



ACQUISITION,
TECHNOLOGY
AND LOGISTICS

OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000

SEP -9 2009

MEMORANDUM FOR COMMANDER, UNITED STATES SOUTHERN COMMAND
(ATTN: ACQUISITION EXECUTIVE)
COMMANDER, UNITED STATES TRANSPORTATION
COMMAND (ATTN: ACQUISITION EXECUTIVE)
DEPUTY ASSISTANT SECRETARY OF THE ARMY
(PROCUREMENT), ASA (ALT)
DEPUTY ASSISTANT SECRETARY OF THE NAVY
(ACQUISITION & LOGISTICS MANAGEMENT),
ASN (RDA)
DEPUTY ASSISTANT SECRETARY OF THE AIR FORCE
(CONTRACTING), SAF/AQC
DIRECTORS, DEFENSE AGENCIES
DIRECTORS, DOD FIELD ACTIVITIES

SUBJECT: Follow-on Actions in Response to OIG Report Notification: "Effect of Payments into Boeing Pension Funds on Economic Price Adjustment Clauses in DoD Contracts" (Project No. D2006-D000CH-0226.000)

The purpose of this memorandum is to reiterate the need to use caution when incorporating Economic Price Adjustment (EPA) provisions in contracts. As stated in PGI 216.203-4, EPA provisions can result in significant and unanticipated price increases which can have major adverse impacts to a program.

The situation described in the subject audit underscores the importance of ensuring EPA clauses are properly structured and carefully monitored after contract award. The Department of Defense Inspector General (DoDIG) found that Boeing's pension contributions between 2003 and 2005 disproportionately influenced the Bureau of Labor Statistics (BLS) index (ECI 3721) used in the EPA clauses of the Air Force C-17 Globemaster III, the Navy F/A-18 E/F Super Hornet, and the Army AH-64D Apache Longbow contracts. This situation only became apparent after contract award.

The basis of a BLS index, per DFARS PGI 216.203-4(6), should not be so large and diverse that it is significantly affected by fluctuations not relevant to contract performance, but it must be broad enough to minimize the effect of any single contractor. In addition, care should be exercised in those cases that deal with volatile commodities that have only a limited number of sources of supply. In these cases it may be appropriate to consider an alternative methodology, such as one based on published

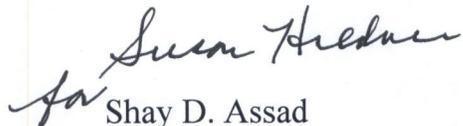
market prices. DoD contracting officers shall use caution when incorporating economic price adjustment provisions in contracts.

Since the ECI 3721 index failed both of the PGI tests, the DoDIG determined that use of this BLS index constituted a material internal control weakness (as defined by DoD Instruction 5010.40, "Managers Internal Control (MIC) Program Procedures," January 4, 2006). As a result of the audit recommendations, PGI 216.203-4 was revised to prohibit the BLS employment cost index for total compensation, aircraft manufacturing (NAICS Product Code 336411, formerly Standard Industrial Classification Code 3721, Aircraft) in any EPA clause in DoD contracts.

It is the policy of the Department that Multi-Year (MY) contracts with EPA clauses will be monitored to ensure that economic price adjustments are the result of normal economic behavior as intended by the clause. Accordingly, the Components are responsible for establishing local policies and procedures for reviewing and monitoring MY contracts with EPA clauses.

To ensure continued visibility, Components must also submit an annual report of Contract Data for MY contracts with EPA clauses in the attached format. The initial report of FY 2009 data is due October 30, 2009.

My point of contact for this memorandum is Mr. David Mabee and he can be reached at 703-602-0326 or via e-mail at Dave.Mabee@osd.mil.



Shay D. Assad
Director, Defense Procurement
and Acquisition Policy

Attachment:
As stated

cc:
DCAA

DPAP Multiyear Contract Data Submission (revised FY2009)

	1	2	3
Contract Number	_____	_____	_____
Organization	_____	_____	_____
POC Name	_____	_____	_____
POC Number	_____	_____	_____
Program	_____	_____	_____
Contractor	_____	_____	_____
Contract Type	_____	_____	_____
Performance Period (Mo/Yr to Mo/Yr)	_____	_____	_____
Total Contract Price at Award	_____	_____	_____
Quantity at Time of Award	_____	_____	_____
“Current” as of date for below	_____	_____	_____
Current Total Contract Price	_____	_____	_____
Current (Revised) Quantity	_____	_____	_____
Current Incurred Costs	_____	_____	_____
Initial Projected Savings Amount to justify multiyear	_____	_____	_____
Initial Projected Savings Percentage to justify multiyear	_____	_____	_____
Negotiated Profit Rate	_____	_____	_____
Has EPA Index? (Note 1)	_____	_____	_____
EPA Index used (Note 2)	_____	_____	_____
Source of EPA Index (Note 3)	_____	_____	_____
EPA Adjustment Year 1	_____	_____	_____
EPA Adjustment Year 2	_____	_____	_____
EPA Adjustment Year 3	_____	_____	_____
EPA Adjustment Year 4	_____	_____	_____
EPA Adjustment Year 5	_____	_____	_____
Comments (if any)	_____	_____	_____

Please do not insert additional rows above the comment line

Notes:

- (1) Answer Y or N
- (2) If there is an index, state title, otherwise leave blank
- (3) State the source or publisher of the index, e.g., BLS, EIA, Global Insights, etc.