in FAR 52.245-1. In other words, it was GD that was incorrectly classifying the inventory, not PMO Stryker.

- Finding top of page 9. “Stryker Inventory Was Not Assigned a Value and Recorded in Appropriate Army Accountability and Financial Accounting Systems.

Supporting factual statement/conclusion on page 10. “[GD] did not assign the inventory a value in its system ... because it considered the Stryker inventory to be [GP]. Therefore, [it] did not account for the Stryker inventory according to [FAR] Government property guidance for CAP.” (Emphasis added).

Response: Applying FAR 52.245-1 to the finding on page 9 and the supporting factual statement/conclusion in the discussion reveals that are inconsistent and contradictory. It also reveals that the factual statement/conclusion is correct one. The inclusion of the phrase “guidance for CAP” in the factual statement indicates the determination is the inventory is CAP because the guidance in FAR 52.245-1 is the same for GP and CAP. Accordingly, pursuant to FAR 52.245-1 guidance on CAP, GD is responsible for assigning a value accounting for Stryker inventory in its property management and financial accountability systems. Therefore, contrary to the finding on page 9, it is inconsistent with FAR 52.245-1 and other DoD guidance on CAP to assign a value to the Stryker inventory in the contractor’s possession and record it in Army accountability and financial accounting systems.

However, as will be explained in more detail below, the factual statement/conclusion on page 10 also contradicts most of the other findings and supporting statements in the report.

- Middle of page 10. “While [GD] officials classified Stryker inventory delivered to the GOCO warehouse as [GP], PMO Stryker officials incorrectly classified the inventory as CAP.”

Response: The same arguments that apply to the examples on pages 7 and 8 apply here as well. Moreover, this finding is contradicted by the finding at the top of page 10.

- Bottom quarter of page 10. “While Stryker inventory consumed during the contract period of performance for the logistics services contract *could possibly be considered CAP*, the inventory identified in this report was from prior-year periods and needed to be officially delivered and accepted by the Army and accounted for as Government property.” (Emphasis added)

Response: The following summarizes the three key factual findings on page 10:

- (a) GD is at fault for NOT treating Stryker inventory as CAP;
- (b) PMO-Stryker is at fault for treating it as CAP; and
- (c) The inventory consumed during the period of performance “*could possibly be considered CAP*” (so implicitly this means it could also possibly not be considered CAP).

These three factual statements underscore the need for additional supporting facts and explanation of the underlying rationale in the report. For instance, the report does not supply facts nor an explanation clarifying how the Stryker inventory can be both CAP and not CAP at the same time. Similarly, the report does not provide an explanation for finding the inventory

“could possibly be considered CAP” and possibly not be considered CAP. This is particularly important here considering PMO Stryker, DCMA and the Government property policy experts all opined the referenced inventory is CAP. Without such facts and explanation, the report will not achieve its purpose of educating the reader and protecting the integrity of the procurement process.

- Bottom of page 10, top of 11. “By classifying the Stryker inventory as CAP, PMO Stryker officials were able to bypass the accountability and financial reporting requirements for Government property after the Stryker inventory was delivered to the GOCO warehouse.”

Response: PMO Stryker objects to the implication that by classifying the Stryker inventory as CAP it was bypassing any financial reporting requirements. The Stryker inventory was being procured by GD in the performance of the CLS Stryker so pursuant to FAR Subpart 45 it had to be classified as CAP. Further, classifying the property as CAP does not bypass any accountability or reporting requirements as the report suggests, rather it places the burden of accounting and reporting on the contractor.

Utilizing partial language from guidance documents will lead to contextual misinterpretations. For instance, the sentence following the lengthy quote from the joint USD (AT&L) and USD(C) memorandum, “Military Equipment Valuation Contractor Acquired Property Business Rule,” December 22, 2007 on page 11 of the report is reads as follows: “Consistent with DODI 5000.64, there is no requirement for accountability by DOD Components for such property prior to delivery to the Government. Third parties (to include contractors) have stewardship responsibility, to include creating and maintaining records of all Government property accountable to the contract...”. (Emphasis added).

This language refutes the various findings and recommendations in the report that PMO Stryker should have accounted for the inventory in Army property accountability and financial accounting systems. A fair and objective analysis requires the report consider and analyze this statement in relation to the facts.

- Bottom of Page 13: “Although PMO Stryker and Army Contracting Command officials classified the Stryker inventory as CAP, the officials did not require General Dynamics to account for the inventory as CAP, follow guidance and accept delivery of CAP by contract line item where the material then becomes Government property, or identify the actual cost of the CAP inventory acquired on previous contracts and transfer the inventory cost to the current Stryker CLS contract.”

Response: This is another factually inaccurate finding. PMO Stryker did require GD to account for the inventory as CAP by including the applicable Government property clauses in the contract. The Stryker CLS contract also included a number of different CDRL reporting requirements related to the parts procured and held in inventory. This finding further does not

acknowledge that the GP Rules requiring the delivery of excess CAP to the Government for acceptance and for transfer between orders on the same contract was not implemented until May 2011. It does not acknowledge that the requirement that CAP items be delivered and accepted by the Government before being transferred between contracts was not implemented until January 2011, approximately four years after the CLS contract was awarded. As such, at a minimum, the report should include these findings in the report and consider them in its analysis and conclusions.

- Top of pg. 16, “PMO Stryker officials inappropriately categorized all Stryker inventory as CAP and did not recognize the inventory...as Government property, which could include CAP, that was managed in the contractor’s inventory management system.”

Response: This is another example of the report treating CAP and GP differently. Pursuant to FAR 52.245-1, GP in the possession of the contractor is either CAP or GFP. If it is not CAP, then it has to be GFP and vice versa. Regardless, the contractor is accountable for all GP on the contract.

This is the only time the word “all” is used. This implicitly recognizes at least some of the property was correctly classified as CAP, which again contradicts the various findings about the property being “incorrectly classified,” “could possibly be considered CAP,” or “may be considered CAP.” The report needs to explain which inventory the IG believes was correctly characterized as CAP. It should also consider the GP rules in place at the time and the contract.

This finding further indicates the property “was managed in the contractor’s inventory management system.” This contradicts the findings that the property was not being managed and was not being accounted for in either the Army or contractor property management system. This portion of the finding also contradicts the various factual findings that GD was not accounting for the property in its system because it classified the property as GP.

As noted previously, the audit report incorporates the FAR definition of CAP. Audit report, p. 10. The report further provides, “CAP business rules for cost-reimbursable contracts were generally designed to address *“property acquired, fabricated, or otherwise provided by the contractor”* that would eventually be delivered to the Government as part of a higher level end item, not as used by the Army on its logistics services contract with no end item deliverable.” Audit Report p. (i), 8, 10, and 15.

Response: The report never explains why the business rules being designed for CAP that is delivered as part of a higher level end item is important or significant to its analysis or findings. It also never explains the basis or authority for the interpretation. It should also be noted that a review of the CAP business rules will reveal the statement is not entirely supported. In fact, it appears the CAP business rules were also designed for CAP items that were not intended as a deliverable at the time of award. Specifically, paragraph 2(a) of the General CAP business rules provides, “[t]he following procedures acknowledges that CAP may not be anticipated at the time of contract award.” The business rules further describe the procedures to follow to account for CAP that is not part of an end item deliverable. Audit report p. 38. The interpretation in the audit report must therefore be assumed as the subjective interpretation of the auditors.¹ As such, the

audit report should be revised to explain basis for this interpretation as well as why it is significant.

It is conceivable the report relies on this interpretation of the CAP business rules as the basis for the following discussion:

“...[T]he Stryker inventory stored at the GOCO warehouse does not support the production of Stryker vehicles that are later delivered to the Army and accepted by DCMA. Instead, the Stryker inventory consists of spare parts that are used to sustain fielded Stryker vehicles for which the Army had already taken delivery. Therefore, based on the interpretation of the CAP guidance by PMO Stryker and DCMA officials, the Army will never take delivery of the Stryker inventory, assign the inventory a value, record it in an appropriate Army property accountability system, and recognize the inventory on the Army’s financial statements.” Audit report, p. 13.

The report fails to tie this discussion to its interpretation of the business rules. However, reading this with its interpretation of the CAP business rules appears to suggest that the auditors do not believe the items in inventory are CAP because they are delivered in the performance of a service contract. If this is in fact the case, the report should say so and include the legal, regulatory authority as well as any facts supporting it. PMO Stryker believes that this is factually incorrect. The Army takes delivery of CAP items at the time it accepts performance of the services performed on the vehicles. This is consistent with the FAR definitions as well as all of the GP guidance. It is also the opinion expressed by the DoD CAP and Government property policy expert during the July 2012 meeting referenced on page 15 of the report.

If this is not the case and there is some other explanation for this discussion and finding, the report should explain how and why the parts being used to sustain Stryker vehicles is important in classifying the property. It should further be state the DoD CAP and Government property policy experts’ opinion on when delivery and acceptance of CAP items used in the performance of service contract (e.g., a repair/maintenance effort) takes place. It should further be required to explain the connection between this finding and the topic heading it falls under. Specifically, it should identify the DoD Guidance on CAP that PMO Stryker inappropriately applied with its supporting rationale for it.

Accordingly, due to the issues resulting from applying FAR 52.245-1 and other DoD guidance, PMO Stryker requests that the report be revised to provide sufficient facts to support its findings and conclusion. PMO Stryker further requests that the report cite to and consider FAR 52.245-1 in its analysis of the findings and conclusion regarding the Army’s treatment of the Stryker inventory. Ultimately, without a common understanding of the definitions and sufficient facts to support an analysis, it is difficult to formulate a meaningful response to the audit.

III. The audit report retroactively applies Government Property rules and regulations to an existing contract.

The Government property (GP) regulations, guidance, and policy (referred to collectively as “GP Rules”) have been in a virtual state of flux since long before the award of the Stryker CLS contract. In fact, as will be shown the vast majority of the GP Rules cited in the report as support for the various alleged failings of PMO Stryker officials did not come into existence until years after the Stryker CLS contract was awarded.

The delivery order for Stryker CLS was awarded on 21 December 2006. An examination of the various GP Rules referenced in the audit report will reveal that only two were in existence, at least in the form they are in today, at the time of contract award: (1) DoD Regulation 4140.1-R “DoD Supply Chain Materiel Management Regulation,” dated 23 May 2003;⁶ and, (2) Army Regulation 735-5, “Policies and Procedures for Property Accountability,” dated 28 February 2005. All of the other GP Rules were issued or reissued with significant revisions after the December 2006 contract award. The following lists the various GP Rules cited in the report, the effective dates of the Rule illustrates this point:

- June 2007 – FAR Subpart 45 was re-written to streamline and improve current policies and procedures, eliminate unnecessary burdens on contractors and Contracting Officers, incorporate more commercial business practices into the government property regulations, and conform GFP property management rules to their private sector counterparts. The rewrite consolidated several FAR clauses together including creation of a new FAR 52.245-1, Government Property.⁷ Audit Report pgs. 10, 15, and 29.
- 22 Dec 07 – USD AT&L joint memo re: “Military Equipment Valuation Contract Acquired Property Business Rule.” Audit Report pgs 11 and 12.
- May 09 -- DoD Financial Management Regulation (DoD FMR) 7000.14-R, Volume 4, “Accounting Policy and Procedures,” Chapter 4, adding definitions of approved acquisition objective, excess inventory, net realizable value, among revisions. Audit report pgs 16-19, 21-23, 29, and 49-50.
- 11 Jan 10 -- USD(AT&L) memorandum, “Contractor Acquired Property (CAP) Under Cost Reimbursement Contracts and Line Items,” (CAP Business Rules). Audit report pgs. (ii), 1, 8, 10, 12, and 15.

⁶ A reissuance of this regulation is currently under development. Further, DoDI 4140.01, “DoD Supply Chain Materiel Management Policy” was issued on 14 Dec 2011 providing supplemental policy guidance in this area.

⁷ For a comprehensive discussion of the regulatory history on Government property prior to the June 2007 rewrite of FAR Subpart 45 see <http://government-property.com/wp-content/uploads/2012/02/history-of-Contract-Property.pdf>; and, <http://www.npma.org/Archives/18-6%20Geetz.pdf>.

- 20 Jan 11 –Revisions to DFARS and DFARS PGI affecting Subpart 245, 245.1, 245.2, 245.4. Audit report pgs. 13-15, and 29.
- 18 May 11 - DFARS Procedures, Guidance, and Information 245.103-71 Transferring Government Property Accountability. (Not directly cited, but changes related to the DFARS PGI).
- 19 Aug 2011 – Revisions to DFARS Government Property (DFARS Case 2009-D008) revising DFARS part 245 to conform with changes to the Federal Acquisition Regulation. Affected subparts/sections: DFARS part 245; 245.107; 245.5; 245.6; 245.70; 245.71; 245.72; 245.73; Table of Contents, DFARS part 252; 252.245; PGI 245.6. Audit report pgs. 13-15.
- April 2012 – FAR 52.245-1 Government Property (Apr 2012). Audit p. 10, 15, and 29.

The DoD-IG relies on the above GP rules in support of the following finding, among others:

“While Stryker inventory consumed during the contract period of performance for the logistics services contract could possibly be considered CAP, the inventory identified in this report had accumulated over many contract years and different periods of performance and needed to be officially delivered and accepted by the Army and accounted for as Government property.” Audit report pgs. 8 and 10.

There is no reference or discussion in the report that the policies supporting this finding were not implemented during the fourth contract year of the contract. There is equally no discussion about the lack of guidance on the treatment of GP and CAP in existence at the time or how the property should have been treated based on the guidance at the time. There is no factual findings or analysis supporting the claim the inventory accumulated over many years and different periods of performance.

In fact, Table 1 on page 9 simply identifies the total value of the inventory as of January 2012. The Table does not even identify the amount of inventory that accumulated in each period of performance so it is of little or no value to the report.⁸ Appendix A of the report does indicate the auditors’ reviewed delivery orders 0019, 0169 and 0269, but there are no specific findings regarding the amount of inventory that accumulated under each order or findings related to periods of performance of each delivery order. Audit report pg. 31.

The audit report should further acknowledge and consider FAR 1.108(d)(3) in its findings and analysis. FAR 1.108(d)(3) grants contracting officers’ (PCOs’) the discretion to incorporate a change to acquisition regulation(s) to an existing contract only when appropriate consideration

⁸ The Table was developed prior to DoD-IG’s conceding that the inventory “could possibly be considered CAP” during the period of performance in which it is consumed. In other words, the Table was developed in support of the DoD-IG’s early finding that the inventory was never CAP. It, however, was not updated to reflect the changes in its findings.

is provided.⁹ In other words, absent specific policy direction mandating the inclusion of a change to a contract clause, a PCO is never required to incorporate contract clause (or policy) changes into existing contracts and does not even have the discretion without appropriate consideration.¹⁰ As such, a fair and objective analysis would consider FAR 1.108(d)(3) and the multitude of actions that were taken by PMO Stryker in response to the ongoing Rule changes.

A fair and objective analysis would take the GP Rules that were in place at the time of the award of the CLS contract as well as the actions that were taken in response to the evolving rules. Such an analysis will reveal that the PMO Stryker incorporated the appropriate Government Property clauses at the time of the award.¹¹ It will reveal that PMO Stryker properly classified the property that was procured by the contractor in the performance of the logistic's contract and held in inventory as CAP in accordance with the regulations. It will reveal the CLS contract included numerous CDRL reporting requirements providing PMO Stryker with the necessary and required oversight into the Government property in the possession of the contractor.¹² These reports include: parts receipt report (parts purchased including cost), repaired parts including cost, consumption, and on-hand inventory. A fair and objective review will reveal that following the FAR 45 re-write, PMO Stryker executed Modification P00039 to the Stryker Requirements contract to incorporate FAR 52.245-1 (June/2007). It will reveal that DoD Components were and still are not required to establish records and maintain accountability of CAP until delivery takes place.¹³ It will reveal that the requirement for delivery of CAP items not anticipated at the time of award and considered excess to the needs of the accountable contract and that is needed on follow-on contracts was not incorporated into DFARs PGI 245.402-70 until January 12, 2011, (i.e., the fourth year of the CLS contract). It will similarly reveal that the requirement to transfer excess property between delivery orders on the same contract was not incorporated into PGI 245.103-71 until May 18, 2011.

The retroactive application of these GP Rules to the Stryker CLS effort results in PMO Stryker and the Army being forced into answering for inappropriately applying guidance that did not even in existence at the time the related decisions were made. A fair and objective analysis requires that the audit report address and consider the GP Rules that were in place at the time of contract award. Alternatively, the report should expressly acknowledge that the GP Rules being

⁹ FAR 1.08(d)(3) applies to changes to DFARs and AFARs as there are not supplemental requirements in either regulation.

¹¹ The Stryker Requirements contract contained the following Government Property related clauses applicable to CLS delivery order: a) FAR 52.245-5, Government Property (Cost-Reimbursement, Time-and-Material, or Labor Hour Contracts) (Deviation, per DAR Tracking Number 99-00008, (3 July 1999); b) FAR 52.245-9 Use and Charges (Aug/2005); and c) DFAR 252.245-7001, Reports of Government Property (May/1994). FAR 52.245-5 was consolidated into FAR 52.245-1 as part of the FAR re-write. FAR 52.245-1 (June/2007) was incorporated into the contract by modification in July 2008.

¹² See for instance, DFAR 252.245-7001, Reports of Government Property (May/1994).

¹³ See [REDACTED], OUSD (AT&L) P&E Policy white paper, "Property in the Possession of a Contractor [PIPC]," which provides a concise and easily understandable description of the req'ts for accounting and financial treatment of CAP at http://www.acu.osd.mil/pepolicy/pdfs/reference_library/PIPC_Whitepaper.pdf and

applied were not promulgated at the time of contract award and address if PMO Stryker was complying with the GP Rules in place at the time.¹⁴

IV. Response on "Obsolete and Excess Stryker Inventory for High-Dollar Review Parts" (pages 23-28):

Part 1 – Thermal Imaging Module: This part represents \$57m of the \$72m (79%) the report identified as excess or obsolete. Since these parts became obsolete and unusable on the Stryker platform, PM-SBCT and GDLS have held onto the material to determine if the government could make any other use of them. Due to the high dollar value of the item and low storage cost, PM-SBCT made the decision to hold onto the parts until all avenues had been completely exhausted. After there was no success in identifying another source for the parts, PM-SBCT provided direction to GDLS to put this material through the disposal process.

Part 2-4 - Commander's Seat Assembly: These parts were made obsolete on the Stryker vehicles by an engineering change order. The material was retained in case there would be a need to go back to a non-blast attenuating seat. The majority of the seats have been disposed and the remaining will be worked through PM-SBCT's excess and obsolete inventory review process.

Part 5 – Ramp Manifold: This part is obsolete and is being worked through PM-SBCT's excess and obsolete inventory review process. The material on hand is a mix of parts bought for sustainment and parts reclaimed from retrofitting the vehicles to the new configuration.

Part 6 - Netting Material: These items were bought for a forecasted requirement from deployed vehicles that never materialized. GDLS estimated high consumption due to believing deployed units would require high replacement. Very few replacements items were actually consumed resulting in excess inventory. This item will be worked through PM-SBCT's excess and obsolete inventory review process.

Part 7 – Collapsing Sign Stand: This item is excess due to an incorrect Contractor engineering estimate that was made at the time of procurement. There are 176 of these per vehicle and the engineering estimate forecasted a higher demand rate. These will now be worked through PM-SBCT's excess and obsolete inventory review process.

Part 8 – Drive Assembly Elevation: This item was previously loaded onto the SBCT's Authorized Stockage List (ASL) as a high demand critical item. In 2010 it was removed from the ASL due to a low demand rate and the inventory was sent back to wholesale supply. These will be worked through PM-SBCT's excess and obsolete inventory review process.

¹⁴ As a minimum, the addition of language recognizing the GP Rules were evolving and were not in existence during much of the contract period.

Part 9 – Power Electronics Assembly: This item was initially considered a critical high demand part requiring a need to be placed into a Fly Away package (held for Contingency Operations). This item will be worked through PM-SBCT's excess and obsolete inventory review process.

Part 10 – Engine Container: Item will be worked through PM-SBCT's excess and obsolete inventory review process.

Part 11-16 – Driveline components: All 6 of these parts are used on the 3.5 driveline. When the Stryker Double V Hull (DVH) was fielded, it was fielded with a 5.5 driveline. Since DVHs are the primary Stryker vehicle used during deployment, demand for non-DVH material saw a significant decrease. The parts referenced in the report are still used on Strykers with a 3.5 driveline, but the demand is expected to be significantly less in the future. Therefore, these parts will be worked through PM-SBCT's excess and obsolete inventory review process.

Recommendation 2: Recommend that the Program Executive Officer, Ground Combat Systems, require the Project Manager for the Stryker Brigade Combat Team, to:

- a. Accept delivery of all contractor-acquired property that was not consumed during the contract period of performance on a contract line item in accordance with Defense Federal Acquisition Regulation Supplement, Procedures, Guidance, and Information 245.402-70. Additionally, all Stryker inventory identified in this report needs to be officially delivered and accepted as Government property before the award of the follow-on Stryker contractor logistics support contract scheduled in FY 2013.
- b. Require General Dynamics to accept responsibility and create and maintain appropriate accountability records in accordance with Federal Acquisition Regulation 52.245-1 for any inventory considered contractor-acquired property or the Project Management Office, Stryker Brigade Combat Team needs to accept delivery of the inventory at the Government-owned, contractor-operated warehouse as Government property.
- c. Develop procedures to properly value the Stryker inventory, as required by DoD Financial Management Regulation 7000.14-R, volume 4, chapter 4, or follow the best practices outlined in the Under Secretary of Defense for Acquisition, Technology, and Logistics and Under Secretary of Defense (Comptroller) memorandum, "Baseline Valuation and Certification for Department of Defense (DoD) Inventory and Operating Materials and Supplies," November 8, 2005.
- d. Perform a thorough review of the Stryker inventory, record the inventory in an Army property accountability system, and properly stratify the inventory as approved acquisition objective, economic retention stock, contingency retention stock, or potential reutilization stock, as required by DoD Regulation 4140.1-R and Army Regulation 735-5.

e. Establish a detailed transaction history for Stryker inventory that records anticipated receipts of inventory as material due-ins, material received, or material transferred out, as required by DoD Regulation 4140.1-R and Army Regulation 735-5.

f. Adhere to DoD Financial Management Regulation 7000.14-R, volume 4, chapter 4, and report the Stryker inventory on Army Financial Statements in the appropriate general ledger accounts to support the Army's goal of having auditable financial statements to comply with Public Law 111-84, section 1003.

g. Accept delivery of Stryker inventory as Government property and value the inventory in Logistics Modernization Program before parts are requisitioned and charged to the Stryker brigades.

h. Implement a comprehensive inventory management improvement plan that complies with the DoD comprehensive inventory management plan and addresses over forecasting, total asset visibility, excess inventory, economic retention requirements, and aggressive potential reutilization and disposal reviews to meet the intent of Public Law 111-84 section 328.

Program Executive Officer Ground Combat Systems Comments:

Recommendation 2.a. Concur in part. "Stryker inventory that is excess to the needs of the CLS contract will be handled in accordance with Defense Federal Acquisition Regulation Supplement, Procedures, Guidance, and Information 245.402-70." Due to the volume of material needing to be reviewed and because the inventory identified in this report was bought in support of contracts other than CLS, the acceptance of all material will not be completed prior to the award of the next CLS contract; targeted for December 2012. All material acceptances are targeted to be complete by 30 September 2013.

Recommendation 2 (b): Concur. PM SBCT's position is that GD will continue to maintain appropriate accountability records in compliance with FAR 52.245-1 Government Property. This process began with the first Stryker CLS contract in May of 2002 and will continue.

Recommendation 2 (c): Concur. Stryker inventory that is procured by the contractor in the performance of Stryker logistic contract is CAP. As such, the valuation, financial and accounting treatment shall be in accordance with DFARs PGI 245.402-70(4) and (5) .

Stryker inventory that is directly acquired by the Government and furnished to the contractor for the performance of the CLS contract shall be valued in accordance with DoD Financial Management Regulation 7000.14-R, volume 4, chapter 4.

On October 31, 2012,
the Deputy PEO
revised his response.
See page 82.

DFARs PGI 245.402-70(4) and (5) :

“(4) Individual contractor-acquired property items should be recorded in the contractor’s management system at the contractor’s original purchase cost or best estimate.

(5) Financial/accounting treatment shall be in accordance with DoD Financial Management Regulations, DoD 7000.14-R, volume 4, chapter 6.”

This was initiated on 1 Oct 2011. It is estimated that this will be completed by 01 March 2014.

Recommendation 2 (d): Concur. Under the CLS contract, inventory that is delivered to and accepted by the Government will be recorded, valued, and properly stratified in LMP. This began as of 1 Oct 2012.

Recommendation 2 (e): Concur. For inventory classified as CAP, the contractor is required to establish a detailed transaction history pursuant to FAR 52.245-1 and DFAR PGI subpart 245. PMO Stryker will continue to maintain a detailed transaction history for all property in the Government's possession in accordance with the existing guidance.

Recommendation 2(f): Concur. Stryker inventory that was received under completed CLS contract delivery orders that has been accepted will be properly reported in the Army’s financial statements by using the LMP system. In accordance with policies and guidance, Stryker inventory considered CAP will not be reported in the Army’s financial statements. This process has begun as 1 Oct 2011 and will be completed by 01 March 2014.

Recommendation 2(g): Concur in part. Stryker parts have been requisitioned through the Army supply system since October 2011. Stryker Brigades have been charged for the material they order. After Stryker CLS material bought under previous contract periods of performance is accepted in March 2014, that material will be valued in LMP before being requisitioned and charged to the Stryker Brigades. Therefore, PMO Stryker non concurs with the timeline for implementation of this recommendation. There will be a transition period before full acceptance and valuation where requisitioning will occur so as not to impact the readiness of Stryker vehicles. The accepting and valuing of all inventory in LMP is targeted to be complete by 01 March 2014.

Recommendation 2(h): Concur. PMO Stryker has already complied with this recommendation by incorporating the following inventory performance metrics into the contract as of 1 October 2011: Requisition Fill Time; Inventory Turns; Inventory Accuracy; and First Pass Stock Availability. These metrics are currently being tracked and reported by GD, and the USG is auditing the performance of those metrics against the contractually required performance standards. PMO Stryker also intends to implement an incentive arrangement in the follow-on contract, which will incentivize both cost reduction, and performance against the established metrics. In terms of excess stock and disposal, PM SBCT reviews all GD requests for disposition instructions, and provides instructions that comply with FAR 45 and 52.245, DFARs 245, DoD 4160.21-M-1, and DCMA Plant Clearance Instructions.

Recommendation 3: Recommend that the Program Executive Officer, Ground Combat Systems, develop performance standards for or Project Management Office, Stryker Brigade Combat Team personnel that address proper accountability and financial controls over all Government property.

Program Executive Officer Ground Combat Systems Comments:

Recommendation 3. Concur. The Program Executive Officer, Ground Combat Systems, has in place performance standards for the Project Management Office, Stryker Brigade combat Team personnel that address proper accountability and financial controls over all Government property.

Recommendation 5: Recommend that the Program Executive Officer, Ground Combat Systems, require the Project Manager for the Stryker Brigade Combat Team.

a. Perform a thorough review of all Stryker spare part inventory and take appropriate action to dispose of obsolete parts.

b. Perform a thorough review of excess Stryker inventory and determine whether the parts can be used to meet other related Stryker requirements and ensure any material buy-back provisions do not provide a disincentive for the contractor to fully use the excess inventory.

Program Executive Officer Ground Combat Systems Comments:

Recommendation 5 (a): Concur. CLS contract language has been updated, as of 01 March 2012, to require the contractor to perform proper inventory management and specifically manage excess inventory.

Recommendation 5 (b): Concur. "PMO Stryker is continuously analyzing worldwide requirements for potential uses of excess property". The CLS contract language has been updated as of 1 March 2012 to require the contract to perform proper inventory management and specifically manage excess inventory. A CDRL was added requiring the contractor to regularly report excess and obsolete inventory to the government for disposition. Using this scope language and the CDRL, PM SBCT has formalized an excess and obsolete inventory review process for parts managed by the contractor under the CLS contract. This process began in May 2012 and has resulted in almost \$5m unusable inventory disposals to date. Each time the excess and obsolete inventory reports are provided to PM SBCT for review, PM SBCT will analyze worldwide requirements for use outside of the CLS contract. If requirements exist for Stryker or other government programs, the parts could be provided as GFM instead of being disposed.

Report Appendix F. Summary of Potential Monetary Benefits:

Type of Benefit: Economy and Efficiency. Reduces costs for future requirements by using current inventory to meet demand.

On October 31, 2012, the Deputy PEO revised his response. See page 82.

Amount of Benefit: \$1.1 million of funds put to better use by reusing existing engine containers instead of purchasing new engine containers.

Account: Army Working Capital Fund – 97X4930.001

Program Executive Officer Ground Combat Systems Comments to Potential Monetary Benefits:

The Program Executive Officer Ground Combat Systems agrees that the potential monetary benefits reported are reasonable given the assumptions made and the processes followed.



DEPARTMENT OF THE ARMY
PROGRAM EXECUTIVE OFFICE
GROUND COMBAT SYSTEMS
6501 E. ELEVEN MILE ROAD
WARREN, MICHIGAN 48397-5000

REPLY TO

AMSTA-CSC-J

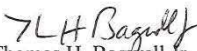
31 October 2012

MEMORANDUM FOR Director of Pricing and Logistics Acquisition – Acquisition and Contract Management, Department of Defense Office of the Inspector General, 4800 Mark Center Drive, Alexandria, Virginia 22302-1500

SUBJECT: Draft Report: Accountability Was Missing for Government Property Procured on the Army's Services Contract for Logistics Support of Stryker Vehicles (Project No: D2011-D000CH-0032.001)

1. Reference:
 - (a) Memorandum, DODIG, dated 17 September 2012, subject as above.
 - (b) Memorandum, PEO GCS, dated 17 October 2012 subject as above.
 - (c) Meeting, 30 October 2012 between DODIG and PMO Stryker Brigade Combat Team.
2. On 30 October 2012 at referenced meeting DODIG requested that the responses submitted to recommendations 2.b., 2.e., and 5.b. be reviewed.
3. We have reviewed the identified responses to subject DODIG Draft Report and submit clarification to responses 2.b. and 5.b.; our response to 2.e. remains unchanged. Our specific comments are contained in the enclosed reply.
4. The TACOM Internal Review and Audit Compliance Office will track that status of the corrective actions through completion and perform a follow-up review to verify implementation.
5. Point of contact for this reply is [REDACTED]

Encl


Thomas H. Bagwell Jr., SES
Deputy Program Executive Officer
Ground Combat Systems

Recommendation 2: Recommend that the Program Executive Officer, Ground Combat Systems, require the Project Manager for the Stryker Brigade Combat Team, to:

b. Require General Dynamics to accept responsibility and create and maintain appropriate accountability records in accordance with Federal Acquisition Regulation 52.245-1 for any inventory considered contractor-acquired property or the Project Management Office, Stryker Brigade Combat Team needs to accept delivery of the inventory at the Government-owned, contractor-operated warehouse as Government property.

Program Executive Officer Ground Combat Systems Revised Comments:

Recommendation 2 (b): Concur. PM SBCT's position is that GD will continue to maintain appropriate accountability records in compliance with FAR 52.245-1 Government Property. This process began with the first Stryker CLS contract in May of 2002 and will continue. Furthermore, PMO SBCT is reminding GDLS (via a PCO letter to be issued NLT 10 Nov 2012) of their contract requirements to create and maintain accountability records for inventory. PM SBCT will perform surveillance, IAW the contract surveillance plan, of GDLS's adherence to these contract requirements.

Recommendation 5: Recommend that the Program Executive Officer, Ground Combat Systems, require the Project Manager for the Stryker Brigade Combat Team.

b. Perform a thorough review of excess Stryker inventory and determine whether the parts can be used to meet other related Stryker requirements and ensure any material buy-back provisions do not provide a disincentive for the contractor to fully use the excess inventory.

Program Executive Officer Ground Combat Systems Revised Comments:

Recommendation 5 (b): Concur. "PMO Stryker is continuously analyzing worldwide requirements for potential uses of excess property. Further, as noted in response to recommendation 5(a), PMO Stryker has added a CDRL requirement and instituted a formal process". CLS contract language has been updated to require the contractor to perform proper inventory management and specifically manage excess inventory. In addition, a new CDRL was added requiring the contractor to regularly report excess and obsolete inventory to the government for disposition. Using this scope language and the CDRL, PM SBCT has formalized an excess and obsolete inventory review process for parts managed by the contractor under the CLS contract. This process began in May 2012 and has resulted in almost \$5m unusable inventory disposals to date. Each time the excess and obsolete inventory reports are provided to PM SBCT for review, PM SBCT will always analyze worldwide requirements for use outside of the CLS contract. If requirements exist for non-CLS Stryker or other government requirements, the excess parts identified will be provided as GFM instead of being disposed. In addition, the FY13 CLS contract (to be awarded by 31 Dec 2012) will incentivize the contractor to increase inventory turns to fully utilize all excess inventory so the contractor will not be discouraged to buy back that material in support of non-CLS requirements.



Inspector General Department of Defense

