

# Inspector General

United States  
Department of Defense



The Army's Procurement and Conditional  
Acceptance of Medium Tactical Vehicles

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### **Acronyms**

DCMA	Defense Contract Management Agency
FAR	Federal Acquisition Regulation
FMTV	Family of Medium Tactical Vehicles
LMTV	Light-Medium Tactical Vehicles
MTV	Medium Tactical Vehicles



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202-4704

December 21, 2007

MEMORANDUM FOR AUDITOR GENERAL, DEPARTMENT OF THE ARMY  
DIRECTOR, DEFENSE CONTRACT MANAGEMENT  
AGENCY

SUBJECT: Report on the Army's Procurement and Conditional Acceptance of Medium  
Tactical Vehicles (Report No. D-2008-038)

We are providing this report for review and comment. In preparing the final report, we considered comments on the draft report from the Deputy Program Executive Officer for Combat Support and Combat Service Support; the Deputy Chief of Staff, TACOM Life Cycle Management Command; and the Acting Director, Defense Contract Management Agency.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The Deputy Program Executive Officer for Combat Support and Combat Service Support comments were partially responsive. Accordingly, we request that the Program Executive Officer for Combat Support and Combat Service Support provide additional comments on Recommendation B.1. by January 22, 2008.

If possible, please send management comments in electronic format (Adobe Acrobat file only) to [AudACM@dodig.mil](mailto:AudACM@dodig.mil). Copies of the management comments must contain the actual signature of the authorizing official. We cannot accept the / Signed / symbol in place of the actual signature. If you arrange to send classified comments electronically, they must be sent over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Questions should be directed to Mr. John E. Meling at (703) 604-9091 (DSN 664-9091) or Mr. Kevin W. Klein at (703) 604-9032 (DSN 664-9032). See Appendix D for the report distribution. The team members are listed inside the back cover.

By direction of the Deputy Inspector General for Auditing:

A handwritten signature in cursive script, reading "Bruce A. Burton".

Bruce A. Burton  
Deputy Assistant Inspector General  
Acquisition and Contract Management



(Project No. D2006-D000AE-0225.000)

## The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles

### Executive Summary

**Who Should Read This Report and Why?** Contracting officers and contract administrators should read this report because it discusses the Army's practices for conditional acceptance and first inspection acceptance of the vehicles.

**Background.** The Family of Medium Tactical Vehicles (FMTV) consists of families of Light-Medium Tactical Vehicles, which are 2½-ton trucks, and Medium Tactical Vehicles, which are 5-ton trucks. The FMTV includes complementary trailers that supplement the vehicle fleet. The vehicles have common components and various body styles for special combat, combat support, and combat service support organizational missions. The approved Presidential Budget for FYs 2005 and 2006 provided approximately \$956 million to procure 7,071 FMTVs. In addition, Congress provided another \$797 million to the program as part of the Emergency Supplemental Appropriations Acts in FYs 2005 and 2006. The supplemental budgets for FYs 2005 and 2006 provided funding to procure an additional 3,970 FMTVs.

**Results.** The Army was appropriately using supplemental funds that Congress provided to the FMTV program office in support of the Global War on Terrorism. However, the FMTV program office was not adequately protecting the Government's interest because it conditionally accepted FMTVs. Further, the FMTV contractor, Stewart and Stevenson Tactical Vehicle Systems, Limited Partnership, was not meeting contract requirements for acceptance of vehicles at first Government inspection. The following two findings discuss those issues.

- As was the case more than 11 years ago, the procuring contracting officer for the FMTV, after consulting with the Project Manager Tactical Vehicles, authorized the administrative contracting officer to conditionally accept incomplete vehicles and paid the contractor up to 100 percent of the contract price for some of the vehicles. The conditional acceptance of vehicles resulted in the Army prematurely paying the FMTV contractor more than \$3.8 million for vehicles. The conditional acceptance of vehicles also unnecessarily increased the Army cost risk. When authorizing the conditional acceptance of vehicles, the procuring contracting officer should limit payment to the contractor as stated in the contract to protect the Government's interest. The procuring contracting officer should also limit vehicle conditional acceptance to reasons of economy and urgency when those conditions exist (finding A). (This is a repeat finding that was discussed in DoD Inspector General Report No. 96-005, "Quick-Reaction Audit Report on Conditional Acceptance of Medium Tactical Vehicles," October 12, 1995.)
- The FMTV contractor submitted vehicles for Government acceptance that did not meet first inspection acceptance requirements in the contract.

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Specifically, Government acceptance of FMTV lots at first inspection decreased from 86 percent in January 2004 to 21 percent in January 2007. As a result, the Defense Contract Management Agency (DCMA) incurred additional reinspection costs to verify that vehicles resubmitted for inspection met contract specifications. The Director, Defense Contract Management Agency needs to continue charging the contractor for Government reinspection costs, as he began to do during the audit. Also, the Program Executive Officer for Combat Support and Combat Service Support should slow the contractor's daily vehicle production rate until the contractor can meet vehicle first acceptance inspection requirements in the contract (finding B).

The Army's internal controls for the FMTV contract were not adequate. We identified material control weaknesses in the process used by the procuring contracting officer to conditionally accept incomplete vehicles and pay the contractor up to 100 percent of the contract price for some of the vehicles.

**Management Comments and Audit Response.** The Deputy Chief of Staff, TACOM Life Cycle Management Command concurred with the recommendations to limit payment to the contractor as required in the contract to protect the Government's interest and limit vehicle conditional acceptance to reasons of economy and urgency when those conditions exist. The Deputy Chief of Staff planned to implement the recommendations by September 30, 2007. The comments were responsive and no further comments are needed.

The Deputy Program Executive Officer for Combat Support and Combat Service Support, responding for the Program Executive Officer for Combat Support and Combat Service Support, nonconcurred with the recommendation to slow the contractor's daily vehicle production rate until the contractor can meet vehicle first acceptance inspection requirements in the contract. The Deputy stated that the first pass yield is one of many internal metrics used by DCMA Sealy to assist them in ensuring that the quality of the trucks presented to the Government for acceptance is maintained. He stated that the contractor continues to meet its monthly and yearly contractual truck delivery requirements to the Government. Additionally, the Deputy stated that vehicles produced and fielded are meeting or exceeding user requirements as evidenced by FMTV's operational readiness rate of over 93.5 percent. He stated that decreasing FMTV production would not be in the best interest of our Army or its soldiers, and any delay in fielding those vehicles will directly and unnecessarily place soldiers at risk. The Deputy Program Executive Officer's comments did not address the issue of the contractor not being able to provide vehicles for inspection that meet contract requirements. DCMA has issued over 285 corrective action requests based on contractor quality issues. Further, while contractor monthly deliveries have met total vehicle quantities, the contractor did not deliver the vehicle variant quantities prescribed in the contract. Instead, the procuring contracting officer allowed the contractor to substitute different FMTV variants to meet overall monthly quantity requirements. Temporarily decreasing daily vehicle production requirements would provide the contractor an opportunity and incentive to correct production problems and increase its capability to present vehicles that conform to contract specifications at first inspection and enable the Army to immediately ship vehicles to the Army units. According to the Deputy Chief of Staff, G-8, only 445, or 10 percent, of the 4,354 vehicles scheduled to be

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delivered by September 2008 are going to Southwest Asia. Therefore, temporarily reducing the daily production rate should not affect deliveries to Southwest Asia because even with reduced daily vehicle production requirements, the FMTV contractor will be able to timely produce the 445 vehicles planned for shipment to Southwest Asia. The Army plans to use the remaining vehicles to support the Army's modularity program and backfill for vehicles already shipped to Southwest Asia.

The Acting Director, Defense Contract Management Agency partially concurred with the recommendation to continue charging the contractor for Government reinspection costs, stating that billing for reinspection costs is an option under Federal Acquisition Regulation 52.246-2. The Acting Director stated that DCMA plans to continue charging reinspection costs until the contractor's first pass yield rate exceeds 80 percent. The Acting Director's comments meet the intent of the recommendation and no further comments are needed. (See the Finding section of the report for a discussion of the management comments and the Management Comments section of the report for the complete text of the comments.)

We request that the Program Executive Officer for Combat Support and Combat Service Support reconsider his position on the recommendation and comment on the final report by January 22, 2008.



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Source: Army Evaluation Center Continuous Improvement Briefing

**Family of Medium Tactical Vehicles Cargo Variant**

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## Background

This report is the first of two reports on the overall management of the Family of Medium Tactical Vehicles (FMTV). This report addresses the conditional acceptance and the first inspection acceptance of FMTVs. The second report will address armor requirements for the FMTV program. The FMTV is a family of vehicles that operates throughout the theater as multipurpose transportation vehicles for combat, combat support, and combat service support units. The vehicles operate worldwide on primary and secondary roads, trails, and cross-country terrains.

The FMTV program is a major Defense acquisition program that comes under the management oversight of the Program Executive Officer for Combat Support and Combat Service Support at the TACOM Life Cycle Management Command.<sup>1</sup> The Program Executive Officer's mission is to develop, acquire, field, and sustain the soldier and ground systems for the warfighter by integrating effective and timely acquisition, logistics, and cutting-edge technology. The Project Manager Tactical Vehicles is responsible for managing the FMTV program and reports to the Program Executive Officer. The Director, TACOM Life Cycle Management Command Acquisition Center is responsible for acquisition support and contracting, and oversees the procuring contracting officers. The Army Acquisition Executive is the milestone decision authority for the program. Research, development, test, and evaluation and procurement funds for the FMTV program total approximately \$21 billion to acquire 83,185 vehicles by FY 2022. The program entered the production phase of the acquisition process in 1995.

**FMTV Variants.** The FMTV program consists of Light-Medium Tactical Vehicles (LMTV), which are 2½-ton trucks, and Medium Tactical Vehicles (MTV), which are 5-ton trucks. The FMTV program also includes complementary trailers that supplement the vehicle fleet. The vehicles have component commonality and various body styles for special combat, combat support, and combat service support organizational missions. The LMTV and MTV families consist of vehicle variants for the following capabilities.

- Cargo. The cargo truck performs local and line-haul missions and troop transport for LMTV and MTV variants.
- Van. The van is a shop van mounted on the LMTV chassis. The Army has also developed an MTV expansible van.

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<sup>1</sup> Referred to in previous DoD Inspector General reports as the Tank-automotive and Armaments Command.

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- **Tractor.** The truck tractor performs line-haul missions and is compatible with all semi-trailers that the M931 and M932 truck tractors<sup>2</sup> tow.
  - **Dump.** The dump truck is mounted on the MTV chassis for the mission of hauling and dumping up to 5 cubic yards of material in support of engineer units. The Army is developing a 10-ton dump truck.
  - **Load Handling System.** The load handling system is mounted on the MTV chassis and is capable of self-load and off-load.
  - **Wrecker.** The MTV wrecker truck is capable of multipurpose operations by a single operator using a hydraulic crane and winch. Operations include recovery, removal, and installation of power packs; lift and towing; and material handling.
  - **Cargo Trailers.** The cargo trailers have the same payload capacity as the companion truck.

**Procurement History of FMTV.** In October 1991, the Army milestone decision authority authorized the Project Manager Tactical Vehicles to award Stewart and Stevenson Tactical Vehicle Systems, Limited Partnership<sup>3</sup> a 5-year production contract to produce 11,197 FMTVs for \$1.4 billion. The milestone decision authority authorized full-rate production in August 1995, and, according to the program office, the October 1991 contract was restructured to cover the fifth year of vehicle production with FY 1996, 1997, and 1998 funding. In July 1997, the Army also issued a separate, negotiated requirements contract for 148 vehicles for U.S. and foreign military sales customers. In June 1998, the Army issued an additional contract worth \$9.2 million for test vehicles. In October 1998, the Army noncompetitively awarded the contractor a 4-year production contract to produce approximately 5,390 trucks and 1,040 trailers for \$2.1 billion and an option for the Army to purchase an additional 5,800 trucks or trailers in a fifth production year.

In FY 2001, the Army competed the follow-on procurement of medium tactical vehicles, and Stewart and Stevenson Tactical Vehicle Systems, Limited Partnership won the competition. In April 2003, the Army awarded the contractor a 5-year, \$4.1 billion production contract for 11,011 trucks and trailers. The contract also included an option for the Army to purchase an additional 9,439 trucks or trailers. The approved Presidential Budget for FYs 2005 and 2006 provided approximately \$956 million in funds to procure 7,071 trucks. Further, in 2006, the FMTV program office received a military interdepartmental purchase request from the Army National Guard Readiness Center for \$315 million to procure 2,358 vehicles on the same production contract.

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<sup>2</sup> The M931 and M932 are the predecessor tractor vehicles to the FMTV tractor vehicle.

<sup>3</sup> Although on July 31, 2007, BAE Systems bought out Armor Holdings, Inc., which bought Stewart and Stevenson Services, Inc., on May 25, 2006, this report will refer to the contractor as Stewart and Stevenson Tactical Vehicle Systems, Limited Partnership.

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**FMTV Supplemental Funding.** In the FYs 2005 and 2006 Emergency Supplemental Appropriations Acts, Congress provided the FMTV program office with an additional \$797 million to procure 3,970 FMTVs for the replacement of vehicles lost in waging the Global War on Terrorism and for Army modularity program requirements. The procuring contracting officer modified the April 2003 contract to procure the 3,970 FMTVs.

**Army Modularity's Program.** The Army's modularity program reorganizes and maximizes force effectiveness by structuring into a brigade-based force with three primary goals.

- Increase the number of available brigade combat teams to meet operational commitments while maintaining combat effectiveness that is equal to or better than that of current divisional brigade combat teams.
- Create combat and support formations of common organizational designs that can be tailored to meet the varied demands of the regional combatant commanders, thereby reducing joint planning and execution complexities.
- Redesign brigades to perform as integral parts of the Joint Force to make them more capable across the range of military operations and able to benefit from support from other services and contribute more to other service partners.

**Use of Global War on Terrorism Emergency Supplemental Funds.** As authorized, the Army used emergency supplemental funding that Congress provided to support the Global War on Terrorism. The Army used the funding for the FMTV program in FYs 2005 and 2006 to procure additional vehicles to backfill for medium tactical vehicles that Army units deployed to Southwest Asia. The backfill of vehicles in the Continental United States allowed returning Army units to train for their next mission or deployment. The Army has deployed 12,310 medium tactical vehicles to Southwest Asia and the Horn of Africa. Through emergency supplemental funding, the Army has contracted to procure an additional 10,025 FMTVs to replace the vehicles that may be left in theater. According to a representative of the Army's Deputy Chief of Staff, G-8, the Army will either bring some, all, or none of the vehicles back to the United States. The representative stated that if the Army leaves any vehicles in theater, the Army would either give or sell those vehicles to the Iraqi or Afghan Governments.

## Objectives

The primary audit objective was to determine whether the Army was adequately protecting the Army's interest when using the conditional acceptance provision in production contracts for the FMTV program. In addition, we determined whether the Army was appropriately using the

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supplemental funds that Congress provided to the FMTV program office in support of the Global War on Terrorism.

## Review of Internal Controls

**FMTV Internal Control Weaknesses.** The Army's internal controls for the FMTV contract were not adequate. We identified material internal control weaknesses in the application of internal controls as defined by DoD Instruction 5010.40, "Managers' Internal Control (MIC) Program Procedures," January 4, 2006, associated with the FMTV program and the administration of its current contract, DAAE07-03-C-S023. Although the internal controls outlined in the DoD 5000 series of guidance and the Federal Acquisition Regulation were adequate for controlling the program, Army acquisition officials did not follow those controls. Specifically, the FMTV administrative contracting officer did not adhere to contract provisions when:

- conditionally accepting vehicles that had not completed required first article testing; and
- paying the contractor up to 100 percent of the contract price for conditionally accepted vehicles that were authorized by the procuring contracting officer or authorized by the contract terms.

Further, the Defense Contract Management Agency (DCMA) administrative contracting officer did not begin charging the contractor until December 29, 2006, for reinspection costs when the contractor failed to noticeably improve the acceptance rate for vehicle lot inspections. The DoD 5000 series of guidance states that the primary objective of Defense acquisition is to acquire quality products that satisfy user needs in a timely manner at a fair and reasonable price. By implementing the recommendations in this report, the Army will be better equipped to meet the objective of the Defense Acquisition System. We will provide a copy of this report to the senior officials responsible for internal controls in the Department of the Army and in DCMA.

**FMTV Prior Coverage Internal Control Weaknesses.** DoD Inspector General Report No. 96-005, "Quick-Reaction Audit Report on Conditional Acceptance of Medium Tactical Vehicles," October 12, 1995, stated that the Army contracting officer had used a conditional acceptance clause in the contract with the FMTV program because the program manager believed that there was a need to have vehicles available for deployment. In addition, the program manager believed that conditionally accepting vehicles would smooth out the workload of accepting and fielding vehicles, and that refusal to accept vehicles would create a perception that the Army was being punitive over trivial issues. The auditors did not find a validated need for deploying vehicles. Further, the auditors found that incomplete vehicles were being conditionally accepted, causing the need for extensive retrofitting at additional expense. Conditionally accepted vehicles remained at the contractor's facility without being completed, retrofitted, or used for as long as 2 years. Finally, the auditors found that design changes made the FMTV design unsupportable because of replacement of spare parts and extensive

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rework. The additional inspections and rework did not smooth out the workload; rather, they increased the level of work. The audit report concluded that the Army prematurely paid the contractor \$7.1 million for vehicles the Army could not immediately use.

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## A. Conditional Acceptance of Family of Medium Tactical Vehicles

As was the case more than 11 years ago, the procuring contracting officer for the FMTV, after consulting with the Project Manager Tactical Vehicles, authorized the administrative contracting officer to conditionally accept incomplete vehicles and the administrative contracting officer paid the contractor up to 100 percent of the contract price for some of the vehicles. From January 30, 2004, through January 31, 2007, the procuring contracting officer approved 32 contractor requests and inappropriately conditionally accepted 1,745 FMTVs. This condition occurred because the Project Manager Tactical Vehicles believed that the conditional acceptance allowed a more efficient production and acceptance process. The project manager also believed these practices were in the best interest of the Army even though they were not in accordance with the contract terms and the Federal Acquisition Regulation. The conditional acceptance of vehicles resulted in the Army prematurely paying more than \$3.8 million for vehicles. The conditional acceptance of vehicles also unnecessarily increased the Army cost risk. (This is a repeat finding that was discussed in DoD Inspector General Report No. 96-005, "Quick-Reaction Audit Report on Conditional Acceptance of Medium Tactical Vehicles," October 12, 1995.)

### Policy for Conditional Acceptance

Federal Acquisition Regulation (FAR) Part 46, "Quality Assurance," provides guidance for conditionally accepting vehicles that do not conform to contract specifications.

**FAR 46.101.** FAR 46.101, "Definitions," defines conditional acceptance as acceptance of supplies or services that do not conform to contract quality requirements, or are otherwise incomplete. The contractor is required to correct or otherwise complete the supplies or services by a specified date.

**FAR 46.407.** FAR 46.407, "Nonconforming Supplies or Service," states that the contracting officer should reject supplies or services not conforming in all respects to contract requirements except when the contracting officer determines acceptance or conditional acceptance, for reasons of economy or urgency, is in the best interest of the Government. This part of the FAR does not define economy or urgency; however, the dictionary defines "urgency" as calling for immediate attention and defines "economy" as thrifty and efficient use of material resources.

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FAR 46.407 states that the contracting officer makes the determination to conditionally accept items based on:

- advice of the technical activity that the item is safe to use and will perform its intended purpose;
- information regarding the nature and extent of the nonconformance;
- a request from the contractor for acceptance of the nonconforming or otherwise incomplete supplies or services;
- a recommendation for acceptance, conditional acceptance, or rejection, with supporting rationale; and
- a contract adjustment considered appropriate, including any adjustment offered by the contractor.

FAR 46.407 states that for a major nonconformance, the Government *must* withhold payment sufficient to cover the estimated cost and related profit to correct deficiencies and complete unfinished work. It states that the contracting officer should modify the contract to provide for an equitable price reduction, or other consideration, for a critical or major nonconformance.

Further, FAR 46.407 states that conditional acceptance withholdings should be at least sufficient to cover the estimated cost and related profit to correct deficiencies and complete unfinished work. It also states that the contracting officer must document in the contract file the basis for the amounts withheld.

Withholding funds discourages contractors from repeatedly providing nonconforming supplies or services, including those with only minor nonconformances. The contracting officer can take appropriate action, such as rejecting the supplies or services and documenting the contractor's performance record, to discourage poor performance from the contractor.

## **Contract Payment Terms**

The FMTV contract, contract DAAE07-03-C-S023 with Stewart and Stevenson Tactical Vehicle Systems, Limited Partnership, states that the contractor should receive, as performance-based payments, 80 percent of the vehicle price for successful completion of performance-based payment events defined in the contract. These events include ordering and receiving vendor confirmation of items needed to manufacture vehicles in support of the contract delivery schedule. The Government pays the remaining 20 percent of the vehicle price when the vehicle passes final inspection and acceptance. In addition, the contract provides terms for the Government, at its sole discretion, to conditionally accept vehicles. Specifically, the contract states that conditional acceptance before first article approval allows the

contractor to invoice up to 90 percent of the vehicle's base unit price. The Government may, based on contractor performance, increase the invoice percentage above the 90-percent limitation.

The contractor's performance has not justified exceeding the 90-percent limitation. (See finding B.)

## Conditional Acceptance of Vehicles

The procuring contracting officer accepted 32 contractor requests for the Army to conditionally accept 2,366 vehicles from January 30, 2004, through January 31, 2007, on contract DAAE07-03-C-S023. The procuring contracting officer authorized conditional acceptance of 1,745 of the 2,366 vehicles because the contractor had not met contract vehicle specifications. The procuring contracting officer authorized conditional acceptance of the remaining 621 vehicles because the Army had not provided Government-furnished items to the contractor. The following table shows the number of vehicles conditionally accepted in relation to the total number of vehicles accepted<sup>4</sup> under contract DAAE07-03-C-S023.

### Vehicles Accepted and Conditionally Accepted Under Contract DAAE07-03-C-S023

Fiscal Year	Total Vehicles Accepted at Contractor Submission <sup>1</sup>	Vehicles Conditionally Accepted	Vehicles Conditionally Accepted for Government Responsibility	Vehicles Conditionally Accepted for Contractor's Responsibility
2004	28	28	0	28
2005	2,887	653	201	452
2006	5,267	974	143	831
2007	<u>2,225</u>	<u>711</u>	<u>277</u>	<u>434</u>
<b>Total</b>	<b>10,407<sup>2</sup></b>	<b>2,366</b>	<b>621</b>	<b>1,745</b>

<sup>1</sup> The total of vehicles accepted includes both conditional and final vehicle acceptance.  
<sup>2</sup> Through January 31, 2007.

**Contractor Responsibility for Conditionally Accepted Vehicles.** As was the case more than 11 years ago, the procuring contracting officer for the FMTV, after consulting with the Project Manager Tactical Vehicles, authorized the administrative contracting officer to conditionally accept incomplete vehicles and the administrative contracting officer paid the contractor up to 100 percent of the contract price for the vehicles. From

<sup>4</sup> The total number of vehicles accepted includes FMTV trucks, trailers, and High Mobility Artillery Rocket System chassis.

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January 30, 2004, through January 31, 2007, the procuring contracting officer approved 13 contractor requests for the Army to conditionally accept 1,745 (74 percent) of the 2,366 vehicles for various contractor reasons. Of the 1,745 vehicles, 155 were conditionally accepted for more than one reason, totaling 1,900 reasons for conditional acceptance. In acting on the contractor requests, the procuring contracting officer directed the administrative contracting officer to conditionally accept 466 of the 1,745 vehicles with vehicle nonconformances but did not direct the administrative contracting officer to withhold payment, as required by the FAR, and the administrative contracting officer paid 100 percent of the vehicle price. The administrative contracting officer also conditionally accepted 190 of the 1,745 vehicles that had not completed testing requirements. According to the contract terms, the administrative contracting officer did not need authorization from the procuring contracting officer to conditionally accept those vehicles. However, the contract stated that the administrative contracting officer does need procuring contracting officer authorization to pay more than 90 percent of the vehicle price for those vehicles. The administrative contracting officer paid 100 percent of the vehicle price for those vehicles without authorization.

The administrative contracting officer conditionally accepted and paid full price for the 656 vehicles in response to the following contractor reasons for the Government to conditionally accept the vehicles:

- noncompletion of testing requirements (190 vehicles);
- request for a deviation of nonconforming contractor parts (14 vehicles);<sup>5</sup> and
- delivery schedule delays for the contractor to incorporate engineering change proposals (452 vehicles).

**Testing.** The administrative contracting officer approved and paid the contractor the full contract price for 190 conditionally accepted vehicles that had not completed first article tests, production verification tests, or component first article tests. The contract terms specify that conditional acceptance before first article approval allowed the contractor to invoice up to 90 percent of the vehicle's base unit price. The procuring contracting officer may allow the contractor to invoice more than the 90 percent based on the contractor's performance; however, the contractor's performance did not justify exceeding the 90-percent limitation.

**Nonconforming Parts.** By contract terms, the contractor is responsible for providing vehicles that conform to vehicle specifications. DCMA personnel found during final inspection that the contractor did not install the correct draglink part on 14 vehicles because the contractor had not ordered the correct draglink parts. As a result, the contractor requested a deviation for the draglink, which is a major nonconformance deviation, in a conditional acceptance letter for 22 vehicles. The procuring contracting

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<sup>5</sup> These 14 vehicles were also conditionally accepted for not completing test requirements.

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officer authorized the conditional acceptance of 14 vehicles and did not require the administrative contracting officer to withhold payments from the contractor for the correction of the nonconforming draglink.<sup>6</sup> As required in the FAR, the procuring contracting officer should have directed the administrative contracting officer to withhold payment from the contractor sufficient to cover the estimated cost and related profit of correcting this unacceptable condition.

**Delivery Schedule Delays for the Contractor to Incorporate Engineering Change Proposals.** The procuring contracting officer authorized conditional acceptance of 452 vehicles from December 2004 through April 2005 that were not ready for delivery as required by the contract schedule because the contractor had not, for 16 engineering change proposals incorporated in the contract, included those engineering changes in those vehicles. Subsequently, the contractor retrofitted the 452 conditionally accepted vehicles with requirements specified in the 16 engineering change proposals.

**Army Responsibility.** The procuring contracting officer conditionally accepted 621 (26 percent) of the 2,366 vehicles for reasons caused by the Army, including:

- the Army had not incorporated engineering change proposals in the contract; and
- the Army had not provided Government-furnished items, such as technical manuals, weight classification signs, and paint patterns.

In these cases, the procuring contracting officer had the authority to pay full vehicle price because the Government was responsible for the conditions that caused the conditional acceptance.

**Engineering Change Proposal Example.** The procuring contracting officer authorized conditional acceptance of six vehicles because the contractor had incorporated an agreed-on engineering change proposal for the expansible van vehicle platforms and chassis that had not yet been added to the contract through contract modification. The contracting officer stated that DCMA could not fully accept the six vehicles with the new engineering change because the Army had not added the engineering change to the contract through contract modification. The contracting officer properly paid the full vehicle price to the contractor because the conditional acceptance was Government-caused.

**Government-Furnished Item Examples.** The procuring contracting officer authorized conditional acceptance of the other vehicles because the Army had not provided Government-furnished items. The Army accepted 296 vehicles because of the lack of technical manuals, 233 vehicles because of a lack of weight classification signs, and 86 vehicles because of the lack of paint patterns. The Army was responsible for the delivery of these items. Because the Army had not provided these items, the administrative contracting officer conditionally accepted the vehicles. The administrative

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<sup>6</sup> The contractor used the correct draglink for the remaining eight vehicles.

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contracting officer had the authority to pay the full vehicle price to the contractor because the conditional acceptance was caused by the lack of Government action.

## **Reason for Conditionally Accepting Vehicles**

The Project Manager Tactical Vehicles (the Project Manager) stated that the Army should continue conditionally accepting vehicles from the contractor because conditional acceptance provided a more efficient production and acceptance process.

## **Audit Evaluation of Reason for Conditional Acceptance**

The Project Manager's reason for continuing to conditionally accept vehicle lots was not valid. The conditional acceptance of vehicle lots did not provide for a more efficient production and acceptance process.

**Efficient Production.** The Project Manager stated that the Army needed to continue conditionally accepting vehicle lots for more efficient production. However, conditionally accepting vehicle lots did not result in a more efficient production process and was not economical for the Government because:

- DCMA was required to reinspect vehicle lots until they passed inspection acceptance, which resulted in increased time and expense to the Government; and
- after conditional acceptance of vehicle lots, DCMA was required to oversee contractor changes made to the vehicles before reinspection for acceptance.

**Acceptance Process.** The Project Manager stated that the Army needed to continue conditionally accepting vehicle lots because conditional acceptance provided a more efficient acceptance process. However, from January 2004 through January 2007, the contracting officer's conditional acceptance practice did not provide for increased acceptance efficiency. Instead, the percentage of FMTV lots passing initial acceptance inspection declined from 86 percent to 21 percent. Based on the contractor's declining rate of vehicle lot acceptance, the contracting officer's conditional acceptance of the FMTVs was not resulting in a more efficient or economic acceptance process, as required by the FAR for conditional acceptance, and was not in the best interest of the Government. Finding B addresses the decline in first inspection acceptance of FMTV lots. Further, the administrative contracting officer stated that the Government did not allow the contractor to ship conditionally accepted vehicles with major nonconformances until they met contract specifications. As a result, the Army did not deploy the conditionally accepted vehicles with major nonconformances more rapidly

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and the Army did not meet the urgency requirement as established in the FAR to continue conditionally accepting FMTVs.

## **Effect of Not Withholding Payments**

The contractor did not have the incentive to resolve the problems that led to the conditional acceptance when the procuring contracting officer authorized the FMTV administrative contracting officer to conditionally accept vehicles not conforming to contract requirements and did not instruct the administrative contracting officer to withhold payment, as required by the FAR. Similarly, the administrative contracting officer did not provide incentive to the contractor to complete required testing when he conditionally accepted vehicles that had not received first article approval and did not withhold payments as stated in the contract. Because the administrative contracting officer did not withhold payment for vehicles conditionally accepted between January 2004 and January 2007, the Army made premature payments of more than \$3.8 million for incomplete vehicles. Specifically, the \$3.8 million the Army prematurely paid the contractor was for the 190 vehicles that had not completed testing requirements. The \$3.8 million is the difference between the amounts paid to the contractor for successful completion of events for contract performance-based payments and the total amount paid to the contractor for the conditional acceptance of the 190 vehicles. The remaining 466 vehicles were conditionally accepted with major nonconformances and delivery schedule delays for the contractor to incorporate engineering changes; however, we could not determine the amount prematurely paid to the contractor for those vehicles because the amount to be withheld is based on the estimated cost to correct the deficiencies as stated in the FAR 46.407. Information on the estimated cost to correct the deficiencies was not included on the contractor's requests for conditional acceptance.

## **Management Actions**

During the audit, the administrative contracting officer recognized the need to withhold payment on conditionally accepted vehicles. Specifically, on October 23, 2006, the administrative contracting officer issued a letter to the contractor. The letter stated that the administrative contracting officer would withhold 10 percent of the payment for 106 vehicles that were previously conditionally accepted and paid in full. The amount to be recouped totaled approximately \$2.2 million. The administrative contracting officer planned to recover the money by deducting the amount from the contractor's performance-based payments.

## **Conclusion**

The conditional acceptance of 656 vehicles by the contracting officers resulted in the Army prematurely paying the contractor more than

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\$3.8 million for vehicles for which the Army received no immediate benefit through expedited delivery to Army units. Specifically, the Army did not receive immediate benefit from conditionally accepting the vehicles because the Army did not accept delivery of the vehicles until the contractor completed testing requirements or corrected outstanding vehicle deficiencies.

By continuing to conditionally accept vehicles, the Government is not providing the incentive to produce conforming vehicles as required in the FAR. The conditional acceptance of vehicles unnecessarily increased the Army's cost risk and was not in the best interest of the Government. (This is a repeat finding that was discussed in DoD Inspector General Report No. 96-005, "Quick-Reaction Audit Report on Conditional Acceptance of Medium Tactical Vehicles," October 12, 1995.)

## **Management Comments on the Finding and Audit Response**

Summaries of management comments on the finding and audit responses are in Appendix C.

## **Recommendations, Management Comments, and Audit Response**

**A. We recommend that the Director, TACOM Life Cycle Management Command Acquisition Center direct that the procuring contracting officer for contract DAAE07-03-C-S023:**

**1. Discontinue the practice of conditionally accepting incomplete Family of Medium Tactical Vehicles for nonconformances of contractor responsibility unless reasons of economy or urgency exist as defined in the Federal Acquisition Regulation.**

**Management Comments.** The Deputy Chief of Staff, TACOM Life Cycle Management Command, responding for the Director, TACOM Life Cycle Management Command Acquisition Center, concurred with the recommendation. He stated that he would notify the procuring contracting officer to discontinue the practice of authorizing the conditional acceptance of incomplete FMTVs for nonconformances of contractor responsibility unless reasons of economy or urgency exist as defined in the FAR are documented. The Deputy Chief of Staff planned to implement this recommendation by September 30, 2007.

**Audit Response.** The Deputy Chief of Staff comments were responsive to the recommendation.

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**2. Limit payment to the contractor to 90 percent of the vehicle unit price for conditionally accepted vehicles that have not completed test requirements.**

**Management Comments.** The Deputy Chief of Staff, TACOM Life Cycle Management Command concurred with the recommendation, stating that the Director, TACOM Life Cycle Management Command Acquisition Center would instruct the procuring contracting officer to remind the administrative contracting officer to limit payment to the contractor to 90 percent of the vehicle unit price for conditionally accepted vehicles that have not completed test requirements. The Deputy Chief of Staff planned to implement this recommendation by September 30, 2007.

**Audit Response.** The Deputy Chief of Staff comments were responsive to the recommendation.

**3. Withhold payment of an amount to correct major vehicle nonconformances that were attributable to the contractor as specified in the contract payment terms and the Federal Acquisition Regulation.**

**Management Comments.** The Deputy Chief of Staff, TACOM Life Cycle Management Command concurred with the recommendation. He stated that the Director, TACOM Life Cycle Management Command Acquisition Center would instruct the procuring contracting officer that when authorizing conditional acceptance of vehicles with major nonconformances attributable to the contractor to establish an amount, as specified in the contract payment terms and the FAR, to be withheld by the administrative contracting officer to correct the major nonconformance. The Deputy Chief of Staff planned to implement this recommendation by September 30, 2007.

**Audit Response.** The Deputy Chief of Staff comments were responsive to the recommendation.

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## B. First Inspection Acceptance of Family of Medium Tactical Vehicles

Stewart and Stevenson Tactical Vehicle Systems, Limited Partnership (FMTV contractor) was submitting vehicle lots for Government acceptance that were not meeting first inspection acceptance requirements in the contract. Specifically, Government acceptance of FMTV lots at first inspection decreased from 86 percent in January 2004 to 21 percent in January 2007. This condition occurred because the contractor increased the daily vehicle production output to meet production requirements in DoD's annual and emergency supplemental appropriations, despite the contractor's inability to consistently meet vehicle lot first inspection acceptance requirements at lower production output levels. As a result, DCMA incurred additional reinspection costs to verify that vehicles resubmitted for inspection met contract specifications.

### Policy for Inspection and Acceptance of Goods

The FAR and the DCMA Guidebook provide guidance on the inspection and acceptance of goods delivered to the Government.

**FAR.** FAR 46.102, "Policy," requires contracting agencies to:

- include inspection and other quality requirements in contract clauses to protect the Government's interest,
- ensure that supplies or services meet contract requirements,
- conduct quality assurance before acceptance, and
- reject nonconforming supplies or services unless otherwise covered under the FAR provision.

FAR 46.105, "Contractor Responsibilities," states that the contractor is responsible for carrying out its obligation under the contract by controlling the quality of supplies or services presented to the Government. Further, the contractor should verify that suppliers have an acceptable quality control system and ensure that supplies or service conform to contract quality requirements.

FAR 52.246-2, "Inspection of Supplies—Fixed-Price," authorizes the contracting officer to charge the contractor for any additional cost of inspection or test when prior rejection makes reinspection or retest necessary.

**DCMA Guidebook.** The DCMA Guidebook states that when a supplier has a contractual nonconformance, a corrective action request formally

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communicates the deficiency and the request for corrective action to the supplier. See the definition for “Corrective Action Request” in Appendix B for the different levels of corrective action requests.

## Acceptance Requirements for FMTVs

The contract system specification requires the contractor to present vehicles that conform to the contract requirements for final inspection by the Government. The Product Manager FMTV and DCMA established a memorandum of agreement that defined quality metrics to measure the contractor’s quality performance at final vehicle inspection.

**Contract System Specification.** The contract system specification requires the contractor to ensure that all items produced meet all requirements of the acceptance test documents. It also requires the contractor to inspect each vehicle produced, using a Government-approved final inspection record, before presenting the vehicle to the Government. When defects are found, the contractor is responsible for taking corrective action and performing reinspection before offering the vehicle to the Government for final acceptance.

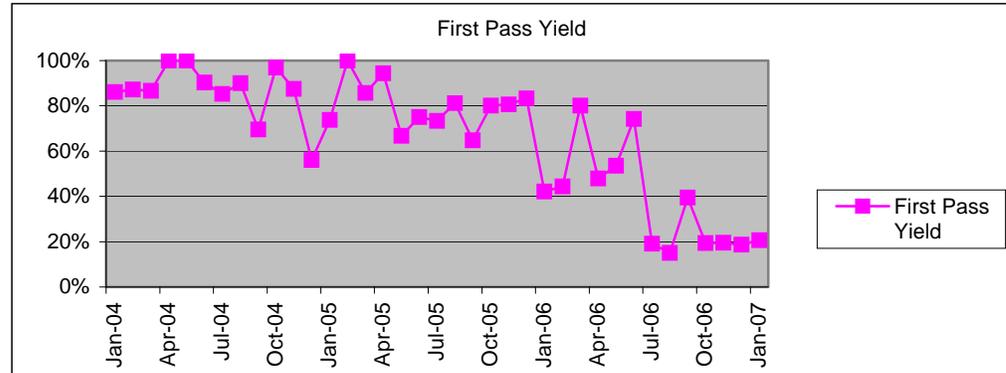
**Memorandum of Agreement.** In a September 1, 2006, memorandum of agreement, “Memorandum of Agreement with TACOM Product Manager Family of Medium Tactical Vehicles and Defense Contract Management Agency Sealy,” the Product Manager FMTV and DCMA established metrics, called the first pass yield, to measure the quality of the vehicles presented by the FMTV contractor. The memorandum of agreement established Government metrics for measuring the contractor’s performance. Per the memorandum of agreement, a first pass yield is calculated by dividing the total number of vehicle lots accepted at first inspection by the total number of vehicle lots presented. The first pass yield goal is to have 100-percent acceptance of vehicle lots presented during first inspection, as required by the contract system specification. A first pass yield rate less than 95 percent indicates that the contractor’s quality system is not preventing quality issues and places the Government at risk. A lot was considered acceptable if it had zero major defects or three or fewer minor defects.

## Inspection and Acceptance Pass Rate

With the increasing vehicle workload resulting from the emergency supplemental appropriations, the contractor has not demonstrated the ability to meet the first pass yield metric established in the memorandum of agreement. Specifically, the vehicle lot first pass yield rate decreased from 86 percent in January 2004 to 21 percent in January 2007. The first pass yield rate declined as the production level increased to meet the additional quantity of vehicles procured due to additional emergency supplemental funds. The increase of funds, and corresponding contractual requirements, required the contractor to eventually increase production to 35 vehicles per day from 12 vehicles per day in 2004. As of January 2007, production had increased to 33 vehicles per day. The following figure illustrates the first

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pass yield rate for vehicle lot inspections from January 2004 through January 2007.



**First Pass Yield Percentage Rates**

## DCMA Actions to Improve Contractor Performance

Although the contractor had not met the first pass yield threshold since February 2005 and DCMA issued 285 level II corrective action requests in 2006, DCMA did not charge the contractor required reinspection costs until after we announced this audit in July 2006. Further, the contractor did not place quality inspectors on the FMTV production line until after issuance of a level II corrective action request in September 2006.

**Level II Corrective Action Request.** On September 5, 2006, DCMA issued a level II corrective action request to the contractor for the period spanning October 1, 2004, through July 3, 2006, as a result of the contractor continuing to present vehicle lots for final acceptance inspection that did not conform to contract requirements. During that period, the contractor presented 570 vehicle lots for final acceptance, of which DCMA accepted 387 on first inspection, equating to a 69-percent first pass yield. DCMA had to reinspect some vehicle lots up to four times before final acceptance. Further, DCMA stated in the corrective action request that the Government expected to see some reduction in defects and an increase in the first pass yield within 30 days. If the downward trend continued, DCMA stated that it would charge reinspection costs as specified in FAR 52.246-2 and identified in the contract under the “Inspection and Acceptance” clause. The contractor responded to the level II corrective action request by stating that the increased defects at final acceptance inspection resulted from segmented training and lack of data feedback for resolution of the problems.

**Contractor Performance After Issuance of the Level II Corrective Action Request.** The contractor’s first pass yield rate improved slightly after issuance of the September 5, 2006, level II corrective action request but declined afterwards. Specifically, the contractor’s first pass yield rate

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increased from 15 percent in August 2006 to 39 percent in September 2006. The first pass yield fell to 19 percent in October, November, and December 2006. The first pass yield increased slightly in January 2007 to 21 percent.

**Reinspection Costs Charged to the Contractor.** On November 21, 2006, DCMA issued a letter to the contractor that assessed the contractor a fee of \$31,298 for reinspection costs. DCMA assessed this amount for reinspections of 26 vehicle lots from July 2006 through October 2006, which consumed 325 labor hours and associated administrative costs. In a November 21, 2006, memorandum, the contractor acknowledged DCMA's right to charge a reinspection fee and requested that DCMA and the contractor meet every 2 weeks to review progress. On November 29, 2006, DCMA agreed to meet with the contractor every 2 weeks to review quality process improvements. The contractor developed a list of tasks for corrective action and DCMA agreed to hold the \$31,298 bill for reinspection costs in abeyance.

On December 29, 2006, DCMA rebilled the contractor \$31,298 for reinspecting the 26 vehicle lots because the contractor had not demonstrated significant improvement in the first pass yield rate.

**Level III Corrective Action Request.** On February 15, 2007, DCMA issued a level III corrective action request to the contractor because the contractor continued to present vehicles for acceptance that did not conform to contract requirements after DCMA issued the level II corrective action request. In the level III corrective action request, DCMA notified the contractor that if the downward trend continued, DCMA would escalate the issue to higher levels of management. It also stated DCMA expected a response from the contractor to resolve the problem within 10 business days.

**Assessment of Additional Reinspection Costs.** On February 21, 2007, DCMA billed the contractor \$90,134 for reinspecting 52 vehicle lots and 76 special variants from November 2006 through January 2007.

**Quality Inspectors on the Production Line.** Part of the problem with the vehicle quality related to the contractor not having quality inspectors situated on the production line. Specifically, the contractor did not have any quality inspectors on its production line when we initiated this audit. The Armor Holdings Vice President for Quality, Tactical Vehicle Systems stated that quality inspectors had not been on the production line since 2003. As part of its response to the level II corrective action request, the contractor placed quality inspectors back on the production line on September 18, 2006.

## Conclusion

The FMTV contractor has not demonstrated the ability to meet the vehicle lot first pass yield rates for final inspection acceptance established in the memorandum of agreement and continued to present nonconforming vehicles for inspection. The daily contractor vehicle production output requirement for FMTVs has more than doubled since the Army received emergency supplemental funds, to a point where the contractor cannot produce quality

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vehicles. Accordingly, the Program Executive Officer for Combat Support and Combat Service Support needs to have the FMTV program office reduce the rate of FMTVs being produced by the contractor until the contractor can produce vehicle lots for first inspection acceptance that at a minimum meet a 95-percent first pass acceptance rate. As discussed in the finding, DCMA did take a number of actions to improve contractor performance before the audit, but those actions did not materially affect contractor performance. As a result, during the audit, DCMA began charging the contractor reinspection fees to encourage the contractor to present vehicle lots for final inspection acceptance in conformance with contract system specifications. Until the contractor begins presenting vehicle lots that meet the 95-percent first pass yield rate, DCMA needs to continue assessing the contractor for costs associated with reinspecting the vehicles.

## **Management Comments on the Finding and Audit Response**

Summaries of management comments on the finding and audit responses are in Appendix C.

## **Recommendations, Management Comments, and Audit Response**

**B.1. We recommend that the Program Executive Officer for Combat Support and Combat Service Support direct the Product Manager Family of Medium Tactical Vehicles to decrease the daily production output requirement for medium tactical vehicles until the contractor can present vehicles for final inspection acceptance that conform to contract requirements and achieve the first pass yield rates specified in the memorandum of agreement between the Product Manager Family of Medium Tactical Vehicles and the Defense Contract Management Agency.**

**Management Comments.** The Deputy Program Executive Officer Combat Support and Combat Service Support, responding for the Program Executive Officer Combat Support and Combat Service Support, nonconcurrent with the recommendation. He stated that the first pass yield measure is one of many internal metrics DCMA Sealy uses to assist them in ensuring that the quality of the trucks presented to the Government for acceptance is maintained. He stated that more importantly, the contractor continues to meet its monthly and yearly contractual truck delivery requirements to the Government. Additionally, the Deputy Program Executive Officer stated that vehicles produced and fielded are meeting or exceeding user requirements as evidenced by FMTV's operational readiness rate of over 93.5 percent. He stated that this outstanding operational readiness rate includes FMTVs used in the Global War on Terrorism in Iraq and Afghanistan. The Deputy

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Program Executive Officer stated that decreasing FMTV production would not be in the best interest of our Army or its soldiers. He stated that in accordance with the approved truck modernization strategy, the FMTV is replacing the older and much less reliable M-35, M809, and M939 tactical vehicles. The Deputy Program Executive Officer stated that the FMTV is a much safer tactical vehicle and is required to modernize the medium fleet. He stated that the FMTV's Low Signature Armored Cab is providing life-saving armor protection for our warfighters and any delay in fielding this vehicle will directly and unnecessarily place soldiers at risk.

**Audit Response.** The Deputy Program Executive Officer's comments did not address the issue of the contractor providing vehicles for inspection that do not meet contract requirements. The Product Manager and DCMA established the first pass yield to measure the quality of the vehicles presented by the contractor and to determine whether the contractor was presenting vehicles that met contract specifications. If the vehicles do not meet contract specifications DCMA generates a corrective action request to communicate the deficiencies and request corrective action by the contractor. If the contractor is not delivering vehicles for inspection that meet system specifications, the Government may take appropriate action, such as terminating the contract. DCMA has issued more than 285 corrective action requests based on quality issues, which the first pass yield measures. According to DCMA officials, the contractor met the total FMTV quantity deliveries required by the contract. However, the procuring contracting officer allowed the contractor to substitute different FMTV variants to meet overall monthly quantity requirements. According to the Deputy Chief of Staff, G-8, only 445, or 10 percent, of the 4,354 vehicles scheduled to be delivered by September 2008 are going to Southwest Asia. The Army plans to use the remaining vehicles to support the Army's modularity program and backfill for vehicles already shipped to Southwest Asia. Therefore, temporarily reducing the daily production rate should not affect deliveries to Southwest Asia because even with reduced daily vehicle production requirements, the FMTV contractor will be able to timely produce the 445 vehicles planned for shipment to Southwest Asia.

We do not dispute that the performance of deployed vehicles meets contract specifications; however, it is important to hold the contractor to performance standards to effectively and efficiently meet the needs of warfighters. Temporarily decreasing daily vehicle production requirements would provide the contractor an opportunity and incentive to correct production problems. It would also enable the contractor to increase its capability to present vehicles that conform to contract specifications at first inspection, which would enable the Army to immediately ship the vehicles to Army units. Therefore, temporarily slowing down the production rate would not increase risk to the warfighter as stated in the management comments. Accordingly, we request that the Program Executive Officer for Combat Support and Combat Service Support reconsider his position on the recommendation and provide additional comments in response to the final report.

**B.2. We recommend that the Director, Defense Contract Management Agency continue to bill the contractor for reinspection costs, as authorized in Federal Acquisition Regulation 52.246-2, "Inspection of Supplies—Fixed-Price," until the contractor presents vehicles for final inspection acceptance that conform to contract requirements and**

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**achieve first pass yield rates specified in the memorandum of agreement between the Product Manager Family of Medium Tactical Vehicles and Defense Contract Management Agency.**

**Management Comments.** The Acting Director, Defense Contract Management Agency partially concurred with the recommendation. He stated that he agreed that billing for reinspection costs is authorized under FAR 52.246-2. However, the Acting Director stated that reinspection charges are just one of many tools that DCMA can use to improve contractor performance. He stated that DCMA took several actions to improve contractor performance, which included issuing corrective action requests and initiating an integrated process team to examine the quality issues. The Acting Director stated that the integrated process team also implemented several actions, such as developing an employee training program, clarifying the vehicle technical specification, developing a paint guidance reference, changing the production process, changing the vehicle inspection, and initiating a defect reduction effort. Because those actions did not improve the contractor's final vehicle inspection acceptance rate to an acceptable level, he stated that DCMA plans to continue charging reinspection costs until the first pass yield rate exceeds 80 percent. Because the first pass yield is specified in the memorandum of agreement, not in the contract, that rate can be adjusted.

**Audit Response.** The Acting Director's comments were responsive to the intent of the recommendation.

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## Appendix A. Scope and Methodology

We evaluated whether the Army was cost effectively producing and funding the Family of Medium Tactical Vehicles (FMTV) in support of the Global War on Terrorism. In addition, we evaluated whether the Army adequately protected the Government's interests when it implemented conditional acceptance provisions in the production contracts for the FMTV.

We conducted this performance audit from July 2006 through July 2007 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.

We reviewed documentation and information dated from June 1, 1991, through February 21, 2007, to accomplish the audit objectives.

We reviewed program documents for the FMTV including the joint service operational requirement document, June 1, 1991; the Acquisition Plan, September 25, 2002; the acquisition program baseline, March 25, 2003; the operational requirements document, April 28, 2003; and the test and evaluation master plan, March 23, 2004.

We reviewed contractual documents for the FMTV including contracts DAAE07-03-C-S023 and W56HZV-04-C-0591 with Stewart and Stevenson Tactical Vehicle Systems, Limited Partnership; contracts W56HZV-04-C-0297 and W56HZV-04-C-0321 with Radian Incorporated; and conditional acceptance letters and performance-based payment invoices from January 2004 to January 2007.

We reviewed funding documents for the FMTV including the Department of Defense "Fiscal Year 2005 Supplemental Request for Operation Iraqi Freedom, Operation Enduring Freedom, and Operation Unified Assistance," February 2005; Public Law 109-13, "Making Emergency Supplemental Appropriations for Defense, the Global War on Terrorism, and Tsunami Relief, for the Fiscal Year Ending September 30, 2005," May 11, 2005; the FY 2005 Funding Authorization Document August 22, 2005; Public Law 109-148, "Department of Defense Emergency Supplemental Appropriations to Address Hurricanes in the Gulf of Mexico, and Pandemic Influenza Act, 2006," December 30, 2005; Department of Defense "Fiscal Year 2006 Supplemental Request for Operation Iraqi Freedom and Operation Enduring Freedom," February 2006; the Army National Guard Military Interdepartmental Purchase Request No. MIPR6FTACNGR01, March 21, 2006; memorandum from the Deputy Secretary of Defense, "Ground Rules and Process for FY 2007 Spring Supplemental," October 25, 2006; and the "FY 2006 Main Supplemental Funds Release Status for the Project Manager Tactical Vehicles," December 14, 2006.

We reviewed the production documents for the FMTV including the production status report for contract DAAE07-03-C-S023,

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September 20, 2006; the shipped vehicles report, January 27, 2007; and the reports of conditionally accepted vehicles received, September 26, 2006, and December 5, 2006.

We also contacted staffs at the Army Deputy Chiefs of Staff (G-3), (G-4), and (G-8); the Joint Capability Development Directorate (J-8); the Director, Operational Test and Evaluation; the Army Materiel Command; the Army Test and Evaluation Command; the Project Manager Tactical Vehicles; the Defense Contract Management Agency; and Stewart and Stevenson Tactical Vehicle Systems, Limited Partnership, to determine program background, history, and the reasons why the Army continued to conditionally accept FMTVs.

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

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

## **Prior Coverage**

No prior coverage has been conducted on the conditional acceptance and the final inspection acceptance of Army medium tactical vehicles during the last 5 years.

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## Appendix B. Glossary

**Administrative Contracting Officer.** The administrative contracting officer is responsible for government contracts administration. The administrative contracting officer develops and applies quality assurance procedures and verifies whether supplies or services conform to contract requirements.

**Combat Service Support.** Combat Service Support staffs, arms, fuels, fixes, and moves the force. Its three major categories of tasks are logistics support, personnel service support, and health services support. Logistics includes supply, transportation, maintenance, and field services. Major personnel service support contributes to the welfare and morale of soldiers. Support functions include personnel and administration services, chaplain operations, and enemy prisoner of war operations. Health services include medical treatment and evacuation of casualties, preventive medicine, and medical supply operations.

**Conditional Acceptance.** Conditional acceptance is the acceptance of contractor supplies or services that do not conform to contract quality requirements or are otherwise incomplete. The contractor is required to correct the deficiencies or otherwise complete contract requirements by a specified date.

**Contract System Specification.** The contract system specification identifies the physical, performance, and inspection requirements of the program. The system specification establishes these requirements by identifying technical data requirements from which the vehicle is to be produced. It also establishes physical characteristics and performance requirements for the vehicles produced. Further, the system specification identifies performance and quality test requirements used to verify that the vehicles meet the specified performance standards.

**Corrective Action Request.** A corrective action request is prepared by a DCMA team member to formally communicate a contractual nonconformance to the supplier. The corrective action request lists the deficiencies and requests corrective action. Suppliers must respond to a corrective action request. There are four levels of corrective action requests:

- Level I corrective action requests are issued (written or verbal) when a contractual noncompliance requires no special management attention to correct. Level I corrective action requests may be directed to working-level personnel.
- Level II corrective action requests are written requests for corrective action for contractual noncompliances that are systemic in nature and could adversely affect cost, schedule, or performance if not corrected. Level II corrective action requests should be directed to the supplier management level responsible for the process with a copy to the responsible administrative contracting officer.

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- Level III corrective action requests call attention to serious contractual noncompliances to the supplier's top management. Level III corrective action requests may be issued with contractual remedies such as reductions of progress payments, cost disallowances, cure notices, show cause letters, or business management systems disapprovals.
  - Level IV corrective action requests involve contractual remedies such as suspension of progress payments or product acceptance activities, termination for default, and suspension or debarment, in accordance with applicable Federal Acquisition Regulation or Defense Federal Acquisition Regulation Supplement policies and procedures.

**Cost Risk.** Cost risk is the risk that a program will not meet its acquisition strategy cost objectives. Two methodologies are used to achieve the cost objectives and minimize cost risk. The first methodology is cost as an independent variable where life-cycle cost objectives are balanced against performance, schedule, and mission needs. In the second methodology, the acquisition authority establishes cost objectives, which are provisions made to measure the cost of processes, products, jobs, and capitalized projects.

**Defense Contract Management Agency.** The Defense Contract Management Agency (DCMA) is an independent agency that performs contract administration functions. The contracting officer delegates the contract administration functions to DCMA. DCMA performs functions that include:

- contract management for diverse product lines;
- price/cost analyses, overhead and contractor system reviews, financial services, property and plant clearance, transportation and packaging, and termination settlements;
- quality assurance by verification of contractor processes and performance of final inspection and acceptance of critical items; and
- program and technical support that analyze cost, schedule, and technical performance.

**Engineering Change Proposal.** An engineering change proposal recommends to the responsible authority that a change to an original item of equipment be considered, and the design or engineering change be incorporated into the article to modify, add to, delete, or supersede original parts.

**Equitable Price Reduction.** An equitable price reduction is an amount that the contracting officer withholds from payment for an item to cover the estimated cost and related profit on unfinished or deficient work on

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conditionally accepted items. The contracting officer must document in the contract file the basis for the amounts withheld.

**First Article Testing and Approval.** First article testing and approval ensures that the contractor can furnish a product that conforms to all contract requirements for acceptance. The Government conducts these tests on a random sample from the first production lot.

**First Pass Yield.** DCMA uses the first pass yield as a measure of quality. It is obtained by dividing the number of lots accepted by the number of lots inspected.

**Full-Rate Production and Deployment.** Full-rate production and deployment is the second stage of the production and deployment phase of the acquisition process. This stage follows after the milestone decision authority approves a system for full-rate production. The system is produced at full-rate and deployed to the field.

**Funding Authorization Document.** A funding authorization document authorizes the use of funds for a governmental activity. The Army Comptroller distributes the money to the Program Executive Office, and the Program Executive Office divides the money among its programs.

**Milestone Decision Authority.** The milestone decision authority is the designated individual with overall responsibility for a program. The milestone decision authority has the authority to approve entry of an acquisition program into the next phase of the acquisition process and is accountable for cost, schedule, and performance reporting to higher authority, including congressional reporting.

**Military Interdepartmental Purchase Request.** A military interdepartmental purchase request is the primary document that DOD organizations use to order goods or services from other DoD Components or non-DoD Federal activities.

**Nonconformance.** A nonconformance is a supply or service that does not conform to contract requirements. There are a variety of nonconformance types.

- A critical nonconformance is a nonconformance that is likely to result in hazardous or unsafe conditions for individuals using, maintaining, or depending on the supplies or services; or is likely to prevent performance of a vital agency mission.
- A major nonconformance is a nonconformance, other than critical, that is likely to result in failure of the supplies or services, or to greatly reduce the usability of the supplies or services for their intended purpose.
- A minor nonconformance is a nonconformance that is not likely to greatly reduce the usability of the supplies or services for their intended purpose, or is a departure from established standards

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having little bearing on the effective use or operation of the supplies or services.

**Performance-Based Payments.** Performance-based payments are a method of providing financing to contractors performing under fixed-price contracts. Performance-based payments differ from traditional progress payments in that they are based on the achievement of specific events or accomplishments that are defined and valued in advance by the parties to the contract, rather than being tied to and based on incurred costs of performance.

**Power Packs.** Power packs consist of a turbine engine and a transmission. Instead of fixing the engine or transmission on-site, maintenance soldiers simply remove the faulty power pack and replace with an operable one.

**TACOM Life Cycle Management Command.** The TACOM Life Cycle Management Command, in partnership with the Army's Program Executive Offices, is one of the Army's largest organizations performing research, development, and sustainment of weapons systems. It provides and sustains mobility, lethality, and survivability requirements for soldiers through ground combat, automotive, marine, and armaments technologies.

**Test and Evaluation Master Plan.** A test and evaluation master plan documents the overall structure and objectives of a program's test and evaluation program. It provides a framework within which to generate detailed test and evaluation plans, and documents schedule and resource implications associated with the test and evaluation program.

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## Appendix C. Management Comments on the Report and Audit Response

The Acting Director, Defense Contract Management Agency and the Deputy Chief of Staff, TACOM Life Cycle Management Command provided comments on the draft report. Summaries of those comments and our responses follow. The complete text of those comments is in the Management Comments section of this report.

### Management Comments on the Overall Report and Audit Response

The Acting Director, Defense Contract Management Agency and the Deputy Chief of Staff, TACOM Life Cycle Management Command commented on statements in the executive summary and background sections of the draft report.

**Management Comments on the Memorandum of Agreement.** The Acting Director, Defense Contract Management Agency commented on the first page of the Executive Summary, which stated, “The FMTV contractor, Stewart and Stevenson Services, was not meeting contract requirements for acceptance of vehicles at first Government inspection.” He suggested the sentence read, “The FMTV contractor, Stewart and Stevenson Services, was not meeting the Government’s goals as stated in the memorandum of agreement between the Product Manager and DCMA for acceptance of vehicles at first Government inspection.” In addition, the Acting Director commented on the first paragraph of the second page of the Executive Summary, which stated, “The FMTV contractor submitted vehicles for Government acceptance that did not meet first inspection acceptance requirements in the contract.” He suggested that the sentence read, “The FMTV contractor submitted vehicles for Government acceptance that did not meet the Government’s first inspection acceptance standards as stated in the memorandum of agreement between the product manager and DCMA.”

**Audit Response.** Contract System Specification Clause 4.4.1, “One Hundred Percent (100 percent) Final Inspection,” requires the contractor to ensure that all items produced meet all requirements of the acceptance test documents. Before presenting the vehicle to the Government, the contractor is required to inspect each vehicle produced, using a Government-approved final inspection record. Supplementing the contract requirement, the memorandum of agreement between the Product Manager and DCMA defined acceptable levels of performance by the contractor when presenting vehicles for final inspection acceptance. Accordingly, the contractor was not meeting the requirements in the Contract System Specification Clause 4.4.1 or the acceptable rate established in the memorandum of agreement for acceptance of vehicles at first Government inspection.

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**Management Comments on the Invoicing Beyond 90 Percent for Vehicles Awaiting First Article Approval.** The Acting Director commented on the Review of Internal Controls section, which stated, “Specifically, the FMTV administrative contracting officer did not adhere to contract provisions when conditionally accepting incomplete vehicles with major nonconformances and paying the contractor up to 100 percent of the contract price for the vehicles.” The Director stated that vehicles waiting for first article approval did not have any noncompliances nor were they incomplete. He recommended the sentence state, “Specifically the FMTV administrative contracting officer did not adhere to contract provisions by allowing the contractor to bill 100 % of the contract price for new FMTV variants that were conditionally accepted while waiting First Article approval.” The Acting Director stated that on August 16, 2007, the administrative contracting officer sent a letter to the contractor’s Vice President for Contracts and Supply Chain Management and the Vice President of Finance and to all DCMA medium tactical vehicle contracting personnel, as well as DCMA senior leadership, to preclude invoicing beyond 90 percent for vehicles waiting first article approval. The letter, “Contract DAAE07-03-C-S023, Section E.8.2, entitled, ‘Conditional Acceptance Prior to First Article Approval,’” repeated the exact language in the contract directing the administrative contracting officer to withhold 10 percent on vehicles conditionally accepted prior to first article approval.

**Audit Response.** The August 16, 2007, letter that DCMA sent to the contractor is a positive measure to preclude the administrative contracting officer from exceeding the 90-percent payment limitation for vehicles conditionally accepted while awaiting completion of first article testing. However, in addition to the administrative contracting officer actions for vehicles awaiting the completion of first article testing, the procuring contracting officer authorized the FMTV administrative contracting officer to conditionally accept 466 vehicles with major nonconformances without appropriate payment amounts being withheld. The Acting Director’s suggested revision would omit reference to those vehicles. To clarify the statement, we changed the sentence to read, “Specifically, the FMTV administrative contracting officer did not adhere to contract provisions when:

- conditionally accepting vehicles that had not completed required first article testing; and
- paying the contractor up to 100 percent of the contract price for conditionally accepted vehicles that were authorized by the procuring contracting officer or authorized by the contract terms.”

**Management Comments on the Charging Reinspection Costs to the Contractor.** The Acting Director commented on in the Review of Internal Controls section, which stated, “Further, the Defense Contract Management Agency (DCMA) administrative contracting officer just began charging the contractor on December 29, 2006, for reinspection costs when the contractor did not meet contract requirements for vehicle inspection acceptance.” He suggested the sentence state, “On December 29, 2006, Defense Contract Management Agency (DCMA) administrative contracting officer just began

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charging the contractor for reinspection costs when the contractor failed to noticeably improve the vehicle lot inspection acceptance rate.”

**Audit Response.** The goals of the memorandum of agreement defined acceptable levels of performance by the contractor as agreed to by DCMA and the Product Manager. As previously stated, the Contract System Specification Clause 4.4.1, “One Hundred Percent (100%) Final Inspection,” requires the contractor to present goods for final inspection that conform to contract specifications. Accordingly, the contractor was not meeting the requirements of Contract System Specification Clause 4.4.1 nor the acceptable rate established in the memorandum of agreement for acceptance of vehicles at first Government inspection. As a result, we did not revise the report.

## **Management Comments on Finding A and Audit Response**

The Acting Director, Defense Contract Management Agency and the Deputy Chief of Staff, TACOM Life Cycle Management Command commented on finding A statements on the use of the conditional acceptance clause, the contractor’s responsibility for conditionally accepted vehicles; nonconforming parts; and the types of conditional acceptance.

**Management Comments on the Use of the Conditional Acceptance Clause.** The Deputy Chief of Staff commented on the “Contractor Responsibility for Conditionally Accepted Vehicles” paragraph, stating that he agreed that some vehicles were conditionally accepted for more than one reason but he believed that 1,900 was a typographical error.

**Audit Response.** Based on supporting documentation, the total number of reasons that the Government conditionally accepted vehicles because of contractor responsibility was 1,900, as stated in the finding. To determine the number of reasons for vehicle conditional acceptance, the audit team reviewed listings of vehicles conditionally accepted from the Defense Contract Management Agency staff at Sealy, Texas. We identified from the lists the vehicle models and the reasons for conditional acceptance from January 30, 2004, through January 31, 2007. The Government conditionally accepted 1,745 vehicles in that timeframe. The Government conditionally accepted 155 of the 1,745 vehicles for more than one reason, totaling 1,900 reasons for conditionally accepting the 1,745 vehicles.

**Management Comments on the Contractor’s Responsibility for Conditionally Accepted Vehicles.** In the “Contractor Responsibility for Conditionally Accepted Vehicles” paragraph, the last sentence stated, “In acting on the contractor requests, the administrative contracting officer paid 100 percent of the vehicle price for 656 of the 1,745 vehicles that were conditionally accepted.” The Acting Director recommended the sentence read:

In acting on the contractor requests, the procuring contracting officer directed that 466 of the 656 out of the original 1,745 vehicles be conditionally accepted and paid at 100 percent of the

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vehicle price. The conditional acceptance of the remaining 190 was authorized by the contract which also required that the contractor to bill no more than 90 percent of the vehicle price. The contractor billed and was paid 100 percent.

**Audit Response.** We modified the finding to meet the intent of the suggested revision.

**Management Comments on Nonconforming Parts.** In the “Nonconforming Parts” paragraph, the third sentence stated, “The administrative contracting officer conditionally accepted 14 vehicles and did not withhold payments from the contractor for the correction of the nonconforming draglink.” The Director recommended the sentence state “The procuring contracting officer authorized conditional acceptance of 14 vehicles but did not require a withhold.”

**Audit Response.** We modified the finding to meet the intent of the suggested revision.

**Management Comments on the Types of Conditional Acceptance.** The Acting Director commented on the first paragraph of the “Effects of Not Withholding Payments” section, which stated:

When the administrative contracting officer conditionally accepted vehicles and did not withhold payment, as required by the FAR, the contractor did not have the incentive to resolve the problems that led to the conditional acceptance. During the audit, the administrative contracting officer recognized the need to withhold payment on conditionally accepted supplies. Specifically, on October 23, 2006, the administrative contracting officer issued a letter to the contractor. The letter stated that the administrative contracting officer would withhold 10 percent of the payment for 106 vehicles that were previously conditionally accepted and paid in full. The amount to be recouped totaled approximately \$2.2 million. The administrative contracting officer planned to recover the money by deducting the amount from the contractor’s Performance-based payments.

The Acting Director stated that there are two distinct types of conditional acceptance:

Conditional acceptance prior to first article completion occurs when a new FMTV variant is designed and tested, prior to first article approval and before it is fielded, it is conditionally accepted with a 10 percent withhold as stated in the contract. Just like any other vehicle the Government accepts, these trucks do not have major noncompliances as they are inspected to the same final inspection criteria as all the other vehicles, the vehicles are just waiting for all testing to be complete and then have any changes that result from the testing be put on the trucks before the vehicles are fielded. At the time of the contract, this conditional acceptance was anticipated. All other conditional acceptance

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actions happened during the period of performance of the contract. In all these cases, identified in the DODIG report, the procuring contracting officer sent a letter authorizing the administrative contracting officer to conditionally accept vehicles and identified the withhold amount if any. If there was a withhold required, it was taken.

The Acting Director recommended the paragraph read:

The administrative contracting officer conditionally accepted vehicles that had not received First Article approval but did not withhold payments as required by the contract. During the audit, the administrative contracting officer recognized the need to withhold payment on these vehicles. Specifically, on October 23, 2006, the administrative contracting officer issued a letter to the contractor. The letter stated that the administrative contracting officer would withhold 10 percent of the payment for 106 vehicles that were previously conditionally accepted and paid in full. The amount to be recouped totaled approximately \$2.2 million. The administrative contracting officer planned to recover the money by deducting the amount from the contractor's Performance-based payments.

**Audit Response.** We modified the finding to meet the intent of the suggested revision.

## Management Comments on Finding B and Audit Response

The Acting Director, Defense Contract Management Agency commented on finding B statements on the contractor submission of vehicles for inspection; the first pass yield; actions to improve contractor performance; corrective actions; and charging reinspection costs.

**Management Comments on the Contractor Submission of Vehicles for Inspection.** The Acting Director commented on the first sentence of the charge paragraph of finding B, which stated, "The FMTV contractor was submitting vehicle lots for Government acceptance that were not meeting first inspection acceptance requirements in the contract." The Acting Director recommended the sentence read "The FMTV contractor was submitting vehicle lots for Government acceptance that were not meeting the Government's first inspection acceptance goals in the memorandum of agreement established between the product manager and DCMA."

**Audit Response.** See our audit response to the Director's comment on the memorandum of agreement on page 27 of this report.

**Management Comments on the First Pass Yield.** The Acting Director commented on the sentence in the "Memorandum of Agreement" paragraph, which stated, "The first pass yield is to have 100 percent acceptance of vehicle lots presented during first inspection, as required by the contract system specification." The Acting Director recommended the sentence read, "The first pass yield is to have 100 percent acceptance of vehicle lots

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presented during first inspection, a target goal as identified in the memorandum of agreement between the product manager and DCMA.”

**Audit Response.** The goals of the memorandum of agreement define acceptable levels of performance by the contractor as agreed to by DCMA and the Product Manager. However, the Contract System Specification Clause 4.4.1, “One Hundred Percent (100%) Final Inspection,” requires 100 percent of the goods presented by the contractor for final inspection to conform to contract specifications. Accordingly, we did not revise the report.

**Management Comments on the Actions to Improve Contractor Performance.** The Acting Director commented on the sentence in the first paragraph of the “DCMA Actions to Improve Contractor Performance,” which states, “Although the contractor had not met the first pass yield threshold since February 2005 and DCMA issued 285 level II corrective action requests in 2006, DCMA did not charge the contractor required reinspection costs until after we announced this audit in July 2006.” He recommended the sentence read, “The contractor had not met the first pass yield threshold since February 2005 and DCMA issued 285 level II corrective action requests in 2006. As a result of a significant drop in first pass yield in July 06, DCMA added consideration of reinspection charges among many other actions taken to improve contractor performance.”

**Audit Response.** We agree that the contractor’s performance significantly dropped in July 2006, but the contractor’s performance also significantly dropped in January 2006. Accordingly, the finding correctly stated that DCMA did not start charging the contractor reinspection costs until after we announced the audit in July 2006 even though the contractor’s performance deteriorated much earlier.

**Management Comments on the DCMA Corrective Actions.** Regarding the “Conclusion” paragraph of finding B, the Acting Director stated that DCMA began taking action to improve contractor quality well before the audit. Accordingly, he recommended that the sentence that stated, “Also, during the audit, DCMA began taking appropriate actions to get the contractor to improve the quality of vehicle lots presented for final inspection” be changed. He recommended that the sentence read “Also, DCMA took several actions to get the contractor to improve the quality of vehicle lots presented for final inspection.”

**Audit Response.** We added a sentence to the conclusion paragraph to give DCMA credit for taking a number of actions to improve contractor performance before the audit although those actions did not materially affect contractor performance. We modified the sentence in question to state, “As a result, during the audit, DCMA began charging the contractor reinspection fees to encourage the contractor to present vehicle lots for final inspection acceptance in conformance with contract system specifications requirements.”

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**Management Comments on the Charging Reinspection Costs.** The Acting Director stated that the “Conclusion” paragraph in finding B suggests that DCMA was required to charge reinspection costs and had failed to do that. He stated that FAR 52.246-2 “Inspection of Supplies–Fixed Price” does not require DCMA to charge reinspection costs, it merely allows the charging of reinspection costs at the discretion of the contracting officer.

**Audit Response.** We agree that the FAR does not require DCMA to charge reinspection costs, but we do not agree that our paragraph implies it is a requirement. We state that the FAR authorizes DCMA to charge reinspection costs, which does not imply that it is a requirement.

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## **Appendix D. Report Distribution**

### **Office of the Secretary of Defense**

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

### **Department of the Army**

Assistant Secretary of the Army (Financial Management and Comptroller)  
Auditor General, Department of the Army

### **Department of the Navy**

Auditor General, Department of the Navy

### **Department of the Air Force**

Auditor General, Department of the Air Force

### **Other Defense Organizations**

Director, Defense Contract Management Agency

### **Non-Defense Federal Organization**

Office of Management and Budget

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## **Congressional Committees and Subcommittees, Chairman and Ranking Minority Member**

Senate Committee on Appropriations  
Senate Subcommittee on Defense, Committee on Appropriations  
Senate Committee on Armed Services  
Senate Committee on Homeland Security and Governmental Affairs  
House Committee on Appropriations  
House Subcommittee on Defense, Committee on Appropriations  
House Committee on Armed Services  
House Committee on Oversight and Government Reform  
House Subcommittee on Government Management, Organization, and Procurement,  
Committee on Oversight and Government Reform  
House Subcommittee on National Security and Foreign Affairs,  
Committee on Oversight and Government Reform

# Defense Contract Management Agency Comments



DEFENSE CONTRACT MANAGEMENT AGENCY  
6350 WALKER LANE, SUITE 300  
ALEXANDRIA, VA 22310-3241

IN REPLY  
REFER TO

DCMA-DMI

OCT 25 2007

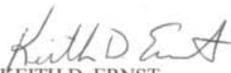
MEMORANDUM FOR PROGRAM DIRECTOR, ACQUISITION AND CONTRACT  
MANAGEMENT, DEPARTMENT OF DEFENSE  
INSPECTOR GENERAL, OFFICE OF THE DEPUTY  
INSPECTOR GENERAL

SUBJECT: Department of Defense – Inspector General Draft Report, Project Number  
D2006-D000AE-0225, Report on The Army's Procurement and Conditional  
Acceptance of Medium Tactical Vehicles

Reference: DoDIG draft audit report, Project Number D2006-D000AE-0225,  
subject as above.

We have attached the Headquarters Defense Contract Management Agency  
response and technical comments to the findings and recommendations cited in the  
subject report.

Point of contact is Ms. Sonya Moman at (703) 530-3163 or  
[sonya.moman@dcma.mil](mailto:sonya.moman@dcma.mil).

  
KEITH D. ERNST  
Acting Director

Attachment  
As

SUBJECT: The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles (Project Number D2006-D000AE-0225)

**Finding B First Inspection Acceptance of Family of Medium Tactical Vehicles**

The FMTV contractor was submitting vehicle lots for Government acceptance that were not meeting first inspection acceptance requirements in the contract. Specifically, Government acceptance of FMTV lots at first inspection decreased from 86 percent in January 2004 to 21 percent in January 2007. This condition occurred because the contractor increased the daily vehicle production output to meet production requirements in DoD's annual and emergency supplemental appropriations, despite the contractor's inability to consistently meet vehicle lot first inspection acceptance requirements at lower production output levels. As a result, the DCMA incurred additional reinspection costs to verify that vehicles resubmitted for inspection met contract specifications.

**Recommendation B2:**

We recommend that the Director, Defense Contract Management Agency continue to bill the contractor for reinspection costs, as authorized in Federal Acquisition Regulation 52.246-2, "Inspection of Supplies—Fixed-Price," until the contractor presents vehicles for final inspection acceptance that conform to contract requirements and achieve first pass yield rates specified in the memorandum of agreement between the Product Manager Family of Medium Tactical Vehicles and Defense Contract Management Agency.

**DCMA Comments: Partially Concur.** DCMA agrees that billing the contractor for reinspection costs is an option. FAR 52.246-2 (e)(1) and (2) state that the "Contracting Officer may charge to the Contractor the additional cost of inspection or test" and that the "Contracting Officer may also charge the Contractor for any additional cost of inspection or test when prior rejection makes reinspection or retest necessary." (Attachment 1)

Reinspection charges are at the discretion of the contracting officer and are just one of many tools that DCMA can use to improve contractor performance. DCMA took several actions to improve contractor performance, which, as mentioned in the DoD IG report included the issuance of corrective action reports (Attachment 2) and, as not mentioned in the DoD IG report, initiating an IPT to further examine the quality issues. The IPT implemented several actions to include development of employee training program, clarification of vehicle technical specification, development of paint guidance reference, production process change, vehicle inspection change, and initiation of defect reduction effort. (Copies of this documentation were provided to the IG team in May 2007). Consideration of reinspection charges began in Jul 06, when the most significant drop in first pass yield occurred. DCMA imposed reinspection charges when it continued to see no noticeable improvement in first pass yield in spite of the actions taken as identified in the previous paragraph. DCMA plans to continue charging reinspection costs until the first pass yield exceeds 80% however this is not a contractual requirement and it can be adjusted.

\*The attachment was omitted because of length. Copies will be provided upon request.

SUBJECT: The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles (Project Number D2006-D000AE-0225)

Because the memorandum of agreement (Attachment 3) is not a contract between the Government and the contractor, the contractor cannot literally be held to perform in accordance with it. However, the memorandum of agreement does document the acceptance standards that both DCMA and the TACOM MTV will employ in an attempt to induce the contractor to provide conforming product. The memorandum of agreement establishes internal Government goals for DCMA's use to monitor and report quality performance to the product manager on a monthly basis. The first pass yield goal is to have 100 percent acceptance of vehicle lots presented during the first inspection. The contract system specification does not address first pass yield. The contract requires that no defects be accepted. Regardless of the number of times DCMA inspects a lot, the contract requirement is met as long it has zero defects when accepted.

**Suggested Language Recommendation B2**

We recommend that the Director, Defense Contract Management Agency continue billing the contractor for reinspection costs, as authorized in Federal Acquisition Regulation 52.246-2, "Inspection of Supplies—Fixed-Price", and use all other method as appropriate until the contractor reaches a first pass yield rate(s) that is/are acceptable to the Government. The Government's acceptable rate(s) which can be adjusted up or down upon agreement of both parties have been documented in the memorandum of agreement between the Product Manager Family of Medium Tactical Vehicles and Defense Contract Management Agency.

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\*The attachment was omitted because of length. Copies will be provided upon request.

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SUBJECT: The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles (Project Number D2006-D000AE-0225)

**Technical Comments:**

**The following misstatements, recommended changes, and DCMA comments are based on the DCMA information in paragraph (b) above clarifying that the First Pass Acceptance requirements are not contractual required but contained in the memorandum of understanding between the product manager and DCMA.**

**Misstatement:** (Page i, paragraph 3) Executive Summary: "..... the FMTV contractor, Stewart and Stevenson Services, was not meeting contract requirements for acceptance of vehicles at first Government inspection."

**Recommended Change:** "..... the FMTV contractor, Stewart and Stevenson Services, was not meeting the Government's goals, as stated in the memorandum of agreement between the Product Manager and DCMA for acceptance of vehicles at first Government inspection."

**Misstatement:** (Page ii, paragraph 1) Executive Summary: "The FMTV contractor submitted vehicles for Government acceptance that did not meet first inspection acceptance requirements in the contract."

**Recommended Change:** "The FMTV contractor submitted vehicles for Government acceptance that did not meet the Government's first inspection acceptance standards, as stated in the memorandum of agreement between the product manager and DCMA."

**Misstatement:** (Page 4, paragraph 1) Review of Internal Controls: "Further, the Defense Contract Management Agency's (DCMA) administrative contracting officer ..... when the contractor did not meet contract requirements for vehicle inspection acceptance."

**Recommended Change:** "Further, the Defense Contract Management Agency's (DCMA) administrative contracting officer ..... when the contractor did not meet the Government's goals for vehicle inspection acceptance, as stated in the memorandum of agreement."

**Misstatement:** (Page 4, Paragraph 1), Review of Internal Controls Section, states, "Further, the Defense Contract Management Agency's (DCMA) administrative contracting officer just began charging the contractor on December 29, 2006, for reinspection costs when the contractor did not meet contract requirements for vehicle inspection acceptance."

**Recommended Change:** "On December 29, 2006, the Defense Contract Management Agency's (DCMA) administrative contracting officer began charging the contractor for reinspection costs when the contractor failed to noticeably improve the vehicle lot inspection acceptance rate."

SUBJECT: The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles (Project Number D2006-D000AE-0225)

**Misstatement:** (Page 13): "The FMTV contractor was submitting vehicle lots for Government acceptance that were not meeting first inspection acceptance requirements in the contract."

Page 15

**Recommended Change:** "The FMTV contractor was submitting vehicle lots for Government acceptance that were not meeting the Government's first inspection acceptance goals, as stated in the memorandum of agreement established between the product manager and DCMA."

**Misstatement:** (Page 14, paragraph 3), Memorandum of Agreement: "The first pass yield is to have 100 percent acceptance of vehicle lots presented during first inspection, as required by the contract system specification."

Page 16

**Recommended Change:** "The first pass yield is to have 100 percent acceptance of vehicle lots presented during first inspection, a target goal as identified in the memorandum of agreement between the product manager and DCMA."

**Misstatement:** (Page 15) "DCMA Actions to Improve Contractor Performance" paragraph 1 "Although the contractor had not met the first pass yield threshold since Feb 2005 and DCMA issued 285 level II corrective action requests in 2006, DCMA did not charge the contractor required reinspection costs until after we announced this audit in July 2006."

Page 17

**Recommended Change:** The contractor had not met the first pass yield threshold since Feb 2005 and DCMA issued 285 level II corrective action requests in 2006. As a result of a significant drop in first pass yield in Jul 06, DCMA added consideration of reinspection charges among many other actions taken to improve contractor performance."

**"B Conclusion** (Page 16): The contractor has not demonstrated the ability to meet the vehicle lot first pass yield rates for final inspection acceptance established in the memorandum of agreement and continued to present nonconforming vehicles for inspection. The daily contractor vehicle production output requirement for FMTV s has more than doubled since the Army received emergency supplemental funds, to a point where the contractor cannot produce quality vehicles. Accordingly, the Program Executive Officer for Combat Support and Combat Service Support needs to have the FMTV Program Office reduce the rate of FMTV s being produced by the contractor until the contractor can produce vehicle lots for first inspection acceptance that at a minimum meet a 95 percent first pass acceptance rate. Also, during the audit, DCMA began taking appropriate actions to get the contractor to improve the quality of vehicle lots presented for final inspection acceptance. Until the contractor begins presenting vehicle lots that meet the 95 percent first pass yield rate, DCMA needs to continue assessing the contractor for costs associated with reinspecting the vehicles."

Page 18

**Comments:** DCMA began taking action to improve contractor quality well before the audit. The essence of the DCMA mission is to provide Government oversight to ensure contract requirements are being met while identifying contractor shortcomings that require improvement. Key daily activities that support the oversight mission are inspections and audits to validate contractor products and processes. As a result of

SUBJECT: The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles (Project Number D2006-D000AE-0225)

these inspections and audits, corrective action reports (CARs) are written that identify any deficiencies and directs the contractor to respond with root cause analysis and implementation of corrective action. As the report indicates, numerous CARs were issued, well before the audit, and cannot be ignored as DCMA actions taken for improving contractor performance. (This documentation was provided to the DODIG previously)

**Misstatement:** (Page 17), Conclusion (continued from page 16), "Also, during the audit, DCMA *began* taking appropriate actions to get the contractor to improve the quality of vehicle lots presented for final inspection."

**Recommended Change:** "Also, DCMA took several actions to get the contractor to improve the quality of vehicle lots presented for final inspection."

**DCMA Comments:** Conclusion B in the report also suggests that DCMA was required to charge reinspection costs and had failed to do that. But FAR 52.246-2 "Inspection of Supplies -Fixed Price" does not require DCMA to charge reinspection costs. It allows the charging of reinspection costs at the discretion of the contracting officer.

#### Conditional Acceptance of Family of Medium Tactical Vehicles

**The following misstatements, recommended changes, and DCMA comments that relate to above finding/recommendation address responsibility for conditional acceptance.**

**DCMA Comment:** Decisions regarding conditional acceptance of vehicles and the withhold amount, if any, are made by the procuring contracting officer, not the administrative contracting officer. Many of the following recommended changes reflect a clarification of this. The procuring contracting officer is with the US Army while the administrative contracting officer is with the Defense Contract Management Agency, which is a separate agency. Only the U.S. Army procuring contracting officer can direct the conditional acceptance of any vehicle under this contract. With the exception of the contract direction to conditionally accept vehicles with a withhold that did not have First Article approval (reference page 8, paragraph 3 "Testing"), the procuring contracting officer directs or authorizes the administrative contracting officer by letter from time to time when to conditionally accept the vehicles and the amount of the withhold, if any. The procuring contracting officer has not delegated the authority to determine conditional acceptance of vehicles or withholds to the administrative contracting officer.

**Misstatement:** (Page 7), "Conditional Acceptance of Vehicles" sentence 2 states, "The administrative contracting officer conditionally accepted.....because the contractor had not met contract vehicle specifications. The administrative contracting officer conditionally accepted the remaining 621 vehicles....."

**Recommended Change:** "The procuring contracting officer authorized conditional acceptance of 1,745 of the 2,366 vehicles because the contractor had not met contract

SUBJECT: The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles (Project Number D2006-D000AE-0225)

vehicle specifications. The procuring contracting officer authorized conditional acceptance of the remaining 621 vehicles because the Army had not provided Government-furnished items to the contractor. "

**Misstatement:** (Page 8, paragraph 1), last sentence states, "In acting on the contractor requests, the administrative contracting officer paid 100%..."

**Recommended Change:** "In acting on the contractor requests, the procuring contracting officer directed that 466 of the 656 out of the original 1,745 vehicles be conditionally accepted and paid at 100% of the vehicle price. The conditional acceptance of the remaining 190 was authorized by the contract which also required that the contractor to bill no more than 90% of the vehicle price. The contractor billed and was paid 100%."

**Misstatement:** (Page 8, paragraph 4), "Nonconforming Parts", 3<sup>rd</sup> sentence states, "The administrative contracting officer conditionally accepted 14 vehicles and did not withhold payments...."

**Recommended Change:** "The procuring contracting officer authorized conditional acceptance of 14 vehicles but did not require a withhold."

**Misstatement:** (Page 8, last paragraph), 1<sup>st</sup> sentence, "The administrative contracting officer conditionally accepted....."

**Recommended Change:** "The procuring contracting officer authorized conditional acceptance of 452 vehicles....."

**Misstatement:** (Page 9), "Engineering Change Proposal Example". "The administrative contracting officer conditionally accepted six vehicles....."

**Recommended Change:** "The procuring contracting officer authorized conditional acceptance of six vehicles ..."

**Misstatement:** (Page 9), "Government-Furnished Items Examples" states, "The administrative contracting officer conditionally accepted ..."

**Recommended Change:** "The procuring contracting officer authorized conditional acceptance of ..."

**Misstatement:** (Page 10), Last paragraph reads, "When the administrative contracting officer conditionally accepted vehicles and did not withhold payment, as required by the FAR, the contractor did not have the incentive to resolve the problems that led to the conditional acceptance. During the audit, the administrative contracting officer recognized the need to withhold payment on conditionally accepted supplies. Specifically, on October 23, 2006, the administrative contracting officer issued a letter to the contractor. The letter stated that the administrative contracting officer would withhold

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Page 12

SUBJECT: The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles (Project Number D2006-D000AE-0225)

10 percent of the payment for 106 vehicles that were previously conditionally accepted and paid in full. The amount to be recouped totaled approximately \$2.2 million. The administrative contracting officer planned to recover the money by deducting the amount from the contractor's Performance-based payments."

**Clarification** The statement above and the one below confuse two distinct types of conditional acceptance as discussed below.

- A) Conditional acceptance prior to first article completion (Attachment 4). When a new FMTV variant is designed and tested, prior to first article approval and before it is fielded, it is conditionally accepted with a 10 percent withhold as stated in Section E.8.2 of the contract. Just like any other vehicle the government accepts, these trucks do not have major non-compliances as they are inspected to the same final inspection criteria as all the other vehicles. They are just waiting for all testing to be complete and then have any changes that result from the testing be put on the trucks before the vehicles are fielded. At the time of the contract this conditional acceptance was anticipated.
- B) All other conditional acceptance actions happened during the period of performance of the contract. In all these cases, identified in the DODIG report, the procuring contracting officer sent a letter authorizing the administrative contracting officer to conditionally accept vehicles and identified the withhold amount if any. If there was a withhold required, it was taken. (This documentation was provided to the IG Team in May 2007)

**Recommended Change:** "The administrative contracting officer conditionally accepted vehicles that had not received First Article approval but did not withhold payments as required by the contract. During the audit, the administrative contracting officer recognized the need to withhold payment on these vehicles. Specifically, on October 23, 2006, the administrative contracting officer issued a letter to the contractor. The letter stated that the administrative contracting officer would withhold 10 percent of the payment for 106 vehicles that were previously conditionally accepted and paid in full. The amount to be recouped totaled approximately \$2.2 million. The administrative contracting officer planned to recover the money by deducting the amount from the contractor's Performance-based payments.

**Misstatement:** (Page 4, paragraph 1), Internal Controls Section. "Specifically the FMTV administrative contracting officer did not adhere to contract provisions when conditionally accepting incomplete vehicles with major nonconformances and paying the contractor up to 100% of the contract price for the vehicles."

**DCMA Comment:** As stated in the above DCMA comment, the vehicles were waiting for first article approval. They did not have any non-compliances nor were they incomplete.

\*The attachment was omitted because of length. Copies will be provided upon request.

SUBJECT: The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles (Project Number D2006-D000AE-0225)

**Recommended Change:** "Specifically the FMTV administrative contracting officer did not adhere to contract provisions by allowing the contractor to bill 100% of the contract price for new FMTV variants that were conditionally accepted while waiting First Article approval."

**Remedy:** To preclude invoicing beyond 90% for vehicles waiting First Article approval, the ACO sent a letter to the contractor's Vice President for Contracts and Supply Chain Management and the Vice President of Finance and to all contracting and all DCMA-MTV contracting personnel as well as its senior leadership, dated 16 Aug 07, Subject: Contract DAAE07-03-C-SO23, Section E.8.2 entitled, "Conditional Acceptance Prior to First Article Approval", repeating the exact language in the contract directing the 10% withhold on vehicles conditionally accepted prior to first article approval. (Attachment 5 and Attachment 6)

**General Administrative Comments.**

- 1) (Page ii Para 1), states "The Director, Defense Contract Management Agency needs to continue charging the contractor for Government reinspection costs, as she began to do in Dec 06."

This appears to be a reference to the administrative contracting officer or should be changed to "he" as the Director of DCMA is a male.

- 2) (Page 2, Footnote 3). This footnote is out of date. It should read, "Although BAE Systems bought out Stewart & Stevenson Tactical Vehicle Systems, LP, (TVSLP) this report will refer to Stewart & Stevenson TVSLP as the contractor."

BAE Systems just acquired Stewart & Stevenson TVSLP but has not changed the name on the government contracts. The name of the contractor should be changed throughout to Stewart & Stevenson TVSLP

\*

Revised

Revised

\*The attachment was omitted because of length. Copies will be provided upon request.

# Department of the Army (Program Executive Office for Combat Support and Combat Service Support) Comments



DEPARTMENT OF THE ARMY  
PROGRAM EXECUTIVE OFFICE  
COMBAT SUPPORT & COMBAT SERVICE SUPPORT  
6501 E. 11 Mile Road  
WARREN, MICHIGAN 48397-5000

SFAE-CSS

10 September 2007

MEMORANDUM FOR Principal Director for Acquisition, Acquisition and Contract Management, Inspector General, Department of Defense, 400 Army Navy Drive, Arlington Virginia 22202-4704

SUBJECT: DODIG Draft Report on The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles (Project No. D2006-D000AE-0225.000)

1. Reference memorandum, Department of Defense Inspector General, 30 July 2007, subject as above.
2. We have reviewed DODIG Draft Report titled "The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles, Project No. D2006-D000AE-0225.000." Our current position is we non-concur to Finding B and Recommendation B.1. pertaining to the "First Inspection Acceptance of Family of Medium Tactical Vehicles."
3. Point of contact for this reply is Ms. Dorine Miller, SFAE-CSS, Comm: 586-574-7689, DSN 786-7689 or email: dorine.miller@us.army.mil.

Encl

  
THOMAS H. BAGWELL, JR.  
Deputy Program Executive Officer,  
Combat Support & Combat Service Support

**Program Executive Office for Combat Support & Combat Service Support (PEO CS&CSS) Reply  
to Department of Defense Inspector General (DODIG) Draft Report,  
The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles  
Project No. D2006-D000AE-0225.000**

**Objectives:** To evaluate whether the Army is adequately protecting the Government's interest when it includes conditional acceptance provisions in production contracts for the Family of Medium Tactical Vehicle Program. To evaluate whether management is cost-effectively producing the Family of Medium Tactical Vehicles as funded in support of the Global War on Terrorism.

**DODIG Conclusion:**

**Finding B – First Inspection Acceptance of Family of Medium Tactical Vehicles**

The FMTV contractor was submitting vehicle lots for Government acceptance that were not meeting first inspection acceptance requirements in the contract. Specifically, Government acceptance of FMTV lots at first inspection decreased from 86 percent in January 2004 to 21 percent in January 2007. As a result, the Defense Contract Management Agency incurred additional reinspection costs to verify that vehicles resubmitted for inspection met contract specifications.

**Additional facts:**

NONE

**RECOMMENDATION**

**For the Program Executive Officer for Combat Support and Combat Service Support to direct the Product Manager Family of Medium Tactical Vehicles to:**

**Recommendation B.1.:** Decrease the daily production output requirement for medium tactical vehicles until the contractor can present vehicles for final inspection acceptance that conform to contract requirements and achieve the first pass yield rates specified in the memorandum of agreement between the Product Manager Family of Medium Tactical Vehicles and the Defense Contract Management Agency.

**Action Taken:**

NON-CONCUR

First pass yield is an internal metric utilized by DCMA Sealy to assist them in ensuring that the quality of the trucks presented to the government for acceptance is maintained. This metric is only one of many metrics used on the FMTV program. More importantly, TVSLP (BAE Systems) continues to meet its monthly and yearly contractual truck delivery requirements to the government. Additionally, vehicles that are being produced and fielded are meeting or exceeding user requirements as evidenced by FMTV's Operational Readiness (OR) Rate of over 93.5 percent. This outstanding OR rate includes FMTVs being utilized in the Global War on Terrorism in Iraq and Afghanistan. Decreasing FMTV production would not be in the best interest of our Army or its soldiers. In accordance with the approved truck modernization strategy the FMTV is replacing the older and much less reliable M-35, M809 and M939 tactical vehicles. The FMTV is also a much safer tactical vehicle and is required to modernize the medium fleet. The FMTV's Low Signature Armored Cab (LSAC) is providing life saving armor protection for our war fighters. Any delay in fielding this vehicle will directly and unnecessarily place Soldiers at risk.

# Department of Army (TACOM Life Cycle Management Command) Comments



REPLY TO  
ATTENTION OF:

AMSTA-CS-CJ

29 August 2007

DEPARTMENT OF THE ARMY  
UNITED STATES ARMY TACOM LIFE CYCLE MANAGEMENT COMMAND  
6501 EAST 11 MILE ROAD  
WARREN, MICHIGAN 48397-5000

MEMORANDUM FOR Principal Director for Acquisition, Acquisition and Contract Management, Inspector General, Department of Defense, 400 Army Navy Drive, Arlington, Virginia 22202-4704

SUBJECT: DODIG Draft Report on the Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles (Project No. D2006-D000AE-0225.000)

1. Reference memorandum, Department of Defense Inspector General, 30 July 2007, subject as above.
2. The TACOM Life Cycle Management Command (LCMC) Internal Review and Audit Compliance Office has reviewed the DODIG Draft Report titled "The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles, Project No. D2006-D000AE-0225.000". We are enclosing the TACOM LCMC's position to the sections of the subject draft report pertaining to the Acquisition Center. Specifically, we concur with Finding A, and recommendations A.1., A.2., and A.3.
3. The TACOM LCMC Internal Review and Audit Compliance Office will track the status of the Acquisition Center's actions and perform a follow-up review to verify that the corrective actions have been completed.
4. Point of contact for this reply is Ms. Kristin Saleh, AMSTA-CS-CJ, Comm: 586-574-5741, DSN 786-5741 or email: kristin.saleh@us.army.mil.

Encl

  
WM W. Pickenheim  
Deputy Chief of Staff

**TACOM Life Cycle Management Command (LCMC) Reply  
to Department of Defense Inspector General (DODIG) Draft Report,  
The Army's Procurement and Conditional Acceptance of Medium Tactical Vehicles  
Project No. D2006-D000AE-0225.000**

**Objectives:** To evaluate whether the Army is adequately protecting the Government's interest when it includes conditional acceptance provisions in production contracts for the Family of Medium Tactical Vehicle Program. To evaluate whether management is cost-effectively producing the Family of Medium Tactical Vehicles as funded in support of the Global War on Terrorism.

**DODIG Conclusions:**

**Finding A – Conditional Acceptance of Family of Medium Tactical Vehicles (FMTV)**

The procuring contracting officer for the FMTV, after consulting with the Project Manager Tactical Vehicles, conditionally accepted incomplete vehicles and paid the contractor up to 100 percent of the contract price for the vehicles. The conditional acceptance of incomplete vehicles resulted in the Army prematurely paying more than \$3.8 million for incomplete vehicles. The procuring contracting officer's practice of conditionally accepting vehicles also unnecessarily increased the Army cost risk. Additionally, the Army's internal controls for the FMTV contract were not adequate and material control weaknesses were identified in the conditional acceptance process used by the procuring contracting officer.

**Additional facts:**

The paragraph at the top of page 8 states in part "Of the 1,745 vehicles, 155 were conditionally accepted for more than one reason, totaling 1,900 reasons for conditional acceptance." We agree that some vehicles were conditionally accepted for more than one reason but believe that the "1,900" is a typographical error.

For clarification purposes, suggest that the first and third sentences of bullet one (Finding A) under the "results" section of the Executive Summary, and any other such references throughout the report (for example, the first paragraph on page 5) be revised to read as follows:

"As was the case more than 11 years ago, the procuring contracting officer for the FMTV, after consulting with the Project Manager Tactical Vehicles, *authorized the administrative contracting officer to* conditionally *accept* incomplete vehicles and *the administrative contracting officer* paid the contractor up to 100 percent of the contract price for the vehicles."

"The procuring contracting officer's *authorization to conditionally accept* vehicles also unnecessarily increased the Army cost risk.

**RECOMMENDATIONS**

**For the Director, TACOM Life Cycle Management Command Acquisition Center to direct that the procuring contracting officer for contract DAAE07-03-C-S023:**

**Recommendation A.1.:** Discontinue the practice of conditionally accepting incomplete Family of Medium Tactical Vehicles for nonconformances of contractor responsibility unless reasons of economy or urgency exist as defined in the Federal Acquisition Regulation.

Revised

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**Action Taken:**

Concur. The Director, TACOM LCMC Acquisition Center will notify the procuring contracting officer to discontinue the practice of authorizing conditional acceptance of incomplete FMTVs for non-conformances of contractor responsibility unless reasons of economy or urgency exist as defined in the FAR are documented.

Target completion: 30 September 2007.

**Recommendation A.2.:** Limit payment to the contractor to 90 percent of the vehicle unit price for conditionally accepted vehicles that have not completed test requirements.

**Action Taken:**

Concur. The Director, TACOM LCMC Acquisition Center will instruct the procuring contracting officer to remind the administrative contracting officer to limit payment to the contractor to 90 percent of the vehicle unit price for conditionally accepted vehicles that have not completed test requirements.

Target completion: 30 September 2007.

**Recommendation A.3.:** Withhold payment of an amount to correct major vehicle nonconformances that were attributable to the contractor as specified in the contract payment terms and the Federal Acquisition Regulation.

**Action Taken:**

Concur. The Director, TACOM LCMC Acquisition Center will instruct the procuring contracting officer that when authorizing conditional acceptance of vehicles with major non-conformances attributable to the contractor to establish an amount, as specified in the contract payment terms and the Federal Acquisition Regulation, to be withheld by the administrative contracting officer to correct the major non-conformances.

Target completion: 30 September 2007.

## **Team Members**

The Department of Defense Office of the Deputy Inspector General for Auditing, Acquisition and Contract Management produced this report. Personnel from the Technical Assessment Directorate and Quantitative Methods Directorate, Department of Defense Office of Inspector General, also contributed to the report.

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# Inspector General Department of Defense

