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Report No. D-2011-049 March 15, 2011

Inspector General

United States Department of Defense

Competition Issues and Inherently Governmental Functions Performed by Contractor Employees on Contracts to Supply Fuel to U.S. Troops in Iraq

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Acronyms and Abbreviations

ASC	Army Sustainment Command
COR	Contracting Officer's Representative
DCAA	Defense Contract Audit Agency
DFARS	Defense Federal Acquisition Regulation Supplement
DFSP	Defense Fuel Support Point
DLA	Defense Logistics Agency
FAR	Federal Acquisition Regulation
FOB	Free On Board
GAO	Government Accountability Office
[redacted]	[redacted]
IOTC	International Oil Trading Company
KBR	Kellogg, Brown, and Root
LOA	Letter of Authorization
LOGCAP	Logistics Civil Augmentation Program
[redacted]	[redacted]
OEF	Operation Enduring Freedom
PGI	Procedures, Guidance, and Information
RO	Responsible Officer
USCENTCOM	U.S. Central Command

INSPECTOR GENERAL
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March 15, 2011

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION, TECHNOLOGY, AND LOGISTICS
COMMANDER, U.S. CENTRAL COMMAND
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Competition Issues and Inherently Governmental Functions Performed by Contractor Employees on Contracts to Supply Fuel to U.S. Troops in Iraq (Report No. D-2011-049)

We are providing this report for review and comment. The report addresses issues Congressman Henry Waxman, the former Chairman of the House Committee on Oversight and Government Reform, raised to the Secretary of Defense relating to the competitions and prices paid under a series of fuel supply contracts awarded to the International Oil Trading Company (IOTC). We also determined the Logistics Civil Augmentation Program contractor performed the inherently governmental function of accepting fuel that IOTC delivered. We considered comments from the Defense Logistics Agency on the draft of this report in preparing the final report.

DoD Directive 7650.3 requires that recommendations be resolved promptly. The comments from the Defense Logistics Agency were partially responsive. Therefore, we request additional comments from the Director, Defense Logistics Agency, on Recommendations A.1, B.1, and B.2 by April 18, 2011.

If possible, please send a .pdf file containing your comments to audacm@dodig.mil. Copies of your comments must have the actual signature of the authorizing official for your organization. We are unable to accept the /Signed/ symbol in place of the actual signature. If you arrange to send classified comments electronically, you must send them over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Please direct questions to Mr. Henry F. Kleinknecht at (703) 604-9324 (DSN 664-9324).

for Richard B. Jolliffe
Assistant Inspector General
Acquisition and Contract Management

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Competition Issues and Inherently Governmental Functions Performed by Contractor Employees on Contracts to Supply Fuel to U.S. Troops in Iraq

What We Did

We initiated this audit to review issues Congressman Henry Waxman, the former Chairman of the House Committee on Oversight and Government Reform raised relating to prices paid on a series of fuel supply contracts awarded to the International Oil Trading Company (IOTC). We reviewed the Defense Logistics Agency (DLA) Energy's decisions to award a series of contracts to IOTC for the delivery of fuel to U.S. troops in Iraq.

What We Found

DLA Energy contracting officers did not perform an adequate proposal analysis for three of four contracts valued at about $2.7 billion that were awarded to the IOTC to supply fuel to U.S. troops in Iraq. The proposal analyses for the three contracts were inadequate because the contracting officer for those contracts:

- primarily used "adequate price competition" as the justification to support price reasonableness even though "IOTC may have reasonably anticipated no competition" because no one else could transport the fuel through Jordan, and
- did not identify that the unusual circumstances of these procurements dictated that some type of cost or pricing data and appropriate field pricing support were needed to support price reasonableness.

As a result, the contracting officer had limited data to support costs for the non-fuel component, such as transportation, of about $1.1 billion and failed to obtain adequate support that the agreed-to fuel prices were fair and reasonable. We calculate that DLA Energy paid IOTC about $160 to $204 million (or 6 to 7 percent) more for fuel than could be supported by price or cost analysis.

In addition, DLA Energy contracting officers inappropriately used the Logistics Civil Augmentation Program (LOGCAP) contractor to accept fuel at three Defense Fuel Support Points located in Iraq. Although a contractor may be used to receive shipments of Government-owned fuel, a contractor may not be used to accept title to fuel on behalf of the Government. The LOGCAP contractor was accepting the fuel because DLA Energy contracting officers did not:

- assign "responsibility for acceptance" to either a contracting officer's representative, a cognizant contract administration office, or another agency;
- adhere to contract terms requiring the use of a DD Form 250 receiving report; and
- negotiate an agreement with the Army Sustainment Command for the Government acceptance of the fuel that IOTC delivered to the contractor-operated fuel sites.

As a result, Kellogg, Brown, and Root (the LOGCAP contractor) accepted the fuel that IOTC delivered for the Government.

Recommendations, Management Comments, and Our Response

We recommend the Commander, DLA Energy obtain some type of cost or pricing data and appropriate field pricing assistance to support the reasonableness of the offerors' proposed prices to supply fuel to contingency operations, and designate and use qualified Government personnel to accept the fuel. The Senior Procurement Executive, DLA, partially agreed with the recommendations, but the proposed actions were not responsive. Therefore, we request additional comments on Recommendations A.1, B.1, and B.2 by April 18, 2011. See the recommendations table on the back of this page.

Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
Commander, DLA Energy	A.1, B.1, and B.2	A.2

Please provide comments by April 18, 2011.

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Management Comments

Introduction

We initiated this project in July 2009 to review issues that Congressman Henry Waxman, the former Chairman of the House Committee on Oversight and Government Reform, raised in an October 16, 2008, letter to the Secretary of Defense relating to prices paid for the fuel delivered under a series of contracts awarded to the International Oil Trading Company (IOTC).

Audit Objectives

Our objective was to review the Defense Logistics Agency (DLA) Energy's decision to award a series of contracts to IOTC for the delivery of fuel through Jordan to U.S. troops in Iraq. Specifically, the audit reviewed whether:

- the fuel needed to be supplied through Jordan,
- an exclusive supply arrangement had an impact on prices, and
- prices paid were fair and reasonable.

In addition, due to conditions identified during our initial fieldwork, we expanded the scope of the audit to include a review of the internal controls related to the receiving, accepting, invoicing, and paying for fuel, as well as an analysis of whether the Army paid for more fuel than it received under the contracts. See Appendix A for a discussion of the scope and methodology and for prior coverage related to these objectives. See Appendices B, C, and D for a copy of Congressman Waxman's letter, a copy of the Secretary of Defense's request that we conduct an independent audit of the contracts, and a discussion of the key issues raised in the Congressman's letter.

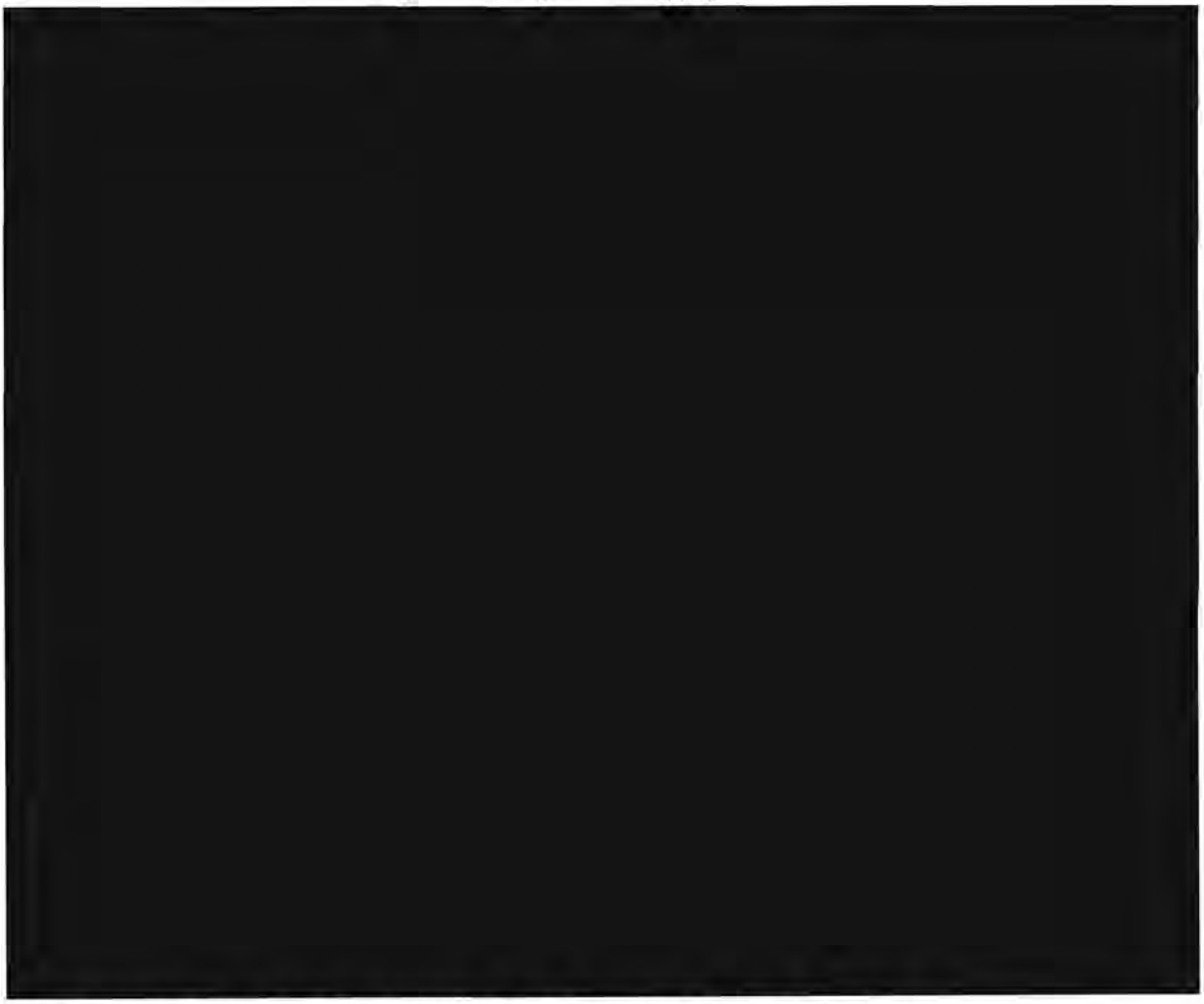
History and Mission of DLA Energy

The origin of DLA Energy dates back to World War II. Originally, it was the Army-Navy Petroleum Board, an entity of the Department of Interior, and it administered the critical petroleum requirements during World War II. In 1945, DLA Energy was transferred to the War Department and became the Joint Army-Navy Purchasing Agency. The Agency underwent several name changes but its mission remained essentially the same until 1962 when it became part of the consolidated military supply organization, the Defense Supply Agency (now known as DLA). The Agency was designated the Defense Fuel Supply Center in 1964 and was the single entity responsible for purchasing and managing DoD's petroleum products and coal. The Defense Fuel Supply Center progressed from a wholesale fuel central procurement activity to a more comprehensive logistics mission as the integrated materiel manager for DoD petroleum products. On February 11, 1998, the Agency was named the Defense Energy Support Center and received the new mission of building an energy program to manage energy products. On July 19, 2010, DLA Energy was given its current name in an effort to clearly identify it as part of DLA. Despite the changes in organizational structure and expanded mission, DLA Energy continues its basic mission of supporting the warfighter and managing DoD's energy sources.

Iraqi Fuel Supply Routes

According to the U.S. Central Command's (USCENTCOM) Joint Petroleum Office, military units operating in Iraq required more fuel to meet their mission requirements, resulting in an urgent need for the fuel supply route through Jordan into Iraq. The Kuwait fuel supply route was already operating at its peak capacity, and due to logistical issues, the quantity of fuel that USCENTCOM could obtain from the North Atlantic Treaty Organization pipeline through Turkey was limited and unreliable. Consequently, the Command needed a third fuel supply route and, due to the political realities of the region, going through Jordan was the only alternative. Figure 1 shows the Kuwait, Turkey, and Jordan fuel supply routes and the estimated daily fuel requirements met by each route.

Figure 1. Iraqi Fuel Supply Routes



Responsibility for Defense Fuel Support Points in Iraq

According to DLA Energy representatives, the Army was having difficulty accounting for its fuel in Iraq and requested assistance from DLA. Therefore, the DLA Director instructed

DLA Energy to manage and oversee the fuel being supplied to the U.S. troops operating in Iraq. During the period covered by IOTC's contracts, DLA Energy was in the process of implementing this action which resulted in IOTC delivering fuel to both capitalized and noncapitalized Defense Fuel Support Points (DFSPs).

Capitalized Sites. The ownership of the fuel inventory at capitalized sites resided with DLA Energy as a part of its Defense Working Capital Fund.

Noncapitalized Sites. The ownership of the fuel inventory at noncapitalized sites resided with the respective Military Service that was managing and overseeing its operations.

DLA Energy used Kellogg, Brown, and Root (KBR), the Army's Logistics Civil Augmentation Program (LOGCAP) contractor, to manage the fuel sites it capitalized, while Service Members managed the sites that had not been capitalized by DLA Energy. Before DLA Energy awarded the Jordan fuel supply contracts, it did not matter whether a contractor operating the fuel sites accepted the fuel, as the fuel being supplied through the other two fuel supply routes was being delivered Free-On-Board (FOB) Origin,[1] where the ownership of the fuel transferred to the Government before its receipt at the DFSPs. However, the fuel supplied under the IOTC contracts was being delivered FOB Destination[2] where ownership did not transfer to the Government until it was accepted by the personnel operating the DFSPs. As a result, DLA Energy needed to ensure that Government employees were present at the capitalized DFSPs to accept the fuel that IOTC delivered on behalf of the Government.

Reasonableness of Fuel Costs Questioned

In October 2003, many members of Congress began raising concerns about KBR's fuel charges. Independent experts also expressed doubts about the reasonableness of KBR's fuel prices, calling them "highway robbery," and noted that they could not reconstruct KBR's prices. In addition, the Defense Contract Audit Agency (DCAA) questioned $106 million of the charges incurred under the contract because KBR did not support the reasonableness of the prices paid for the fuel. DCAA also found that KBR did not demonstrate adequate competition in its Kuwait fuel procurement decision. In that instance, although KBR had received three bids, KBR determined that only one of the providers was qualified to satisfy its requirement because the company was the only supplier licensed by the Kuwait Petroleum Company to procure and distribute petroleum products in Kuwait. Therefore, DCAA concluded that:

- the other offerors' bids were irrelevant because there could not be an expectation of competition when only one supplier was licensed to provide the fuel,

[1] "FOB Origin" means the seller or consignor places the goods on the conveyance. The ownership or title of the goods transfers at the origin and, unless the contract provides otherwise, the buyer or consignee is responsible for the cost of shipping and the risk of loss.

[2] "FOB Destination" means the seller or consignor delivers the goods on the seller's or consignor's conveyance. The ownership or title of the goods transfers at the destination and, unless the contract provides otherwise, the seller or consignor is responsible for the cost of shipping and the risk of loss.

- the procurement did not result in a competitive award and should have been considered a sole-source procurement, and
- KBR should have actively pursued reducing the price for fuel.

Ultimately, on December 30, 2003, DoD relieved KBR of its fuel importation responsibilities.

IOTC's Fuel Contracts

As Table 1 shows, over the last 6 years, DLA Energy issued four fixed-price contracts with economic price adjustment clauses to IOTC for the supply of fuel to the U.S. troops in Iraq through Jordan with an estimated total value of about $3.1 billion.[3]

Table 1. U.S. Central Command's Estimated Fuel Requirements

		Fuel Required (in gallons)			
Contract	**Period of Performance**	**Jet Fuel**	**Diesel**	**Gasoline**	**Contract Value**
SP0600-04-D-0506	Jun 04 - Jun 05	46,280,000	1,722,897	N/A	$359,337,815
SP0600-05-D-0497	Jul 05 - Jun 07	236,250,000	20,150,000	3,079,512	626,145,375
SP0600-07-D-0483	Jul 07 - Aug 09	341,200,000	30,000,000	6,397,500	1,081,175,105
SP0600-09-D-0515	Sep 09 - Feb 10	340,600,000	25,550,000	6,390,500	1,011,173,965
Total		**964,330,000**	**77,422,897**	**15,867,512**	**$3,077,832,260**

The economic price adjustment clauses were designed to eliminate the risk caused by fluctuations in the fuel component of the unit price.

DLA Energy Internal Controls

DoD Instruction 5010.40, "Managers' Internal Control Program (MICP) Procedures," July 29, 2010, requires DoD organizations to implement a comprehensive system of internal controls that provides reasonable assurance that programs are operating as intended and to evaluate the effectiveness of those controls. Although we question the sufficiency of the proposal analyses performed for these contracts, we do not consider the problems identified to have resulted from internal controls weaknesses in DLA Energy's contract award process, but rather judgments made within the contracting officer's authority. However, we did identify internal control weaknesses in DLA Energy's administration of its fuel contracts. Specifically, DLA Energy allowed an IOTC-created fuel delivery and acceptance form to be substituted for the required DD250, "Material Inspection and Receiving Report." The contract language did not ensure that a Government representative accepted title to the fuel. We will provide a copy of the final report to the senior official responsible for internal controls at DLA Energy.

[3] Trigeant, an affiliate company of IOTC, was awarded another fuel delivery contract (contract SP0600-04-D-0490) after DLA Energy terminated a contract it had with the Shaheen Business and Investment Group because the company did not deliver the required fuel.

Finding A. Questionable Competition on Jordan Fuel Supply Contracts

DLA Energy contracting officers did not perform an adequate proposal analysis for three of four contracts valued at about $2.7 billion that were awarded to IOTC to supply fuel through Jordan to U.S. troops in Iraq from July 2005 to February 2010. The contracting officer for the first contract with IOTC should be commended for her proposal analysis techniques and efforts to reduce fuel prices. However, the proposal analyses for the last three contracts were inadequate because the contracting officer for those contracts:

- primarily claimed "adequate price competition" as the justification to support price reasonableness even though "IOTC may have reasonably anticipated no competition,"
- did not include appropriate Federal Acquisition Regulation (FAR) Subpart 15, "Contracting by Negotiation," contract clauses in the solicitations to provide for DCAA audit rights on the noncommercial, nonfuel component of the price, even though the fuel was procured under FAR Subpart 12, "Acquisition of Commercial Items," and
- did not identify that the unusual circumstances surrounding these procurements dictated that some type of cost or pricing data and appropriate field pricing support were needed to support price reasonableness.

As a result, the contracting officer had limited data to support the nonfuel component of price estimated at contract award to be worth about $1.1 billion and did not obtain adequate support that the agreed-to fuel prices were fair and reasonable. We calculate that DLA Energy paid IOTC about $160 to $204 million more (or 6 to 7 percent) more for fuel than could be supported by price or cost analysis.

Guidance

See Appendix E for FAR and Defense Federal Acquisition Regulation Supplement (DFARS) guidance on responsible prospective contractors, pricing policy, adequate price competition, requirements for cost or pricing data, and field pricing assistance.

Proposal Analyses and Price Reasonableness Determinations Can be Improved

#1 – Contracting Officer Could Not Determine the Prices for Contract SP0600-04-D-0506 Were Reasonable

On May 21, 2004, DLA Energy solicited bids for contract SP0600-04-D-0506. The solicitation issued included the following clause that required offerors to submit a letter of authorization (LOA) to demonstrate that the Government of Jordan had authorized them to transport fuel through Jordan before the close of negotiations.

> All offerors must submit [an LOA] from the Jordanian government which permits the contractor to bring fuel through Jordanian territory in transit to Iraq prior to the close of negotiations on June 3, 2004.

IOTC - Only Responsible Offeror. DLA Energy used the lowest price technically acceptable source selection process to evaluate the six offers received in response to the solicitation. All six offers were determined to fall within the competitive range.[4] However, Table 2 shows that IOTC was the only offeror determined to be capable of fulfilling the requirements identified in the contract's solicitation.

Table 2. Responsibility Determination

Offeror	Ability to Satisfy Contract Requirements
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
IOTC	Yes

Price Reduction Efforts. The price negotiation memorandum that the contracting officer prepared for this procurement stated:

> IOTC may have reasonably anticipated no competition and that no other offer could meet the requirements of the solicitation as the Jordanian Ministry of Energy advised IOTC that the Ministry would not issue any additional [LOAs] authorizing the transport of jet fuel for this solicitation. Based on the guidance provided in FAR 15.403-1 (c)(1)(ii)(A) for establishing adequate price competition, the Contracting Officer cannot reasonably conclude that IOTC's offer was submitted with the expectation of competition.

IOTC initially offered to provide the jet fuel for [redacted] per gallon. During negotiations, the contracting officer urged IOTC to lower its price. The contracting officer advised IOTC that the procurement was a competitive action and that it had purchased jet fuel delivered in the region at prices substantially lower than IOTC's offered price in the past. The contracting officer also clarified that the solicitation did not require the use of epoxy-coated trucks, which IOTC was in the process of purchasing with the understanding that their use was required. As a result, IOTC revised its unit price twice from [redacted] to [redacted] and then to [redacted] per gallon.

> *"The contracting officer cannot reasonably conclude that IOTC's offer was submitted with the expectation of competition."*

[4] The competitive range is composed of the most highly rated proposals and is established to convey to the offerors falling within the range that they have a chance of winning and, therefore, encourage them to compete aggressively.

DLA Energy then provided IOTC with price objectives[5] in an estimated price range of $1.49 to $1.51 per gallon. The price objectives were based on current contracts and historical data for fuel movements similar to or the same as delivery through Jordan and included product price, transportation, storage, and testing costs. IOTC provided several reasons for its offer price being well above DLA Energy's price objectives. [redacted] Subsequent to those discussions and after consulting its partner, IOTC again agreed to lower its unit price to $2.10 per gallon [redacted]

In order to further analyze IOTC's $2.10 unit price, the contracting officer requested that IOTC submit a breakdown of the costs that made up its unit price. IOTC submitted the costs, which included [redacted] DLA Energy then had a conference call with IOTC to obtain further insight into the various cost elements. The contracting officer also compared IOTC's unit price to unit prices that the DLA Energy contracting office constructed from prices paid under similar competitively awarded contracts.

[5] The range of prices that the contracting officer considered reasonable based on the prices paid under other fuel delivery contracts in the region.

As Table 3 shows, IOTC's unit price of $2.10 per gallon is significantly higher than the unit prices that DLA Energy constructed from similar competitively awarded contracts.

Table 3. Per Gallon Unit Prices for Jet Fuel

Contractor	IOTC	[redacted] (Constructed)	[redacted] (Constructed)
Product Price	[redacted]	[redacted]	[redacted]
Transportation to Aqaba	---	[redacted]	[redacted]
Net Fuel Price	[redacted]	[redacted]	[redacted]
Transportation to Iraq	[redacted]	[redacted]	[redacted]
Storage at Aqaba		[redacted]	[redacted]
Testing		[redacted]	[redacted]
Demurrage		[redacted]	[redacted]
Jordanian Partners	[redacted]		
Trafigura Participation	[redacted]		
Financing	[redacted]		
Insurance	[redacted]		
Local Operations	[redacted]		
Quality Control	[redacted]		
Miscellaneous	[redacted]		
Profit Margin	[redacted]		
Net Fixed Cost	[redacted]	[redacted]	[redacted]
Total Cost	**$2.1000**	**$1.6480**	**$1.7390**
[redacted]			

The differential between IOTC's final revision and the DLA Energy constructed price was $0.36 ($2.1000 versus $1.7390). In the price negotiation memorandum, the contracting officer stated that although some of IOTC's cost factors were higher than DLA Energy's constructed price, other cost factors, such as transportation, were lower. The contracting officer also noted that IOTC's unit price included several factors [redacted] which would not be experienced by the Government and for which comparable pricing did not exist. Based on those findings, the contracting officer was unable to conclude that IOTC's unit price for jet fuel was reasonable.

After being informed of the situation, USCENTCOM maintained that it had an urgent need for jet fuel sourced through Jordan. As a result, the contracting officer referred the contracting action to the Chief of Contracting, Bulk Fuels, for review and further action by the Center

Senior Procurement Official; this was was followed by a final recommendation for award by the Director, DLA Energy.

[redacted]

#2 - Contracting Officer Determined Prices for Contract SP0600-05-D-0497 Reasonable Based on Conclusion that IOTC's Offer was Submitted with the Expectation of Competition

On March 15, 2005, DLA Energy solicited bids for contract SP0600-05-D-0497. The solicitation included the following clause that required offerors to submit an LOA to demonstrate that the Government of Jordan had authorized them to transport fuel through the country before the close of negotiations on May 18, 2005.

> Offerors importing product(s) into Aqaba must provide a copy of the required Letter of Authorization (LOA) from the Government of Jordan Energy Ministry by May 18, 2005.

IOTC - Only Responsible Offeror. DLA Energy used the lowest price technically acceptable source selection process to evaluate the four offers received in response to the solicitation. All four offers were determined to fall within the competitive range. However, as Table 4 shows, IOTC was again the only offeror determined to be capable of fulfilling the requirements identified in the contract's solicitation.

Table 4. Responsibility Determination

Offeror	Ability to Satisfy Contract Requirements
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
IOTC	Yes

The contracting officer determined IOTC's prices to be fair and reasonable based on his determination that there was adequate competition as defined at FAR 15.403-1 (c)(ii). Specifically, in the price negotiation memorandum, the contracting officer included the following statements to support his determination.

> It was reasonable to expect that two or more responsible offerors, competing independently, would submit offers under the solicitation based on the following: The solicitation was synopsized at FedBizOpps on February 25, 2005 on a full and open basis and after which it was issued on March 15, 2005, and closed on April 11, 2005, a period of 45 days from synopsis to initial closing. Eight firms either registered as interested prospective offerors at the FedBizOpps or contacted the contracting office about this solicitation after it was synopsized and prior to receipt of initial offers, including [redacted] which directly and with an affiliated firm, [redacted] currently has at least one current

> contract with a DLA component in support of US forces in Iraq and has recently had one other contract with DESC [DLA Energy] in support of US forces in Iraq, while offering on other DESC solicitations in the theater. The two prior solicitations for supply of product from Jordan into Iraq (for the requirements of the Iraqi civilian population and for the prior us military requirements) each resulted in the receipt of multiple initial offers, a fact that the IOTC USA was aware of, as their affiliated companies had participated in both solicitations.
>
> Based on the IOTC USA offer received, the contracting officer has concluded and it is considered by the Contracting Officer to a be reasonable conclusion that the IOTC USA offer was submitted with the expectation of competition due to the following circumstances of the offer. IOTC USA's [jet fuel] offered price on this solicitation is [redacted] cents per gallon lower than their current contract price. Both the current [jet fuel] contract price and the IOTC USA [jet fuel] offer are on the identical escalator. The IOTC USA offered price for [jet fuel] is [redacted] per gallon effective March 1, 2005, while their March 1, 2005, [jet fuel] contract [price] is [redacted] per gallon. Another way of making the same comparison is to subtract the awarded price ($2.10 effective January 1, 2004) on the current IOTC USA [jet fuel] contract from the [jet fuel] reference price it was tied to at award [redacted] which results in a margin which is constant over the life of the contract and in this case is [redacted] The same calculation for the IOTC USA offer [redacted] results in a margin of [redacted] **In addition, Mr. Harry Sargeant, an authorized negotiator for IOTC USA, commented during negotiations that he believed that other firms were interested. [emphasis added]**

The rationale that the contracting officer used to support that IOTC submitted its offer with the expectation of competition is questionable. Based on the unusual circumstances surrounding these procurements, it is not reasonable to conclude that IOTC had the expectation of competition just because it was aware that multiple offers had been submitted for the previous two solicitations for the supply of product from Jordan into Iraq. Clearly, the contracting officer for IOTC's first procurement did not come to that conclusion. To the contrary, the contracting officer concluded that IOTC may have reasonably anticipated it had no competition because the Jordanian Ministry of Energy informed the company that it would not issue any additional LOAs authorizing the transport of jet fuel for the solicitation. In addition, that contracting officer was unable to conclude that the $2.10 per gallon award price used to support the reasonableness of the price that IOTC offered for this procurement was reasonable.

The contracting officer for the first contract noted that IOTC's $2.10 unit price included several factors [redacted] that would not be experienced by the Government and for which comparable pricing did not exist. One of those cost factors was the [redacted] fee IOTC paid to [redacted] which holds exclusive rights to transport petroleum through Jordan. [redacted] per gallon in order to fulfill the urgent need of the military to start a fuel supply route through Jordan. Based on information contained in the price negotiation memorandum, [redacted] was only able to provide fuel to fulfill, at most, two-thirds of USCENTCOM's monthly requirement. The remainder of the requirement had to be fulfilled through other sources, [redacted] [6] which at the time of

[6] [redacted]

contract award was offering jet fuel for a significantly lower price of about [redacted] per gallon, a difference of [redacted] per gallon. Presumably, once the supply route was established, IOTC used [redacted] to fulfill USCENTCOM's total fuel requirement. We found that to be the case for contract SP0600-07-D-0483.

#3 - Contracting Officer Determined Prices for Contract SP0600-07-D-0483 Reasonable Based on Conclusion That IOTC Anticipated Other Competitive Offers

On December 15, 2006, DLA Energy issued the solicitation for contract SP0600-07-D-0483. DLA Energy received seven offers in response to the solicitation. DLA Energy switched to the best value source selection process for selecting the source to fulfill the fuel requirements covered by this contract. The solicitation stated that the contract would be awarded to the responsible offeror whose offer conformed to the solicitation and represented the best overall value. The solicitation identified three factors (price, past performance, and technical capability) that the Government planned to use to determine which offer represented the best overall value. The nonprice factors together were significantly more important than price. Table 5 shows the ratings that DLA Energy assigned to the four offerors whose offers were determined to fall within the competitive range.

Table 5. Offerors' Price and Evaluation Ratings

Offeror	Price	Past Performance	Technical Capability	Overall Rating
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
IOTC	$1,370,407,959	[redacted]	[redacted]	[redacted]

On May 3, 2007, based on his integrated assessment of how well the offerors' proposals met the evaluation factors, the contracting officer determined that the fuel and related services proposed by IOTC provided the best overall value and awarded the contract to IOTC.

[redacted]

IOTC - Only Responsible Offeror. [redacted] Therefore, they were unable to satisfy the contract solicitation requirements. Based on that fact, the contracting officer found IOTC to be the only eligible offeror to be awarded the contract.

Table 6. Responsibility Determination

Offeror	Ability to Satisfy Contract Requirements
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
IOTC	Yes.

Price Reasonableness Determination. The contracting officer again determined that IOTC's prices were fair and reasonable based on his determination that there was adequate competition as defined by FAR 15.403-1 (c)(ii). Specifically, the updated price negotiation memorandum that the contracting officer prepared on June 8, 2007, included the following to support the determination that IOTC had submitted its offer with the expectation of competition.

> The solicitation was synopsized at FedBizOpps on December 8, 2006, on a full and open basis. It was issued on December 15, 2006, and closed January 16, 2007. Seven firms submitted initial offers. The three prior DESC solicitations for the supply and delivery of product from Jordan into Iraq (initially for the requirements of the Iraqi civilian population and subsequently for the US military requirements beginning in 2004) all resulted in the receipt of multiple offers. IOTC USA was aware of the competition received on previous solicitations for the fuel requirements from Jordan, as they or their affiliated companies had participated in all prior solicitations. As indicated previously, the small percentage increases (3.7% and 4.7%, respectively) in the prices for [jet fuel] and [diesel], the two largest requirements and the only products for which comparisons between this and the prior solicitations can be made, demonstrate that the proposed prices are reasonable compared to the prices paid previously.

Again, the rationale that the contracting officer used to support that IOTC had submitted its offer with the expectation of competition is questionable.

Contracting Officer Determined that it was in Best Interest of Government to Exercise Option for Contract SP0600-07-D-0483 Rather Awarding New Contract

On October 15, 2007, DLA Energy issued the solicitation for the contract SP0600-07-D-0483 option year-1 competition. DLA Energy received five offers in response to the solicitation. DLA Energy used the best value source selection process to determine whether to exercise the option or to issue a new contract to one of the two offerors determined to fall within the competitive range. The solicitation stated that if a new contract was awarded, it would be awarded to the offeror whose offer conformed to the solicitation and was deemed the most advantageous to the Government, price and other factors considered. The solicitation identified three factors (past performance, price, and plan of operation) that the Government planned to use to determine which offer provided the best value. Price was significantly less important than past performance, and the plan of operation factor was significantly less

important than price. The solicitation also included the following clause requiring offerors to submit an LOA to demonstrate that the Government of Jordan had authorized them to transport fuel through the country prior to contract award.

> An offeror proposing to import any products by ship into Jordan is required to obtain a Letter of Authorization (LOA) from the Government of Jordan's Ministry of Energy and Mineral Resources (MEMR). The Government of Jordan has stated that multiple LOAs can be issued and that an LOA will be issued only for known qualified companies which have good records with MEMR. An offeror must provide a copy of this LOA to DESC prior to contract award.

IOTC - Only Responsible Offeror. [redacted] Therefore, they were unable to satisfy the contract solicitation requirements. Based on that fact, the contracting officer found IOTC to be the only eligible offeror to be awarded the contract.

Table 7. Responsibility Determination

Offeror	Ability to Satisfy Contract Requirements
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]

On February 24, 2008, the contracting officer determined after reviewing the final revised proposals that it was in the best interest of the Government to exercise the existing option under contract SP0600-07-D-0483 rather than to issue a new contract under the solicitation to fulfill USCENTCOM's requirement for fuel routed through Jordan.

Price Reasonableness Determination. The contracting officer considered IOTC's prices fair and reasonable because the option prices were evaluated under the solicitation issued for contract SP0600-07-D-0483, pursuant to FAR 15.404-1(b)(2)(i).

[redacted]

DLA Energy Request for DCAA Audit of Awarded IOTC Contracts. On October 17, 2008, the DLA Energy Director requested DCAA to audit the contracts issued to IOTC to date and stated that he was particularly interested in its conclusions related to the price reasonableness of the contracts. In response to that request, the DCAA Director stated that:

> We are unable to perform the requested audit services because the contract[s do] not contain the contract clause that would permit DCAA access to the contractor's books and records (FAR 52.215-2 Audit and Records-Negotiation). The only access clause in the contract[s] is for the Comptroller General and their designated representative which does not extend access rights to DCAA. By regulation, a firm-fixed price contract for the acquisition of commercial items under FAR Part 12 is not subject to DCAA audit.

Consequently, DCAA is unable to audit contractors' proposals and subsequent contracts unless the solicitation included the appropriate contact clause. Using some type of FAR Part 12 hybrid contract with the appropriate clauses would have precluded these problems. See the DLA Energy Used a Questionable Commercial Item Determination section (on Page 19) for more information.

> *"... the contract[s do] not contain the contract clause that would permit DCAA access to the contractor's books and records . . ."*

In addition, DCAA generally will not accept requests for an audit on price reasonableness after contract award because the prices are already agreed to and an audit would be of little value.

When contracting for both commercial and noncommercial products and services on the same contract, DLA Energy should incorporate FAR Clause 52.215-2, "Audit and Records-Negotiation," in the solicitation to provide for DCAA audit rights for the noncommercial products and services being acquired.

#4 - Contracting Officer Determined Prices for Contract SP0600-09-D-0515 Reasonable Based on Other Questionable Price Comparisons

On December 23, 2008, DLA Energy issued the solicitation for contract SP0600-09-D-0515. DLA Energy received six offers in response to the solicitation. DLA Energy used the best value source selection process to select the source to fulfill the fuel requirements covered by this contract. The solicitation stated that the contract would be awarded to the responsible offeror whose offer conformed to the solicitation and was deemed the most advantageous, price and other factors considered. The solicitation identified three factors (past performance, price, and plan of operation) that the Government planned to use to determine which offer provided the best value. Price was significantly less important than past performance. Plan of operation was significantly less important than price. The solicitation also contained the following responsibility clause:

> (a) An offeror proposing to import any product by ship into Jordan is required to obtain a security clearance [formerly referred to as the LOA] from the Government of Jordan's Ministry of Energy and Mineral Resources (MEMR). An offeror must provide a copy of the approved security clearance issued by MEMR upon the request of the contracting offer and prior to contract award. In addition, an offeror must demonstrate to DESC its capability to provide storage in Aqaba. This capability is subject to review by MEMR....
>
> (b) These requirements are a precondition of award and any offeror who does not meet the requirements will be found non responsible and will be ineligible for award ...

According to the contracting officer, DLA Energy developed the requirements from information that had been obtained from the Ministry of Energy and Mineral Resources. Specifically, a January 22, 2009, letter that the Ministry of Energy and Mineral Resources sent to the U.S. Embassy in Jordan delineated the following requirements that companies had to comply with to use the Port of Aqaba for transporting oil.

[redacted]

In a March 31, 2009, letter, the Secretary General of the Ministry of Energy and Mineral Resources clarified the process for obtaining the security clearance for this contract. Specifically, the Secretary General stated:

[redacted]

IOTC - Only Responsible Offeror. However, as Table 8 shows, IOTC again was the only offeror capable of fulfilling the responsibility requirements identified in the contract's solicitation.

Table 8. Responsibility Determination

Offeror	Ability to Satisfy Contract Requirements
[redacted]	[redacted]
[redacted]	[redacted]
IOTC	Yes

[redacted] IOTC inexplicably raised

the price it offered to supply the required fuel in its Best and Final Offer, while all the other offerors lowered their prices. Table 9 shows IOTC raised the price it offered to supply the required fuel in its Best and Final Offer, while all the other offerors lowered their prices.

IOTC inexplicably raised the price it offered to supply the required fuel for in its Best and Final Offer, while all the other offerors lowered their prices.

Table 9. Offerors' Per Gallon Proposed Fuel Prices

Offeror	Jet	Diesel	Gasoline
Initial Offer			
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
IOTC	[redacted]	[redacted]	[redacted]
Best and Final Offer			
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
IOTC	**$2.75**	**$2.49**	**$1.94**

Price Reasonableness Determination. The contracting officer determined IOTC's prices to be fair and reasonable based on a favorable comparison to the competitively awarded contract prices of the Operation Enduring Freedom (OEF) fuel supply contracts SP0600-07-D-1017, SP0600-08-D-1019, SP0600-08-D-0483, and SP0600-08-D-0484, as well as the prices being paid under IOTC's current contract. Table 10 shows the prices that IOTC offered to supply the fuel for this contract, as well as the contract prices for the various Operation Iraqi Freedom (OIF)/OEF fuel supply programs as of December 1, 2008, that the contracting officer used to support the price reasonableness determination.

Table 10. Per Gallon Fuel Prices Used to Support Price Reasonableness Determination

	Jet	Diesel	Gas
IOTC Proposed	$2.75	$2.49	$1.94
Comparable Contracts			
IOTC's Current Contract	$2.82	$2.72	$2.18
Afghanistan-South (Contract 08-D-0483 and 08-D-0484)	$2.98	$3.21	$2.39
Afghanistan-North (Contract 08-D-1017 and 08-D-1019)	$3.12	$2.53	N/A

In the price negotiation memorandum, the contracting officer stated:

> The competitively awarded, supply of fuel for Afghanistan does, however, provide comparisons to contracts of similar scope and risk to the operation contemplated in Jordan. Afghanistan has no refineries and very limited energy infrastructure, importing most, if not, all of its petroleum-based requirements by truck from sources originating outside the nation. In the Afghanistan programs, the suppliers are not able to rely on any

> US or local government subsidized infrastructure in the distribution chain. The existing infrastructure of terminals, railroads and roads, necessary for deliveries to Afghanistan throughout the regions north and south of it, does not meet Western standards. The transportation involves long distance, multi-day deliveries via trucks and, in the case of deliveries from the north, a combination of rail car, barge and truck movements. The Pakistani refineries and terminals of supply range from 300 miles (Rawalpindi) to 1,250 miles (Karachi) from Kabul via Peshawar. The refineries that supply products from the north range from 960 to 1,400 combined rail and road miles from Kabul. Product from the north is all railed to the northern border of Afghanistan, where it is off-loaded from the rail cars into contractor-provide[d] storage from which trucks are loaded for the remaining 190-mile transfer to Kabul through the Salang Pass and tunnel, the shortest, available route. Product supply from the limited number of refineries closer to Afghanistan in Uzbekistan and Kazakhstan has not been available to the suppliers. In Afghanistan, as is the case in Jordan, all cost and performance risks of these complex, multi-faceted supply and distribution chains necessary for the performance of the contracts, as well as the financing of their entire operations, are borne by the contractors and must be contained in their contract prices. In the case of the Afghanistan supplies from the north, typically 12-18 million gallons of fuel is en route from the refineries to the delivery locations in Afghanistan at any point in time.

We question how comparable the prices paid under the OEF contracts really are to the prices offered to perform under this contract. Although Afghanistan, like Jordan, has limited energy infrastructure and all the costs and performance risk are borne by the contractors, the fuel supply and delivery chains seem to require different levels of effort. The effort required to fulfill the requirements of various OEF fuel supply program contracts seems less involved than what the price negotiation memorandum described as required to successfully perform the Jordanian fuel route requirements. Specifically, the price negotiation memorandum states:

> To supply [the Jordanian fuel route requirements] successfully over the entire length of contract delivery period, the contractor will have to carefully and continually orchestrate its own self-financed, long, complex, multi-faceted logistical fuel supply chain in accordance with the demands of the truck delivery orders placed by the US military. . . . This fuel supply chain must be capable of securing the necessary supplies of products, transporting those products via tanker cargos to Jordan (including paying for the cargos prior to delivering them to Iraq by truck only after which they will receive payment from [DLA Energy]), operating a terminal to receive the tanker cargos and subsequently loading the trucks for the convoys, managing the inventories of the three required products in its storage terminal; inspecting, sampling and testing the products in order to ensure the quality of the fuels throughout their logistics chain; and, arranging, organizing and supporting the large fleet of trucks and drivers needed to meet the schedule of convoys set by the US military escorts, and make the final deliveries from Jordan into Iraq. The estimated contract quantities are the equivalent of just over 35 250,000-barrel tanker deliveries into the contractor's storage terminal facilities over the 28-month delivery period. However, in all likelihood, due to limited storage volumes in the contractor's facilities and varying order quantities among the three products, a significant number of smaller deliveries by tanker will actually be necessary throughout the delivery period in order to continually keep inventories sufficient to complete upcoming convoy orders without suffering any inventory run outs.
>
> The truck convoy orders can consist of up to 2.5 million gallons of fuel (requiring approximately 255 fuel trucks), in addition to the required number of contractor recovery vehicles ("bobtails") at the prescribed ratio of one recovery vehicle for every 18 fuel trucks. A convoy begins crossing into Iraq from Jordan generally every four days under

> the direction of the US military movement control team and escorts and the Jordanian military liaison office at the Karama-Trebil border. The trucks of a single convoy will typically cross the border into Iraq over a two-consecutive-day period. Normally, the convoys are in Iraq for four to five days, travelling from the border to the delivery locations before returning to Jordan. . .

In addition, as Table 11 shows, the quantity of fuel being supplied under the various contracts supporting OEF fuel supply programs is significantly less than the fuel that was estimated to be needed to support the operation contemplated in Jordan under this contract.

Table 11. Annual Fuel Requirements for Jordan and OEF Supply Contracts (gallons)

Contract	Jet Fuel	Diesel	Gas	Total
Jordan	145,971,428	10,950,000	2,738,784	159,660,212
Afghanistan				
SP0600-08-D-1017	64,800,000	N/A	N/A	64,800,000
SP0600-08-D-1019	N/A	4,250,000	N/A	4,250,000
SP0600-08-D-0483	15,000,000	4,250,000	460,000	19,710,000
SP0600-08-D-0484	36,022,500	N/A	N/A	36,022,500

The contracting officer also stated in the price negotiation memorandum that IOTC-proposed prices were lower than what he considered to be the most relevant price guides, IOTC's prior contract prices. Specifically:

> In comparison to the current IOTC contract prices for Jordan, the proposed JP8 [Jet Fuel] price under this solicitation is 7.2137 cents per gallon lower than IOTC's lowest, corresponding JP8 contract price, their offered price of DT2 is 23.1302 cents per gallon lower than their lowest, corresponding DT2 contract price and their MUJ price is 24.8246 cents lower than their current lowest, MUJ contract price. The proposed fixed margin for all three products is [redacted] compared to the lowest margins on the current contract of [redacted] (JP8), and [redacted] (DT2) and [redacted] (MUJ). On the basis of the total estimated proposal value, the proposed award prices are over [redacted] million lower, or 3.1 % lower, than the current contract prices. **IOTC's substantial experience with the unique costs and risks of this operation and the specific market environment in Jordan makes their prior contract prices the most relevant price guides available.** Proposed prices from the two [not responsible] offerors, while lower than IOTC's prices, are not a basis for a reliable comparison with IOTC's prices. Neither of the two [not responsible] offerors has demonstrated experience with the type of work involved with this requirement for managing the complex supply chain necessary to bring fuel from Jordan to western Iraq. **[emphasis added]**

The contracting officer obtained a breakout of the various elements that made up the nonfuel component of IOTC's proposed unit price. The solicitation value for the nonfuel component was about [redacted] million. However, as Table 12 shows, [redacted] and most of the cost elements common to the last breakout that IOTC provided for contract SP0600-04-D-0506 (the first procurement) changed significantly. [redacted] We did not find any documentation in the contract file to indicate that the contracting officer evaluated whether the changes were appropriate. In fact, despite being advised by DCAA before the issuance of the solicitation for this contract that, without the

inclusion of FAR clause 52.215-2, "Audit and Records-Negotiations," DCAA could not access IOTC's books and records to determine the reasonableness of IOTC's costs, the contracting officer still did not incorporate the clause. Instead, the contracting officer stated, in the price negotiation memorandum, that the nature of IOTC's proposed prices "[were] such that they [could] not be validated by the Government."

Table 12. Difference From Previous IOTC Price Breakout (price per gallon)

Nonfuel Cost Element	SP0600-04-D-0506	Proposed for SP0600-09-D-0515	Percent Difference
Transportation	[redacted]	[redacted]	[redacted]
Supply Logistics	---	[redacted]	
Import Licensing	---	[redacted]	
Quality Control and Testing	[redacted]	[redacted]	[redacted]
Port and Custom Fees	---	[redacted]	
Storage	---	[redacted]	
Local Operations/General and Administrative	[redacted]	[redacted]	[redacted]
Financing	[redacted]	[redacted]	[redacted]
Insurance	[redacted]	[redacted]	[redacted]
Profit Margin	[redacted]	[redacted]	[redacted]
Jordanian Partners	[redacted]	---	
Trafigura Participation	[redacted]	---	
Miscellaneous	[redacted]	---	
Subtotal	[redacted]	[redacted]	[redacted]
Unsupported Difference	---	[redacted]	
Net Fixed Cost	[redacted]	[redacted]	[redacted]

Again, we question the appropriateness of using the prices paid on previous IOTC contracts to support a price reasonableness determination for this contract. The reasonableness of the prices paid under all IOTC's previous contracts was based on the prices that the contracting officer for the first contract could not conclude were reasonable.

Contracting Officer Did Not Obtain Cost or Pricing Data to Establish Reasonableness of Offered Prices

The objective of proposal analysis is to ensure that the final agreed-to price is fair and reasonable. The contracting officer is responsible for evaluating the reasonableness of the offered prices. The complexity and the circumstances of each acquisition should determine the level of detail of the analysis required. Generally, when adequate price competition exists, no additional information is necessary to determine the reasonableness of price. However, the contracting officer for IOTC's last three contracts did not identify that the unusual circumstances surrounding the procurements dictated that cost or pricing data from IOTC and appropriate field pricing support were needed to support the reasonableness of the agreed upon prices.

DLA Energy Used a Questionable Commercial Item Determination

The contracting officer for IOTC's last three contracts stated that DLA Energy had not obtained certified cost or pricing data because the fuel and delivery services procured under the Jordan fuel supply contracts were commercial items and, as such, met one of the exceptions that prohibited DLA Energy from obtaining it. We find this conclusion to be questionable. FAR subpart 2.101 requires that for a product or service to be considered commercial, it must be of a type customarily used by the general public or by nongovernmental entities for other than governmental purposes and has:

- been sold, leased, or licensed to the general public;
- been offered for sale, lease, or license to the general public; or
- evolved or been modified from such products or services.

Although the fuel component of the price may satisfy this criterion, there is no commercial market place for the delivery of a billion plus gallons of fuel into a war zone, and we question whether IOTC or any of the other offerors can show data for fuel delivery sales under comparable terms and conditions to commercial customers for nongovernment purposes. Under the circumstances, we believe it would have been more appropriate for DLA Energy to have required the offerors to submit cost or pricing data to support the nonfuel cost elements.

In addition, we believe combining the delivery requirements with the fuel requirements comes very close to constituting the minor modification of a commercial item but that does not change the fuel to a noncommercial item. If combining the fuel and delivery requirements constituted the minor modification of a commercial item, then certified cost or pricing data to support the nonfuel components of the offered price would have also been required. FAR subpart 15.403-1(c)(3)(iii)(C) provides that minor modifications of a commercial item are not exempt from the requirement for certified cost or pricing data if the total price of such modifications exceeds 5 percent of the total price of the contract at the time of contract award. As Table 13 shows, the nonfuel component far exceeded the 5 percent of the total estimated price for all the contracts awarded to IOTC at the time of contract award.

Table 13. Non-Fuel

Contract	Estimated Contract Value	Cost of Non-Fuel Component	Percent
SP0600-04-D-0506	$76,860,000	[redacted]	[redacted]
SP0600-05-D-0497	427,982,385	[redacted]	[redacted]
SP0600-07-D-0483	1,370,407,959	[redacted]	[redacted]
SP0600-09-D-0515	1,011,173,965	[redacted]	[redacted]
Total	**$2,886,424,309**	[redacted]	[redacted]

Therefore, if combining the delivery with the fuel requirements constitutes the minor modification of a commercial item, DLA Energy should have obtained certified cost or pricing data for the nonfuel cost elements.

Contracting Officer Did Not Recognize that Unusual Circumstances Required Additional Cost or Pricing Information be Obtained to Support Price Reasonableness Determinations

At the very least, the contracting officer should have concluded that the unusual circumstances surrounding this series of procurement actions dictated additional cost or pricing information, and field pricing support was needed to determine the reasonableness of the offered prices. According to the DFARS Procedures, Guidance, and Information (PGI) 215.403-3, "Requiring information other than cost or pricing data," when cost or pricing data are not required, the contracting officer must obtain whatever information is necessary in order to determine the reasonableness of the price. FAR subpart 2.101 defines this as "information other than cost or pricing data." When the Truth In Negotiations Act does not apply and there is no other means of determining that prices are fair and reasonable, the contracting officer must obtain appropriate information on the prices at which the same or similar items have been sold previously, adequate for evaluating the reasonableness of the price. Sales data must be comparable to the quantities, capabilities, and specifications of the proposed product or service. Sufficient steps must be taken to verify the integrity of the sales data, to include assistance from the Defense Contract Management Agency, DCAA, and/or other agencies if required.

However, the contracting officer for the last three contracts did not reach this conclusion either. Instead, that contracting officer concluded that no additional support was necessary because multiple offers were received in response to the prior solicitations. Therefore, in the contracting officer's opinion, it was reasonable to conclude that IOTC had submitted its offer with the expectation of competition despite IOTC being the only contractor ever to be found responsible, the existence of indications that IOTC may have known that no other offeror could meet the responsibility requirements contained in the various solicitations, and the fact that all of IOTC's price reasonableness determinations were ultimately based on prices that DLA Energy was unable to conclude were fair and reasonable. In addition, although the contracting officer obtained a breakdown of the various elements that made up IOTC's proposed jet fuel unit price for the last contract, the contracting officer concluded that their nature "[wa]s such that they [could] not be validated by the Government" and never requested any field pricing assistance.

DLA Energy Fuel Prices Tracked to IOTC Fuel Costs

The prices paid for a gallon of fuel under these contracts were composed of two components: the fuel (product) price and a fixed differential (or nonfuel) price. The product prices were periodically adjusted (upwardly and downwardly) to protect the contractor and the Government against significant economic fluctuations in the cost of the various fuels supplied under the contracts. [redacted] We attempted to determine the impact that the unusual circumstances surrounding these procurement actions and the contracting officer's failure to obtain cost or pricing data and field pricing support had on the prices paid under IOTC's contracts.

Product Price. To evaluate the impact on product prices, we compared how much the Defense Finance and Accounting Service paid IOTC for the jet fuel[7] delivered under contract SP0600-07-D-0483 to the amount that IOTC paid its suppliers. In accordance with the economic price adjustment clause contained in the contract, fluctuations in the U.S. Edition of the Platt's Oilgram Price Report, Turbine Fuel Aviation, FOB Mediterranean Basis Italy quotation caused adjustments to the stated contract jet fuel unit price every 15 days. As Figure 2 shows, the adjustments made to the Government's price for jet fuel as a result of the economic price adjustment clause contained in the contract SP0600-07-D-0483 tracked to changes in IOTC's actual cost over the contract's 2-year performance period.

Figure 2. IOTC's Actual Cost for Jet Fuel Tracked to the Price That DLA Energy Paid for the Jet Fuel Delivered

In addition, as Table 14 shows, DLA Energy's total cost for the jet fuel delivered under the contract was about [redacted] more than the amount that IOTC paid its suppliers.

Table 14. Difference Between the Price Paid for Jet Fuel and IOTC Actual Cost

	Gallons	Fuel Cost	Percent Over Contract Price
Contract Price	286,789,441	$717,064,771	
IOTC Cost	286,789,441	[redacted]	
		[redacted]	[redacted]

Thus, the adjustments made to the contract price for jet fuel as a result of changes in the U.S. Edition of the Platt's Oilgram Price Report, Turbine Fuel Aviation, FOB Mediterranean Basis Italy quotation did not result in IOTC being paid significantly more than its actual cost for the fuel component of contract price.

[7] Jet fuel constituted the bulk of the fuel supplied under the contract SP0600-07-D-0483.

Nonfuel Component of Price. It is difficult to assess the reasonableness of the nonfuel component of IOTC's contract prices because DLA Energy did not obtain cost proposals from offerors that separated the costs even though the nonfuel costs represent about [redacted] of the $2.9 billion total estimated value of IOTC's contracts. To evaluate the impact on the nonfuel component of prices, we compared the amount that IOTC was paid above the various products' spot market prices to the amount that was evaluated during the price negotiations for contract SP0600-04-D-0506. As Table 15 shows the nonfuel per gallon price for IOTC's last three contracts ranged from [redacted] that was evaluated during the price negotiations and what appears reasonable based on the constructed prices and may have resulted in IOTC receiving about $160 million more than what could be supported by price and cost analysis.

> *The nonfuel price . . . includes transportation, storage, fees, financing, operations, overhead, and profit.*

Table 15. Nonfuel Costs

	Gallons		Difference from Evaluated Unit Price	
Contract	**Quantity**	**Unit Price**	**Per Gallon**	**Total Value**
Jet Fuel				
SP0600-04-D-0506	46,210,735	[redacted][1]	------	------
SP0600-05-D-0497	230,397,184	[redacted]	[redacted]	[redacted]
SP0600-07-D-0483	285,070,435	[redacted]	[redacted]	[redacted]
SP0600-09-D-0515	33,253,140	[redacted]	[redacted]	[redacted]
	594,931,494			[redacted]
Diesel				
SP0600-04-D-0506	1,722,897	[redacted]	------	------
SP0600-05-D-0497	15,101,490	[redacted]	[redacted]	[redacted]
SP0600-07-D-0483	23,009,515	[redacted]	[redacted]	[redacted]
SP0600-09-D-0515	6,944,257	[redacted]	[redacted]	[redacted]
	46,778,159			[redacted]
Gasoline				
SP0600-04-D-0506	------	[redacted]	------	------
SP0600-05-D-0497[2]	1,637,979	[redacted]	[redacted]	[redacted]
SP0600-05-D-0497[2]	1,299,839	[redacted]	[redacted]	[redacted]
SP0600-07-D-0483	4,310,528	[redacted]	[redacted]	[redacted]
SP0600-09-D-0515	614,391	[redacted]	[redacted]	[redacted]
	7,862,737			[redacted]
Total				[redacted]

[1] Nonfuel unit price that was evaluated during the price negotiations for contract SP0600-04-D-0506.
[2] DLA Energy issued two modifications to contract SP0600-05-D-0497 that purchased gasoline at two different prices.

The price analysis that DLA Energy conducted for contract SP0600-04-D-0506 showed that the nonfuel component of the IOTC jet fuel was [redacted] per gallon. Even though the

contracting officer was unable to determine that IOTC total price was reasonable, the nonfuel component of the price appears in line with the 69 cent per gallon average for the nonfuel cost shown to be associated with the prices constructed from other comparable procurements evaluated (see Table 3), especially after factoring in the [redacted] fee that IOTC paid its Jordanian partners, which then puts IOTC's price just [redacted] than the constructed prices. We also question why the nonfuel fixed costs did not come down on a per unit basis as the estimated contract quantities increased. For instance, jet fuel increased from five to sevenfold over the next three contracts. Often fixed costs, by definition, when spread over a larger base, reduce per unit cost. Without additional data provided such as IOTC's experience and any additional cost associated with its performance on previous contracts, it is hard to justify the increases in the nonfuel component especially in the absence of the expectation of two or more responsible offerors and already having an economic price adjustment existing for the fuel component.

DLA Energy contracting personnel took exception to us using the evaluation of the breakout of nonfuel costs that IOTC provided because they insisted that the prices paid under the Jordan fuel supply contracts were determined to be fair and reasonable based on adequate price competition. Therefore, at DLA Energy's request we also evaluated the nonfuel costs using prices offered by other offerors. As Table 16 shows, the total price paid for the fuel purchased under the IOTC contracts was about $204 million more than what the offerors that appeared most likely to be awarded the contracts would have received were they able to obtain LOAs.

Table 16. Comparison to Other Offerors' Nonfuel Costs

Contract	Quantity (Gallons)	Per Gallon Price		Total Price	
		Other Offeror	IOTC	Other Offeror	IOTC
Jet Fuel					
SP0600-04-D-0506	46,210,735	[redacted]	$2.10	[redacted]	$97,042,544
SP0600-05-D-0497	230,397,184	[redacted]	$2.40	[redacted]	552,953,242
SP0600-07-D-0483	285,070,435	[redacted]	$2.86	[redacted]	815,301,444
SP0600-09-D-0515	33,253,140	[redacted]	$2.75	[redacted]	91,446,135
	594,931,494			[redacted]	**$1,55,743,364**
Diesel					
SP0600-04-D-0506	1,722,897[2]				
SP0600-05-D-0497	15,101,490	[redacted]	$2.35	[redacted]	$35,488,502
SP0600-07-D-0483	23,009,515	[redacted]	$2.88	[redacted]	66,267,403
SP0600-09-D-0515	6,944,257	[redacted]	$2.49	[redacted]	17,291,200
	46,778,159			[redacted]	**$119,047,105**
Gasoline					
SP0600-04-D-0506	N/A				
SP0600-05-D-0497	2,937,818[2]				
SP0600-07-D-0483	4,310,528	[redacted]	$2.73	[redacted]	$11,767,741
SP0600-09-D-0515	614,391	[redacted]	$1.94	[redacted]	1,191,919
	7,862,737			[redacted]	**$12,959,660**
Total				[redacted]	**$1,688,750,129**
Difference				[redacted]	

[1]Average of the best and final prices offered from [redacted]
[2]Added noncompetitively after contract award through two contract modifications. Therefore, there were no competing offers.

Using this approach, it appears that the nonfuel components of IOTC's prices are about $204 million above what the other offerors proposed to charge. As a result, it appears that IOTC received about $160 to $204 million (or 6 to 7 percent) more than can be supported by cost or price analysis.

DLA Energy should have obtained some type of cost or pricing data and field pricing assistance from either DCAA or the Defense Contract Management Agency to support the fair and reasonableness of the offerors' proposed price to deliver fuel to the U.S. troops located in Iraq.

Conclusion

Although numerous companies submitted proposals for the USCENTCOM's Jordan fuel supply requirements, IOTC was only company capable of satisfying the responsibility requirements included in the various solicitations issued for these contracts. Therefore, we disagree that there ever was adequate price competition for these procurements. In addition, although we question DLA Energy's claim that USCENTCOM's fuel delivery requirement is a commercial item, DLA Energy still must evaluate the reasonableness of the offered prices. There were numerous indicators that should have caused the contracting officer to conclude that the unusual circumstances surrounding this series of procurement actions adversely impacted the market forces and dictated that cost or pricing information and field pricing support were needed to determine the reasonableness of the offered prices. This oversight caused DLA Energy to pay IOTC about $160 to $204 million (or 6 to 7 percent) more for the fuel than could be supported by either price or cost analysis.

DLA Energy Management Comments on the Finding and Our Response

Specific Costs and Profit that IOTC Actually Incurred and Realized

The Commander, DLA Energy, stated that the draft report cannot address the allegation that IOTC was a "war profiteer" because the DoD IG did not review the specific costs and profit that IOTC actually incurred and realized.

Our Response

Although we were able to determine that IOTC's fuel costs were in line with the prices DLA Energy paid for the delivered fuel, we were unable to determine whether costs for the nonfuel component were fair and reasonable because the contractor was never required to provide cost or pricing data. Without an auditable cost proposal, it was not possible to effectively identify and evaluate actual costs incurred as they relate to proposed costs for the nonfuel components of the price to determine whether prices were fair and reasonable.

Information Other Than Cost or Pricing Data

The Commander, DLA Energy, stated that the contracting officer should be credited for obtaining "information other than cost or pricing data" for the 2004 and 2009 contracts.

Our Response

Although we did commend the contracting officer for the 2004 contract for her proposal analyses techniques and efforts to reduce fuel costs to meet the urgent need for jet fuel sourced through Jordan, she was unable to determine that prices were fair and reasonable even with the information other than cost or pricing data. This should have indicated to DLA Energy that there would be problems determining price reasonableness on future contracts even with information other than cost or pricing data. In addition, the limited price breakout for the nonfuel component that IOTC provided for the 2004 and 2009 contracts varied significantly as shown in Table 12.

Commercial Item Determination

The Commander, DLA Energy, stated that the fuel on an FOB destination basis for delivery to Iraq was a commercial item. Further, the Commander stated that commercial items are exempt from cost or pricing data and that the FAR definition does not exclude items purchased in or delivered to war zones. The Commander stated that "the determination of whether a product is a commercial item is within the sound discretion of the contracting officer." The Commander further stated that offerors including IOTC had to establish a supply chain that included purchase, transportation, storage, loading, and unloading of the fuel and trucking the fuel to its destination. Finally, the Commander stated that truck transportation was a commercial service in Iraq even during wartime.

Our Response

As stated in the report, we do not believe there is an adequate commercial marketplace where the market establishes prices by the forces of supply and demand for the packaged fuel requirement. The packaged fuel requirement included the fuel products, transportation, storage, loading, and unloading of fuel, and the trucking of fuel through Jordan with a letter of authorization constraint for contract performance for the delivery of more than a billion gallons of fuel into a war zone. As shown in the report, IOTC was the only source that could meet the requirements; therefore, we disagree with the contracting officers' commercial item determination because there was no commercial market supply/demand situation for the packaged requirement to effectively evaluate price reasonableness. Further, by classifying the packaged requirement as a commercial item, the contractor was not required to provide cost or pricing data, and DCAA was unable to provide necessary audit assistance to support price reasonableness.

Price Analysis

The Commander, DLA Energy, stated the draft DoD IG report incorrectly states that DLA paid $160 to $240 million more to IOTC than could be supported by a price analysis. The Commander also stated that using the lower proposed competitive prices was not appropriate because the contracting officer determined the other offerors were not capable of performing the contract and that IOTC cooperated with congressional investigators who concluded that IOTC's profits over the duration of the contract "may have been 14 percent."

Our Response

We used two reasonable approaches to determine how much of the fuel costs were supported by price analysis. It should also be noted that the original LOGCAP contractor received a maximum profit of 7 percent on its costs that it incurred for purchasing and supplying fuel to the U.S. troops in Iraq in the early phases of combat operations. In addition, Chairman Waxman, Committee on Oversight and Government Reform, U.S. House of Representatives considered those fuel costs exorbitant.

Recommendations, Management Comments, and Our Response

A. We recommend the Commander, Defense Logistics Agency Energy, require contracting officers:

1. When contracting for both commercial and noncommercial products and services on the same contract, incorporate Federal Acquisition Regulation clause 52.215-2, "Audit and Records-Negotiation," in the solicitation issued to provide for Defense Contract Audit Agency audit rights for the noncommercial products and services being acquired.

DLA Energy Comments

The Commander, DLA Energy, partially agreed. The Commander stated it was DLA's practice and policy to include audit rights clauses for all products and services determined to be noncommercial, but disagreed that any of the products and services procured under IOTC's contracts were noncommercial items.

Our Response

Although the Commander partially agreed, the comments are nonresponsive. By classifying the packaged fuel requirements as a commercial item, DLA Energy is unable to obtain cost or pricing data and the audit assistance necessary to support the reasonableness of the agreed-to prices. We request that DLA Energy reconsider its position on the recommendation and provide additional comments in response to the final report on the commercial marketplace that exists for the complete packaged fuel supply requirements as described in our response to DLA Energy's comments on its commercial item determination.

2. Obtain appropriate cost or pricing data and necessary field pricing assistance to support price reasonableness determinations for proposed fuel prices in a contingency operation environment when competition is questionable and a comparable commercial market does not exist.

DLA Energy Comments

The Commander, DLA Energy, partially agreed. The Commander stated that DLA would issue policy in January 2011 to implement agency-wide the provisions of the Defense Procurement and Acquisition Policy Memorandum, "Improving Competition in Defense Procurements,"

November 24, 2010. The Commander further stated that DLA has placed a renewed focus on obtaining the information needed to ensure that contract prices were fair and reasonable consistent with Under Secretary of Defense for Acquisition, Technology, and Logistics Memorandum, "Better Buying Power: Guidance for Obtaining Greater Efficiency and Productivity in Defense Spending," September 14, 2010.

Our Response

Although the Commander, DLA Energy, partially agreed, and issued the policy memorandum on January 3, 2011, the proposed actions meet the intent of the recommendation, and no further comments are required. However, if DLA Energy makes the determination that the packaged fuel supply requirement fulfilled under these contracts is a commercial product or service, then DCAA cannot audit prospective offerors' cost proposals to support any price reasonableness determinations. See our response to DLA Energy's comments on its commercial item determination.

Finding B. Contractor Acceptance of Fuel is an Inherently Governmental Function

DLA Energy contracting officers inappropriately used KBR, the Logistics Civil Augmentation Program (LOGCAP) contractor, to accept about $859.8 million of fuel at Defense Fuel Support Points at Al Asad, Al Taqaddum, and Victory Base Complex in Iraq. This occurred because the DLA Energy contracting officer did not:

- assign "responsibility for acceptance" to either a contracting officer's representative (COR), a cognizant contract administration office, or to another agency;
- adhere to contract terms that required the use of a DD Form 250, "Material Inspection Receiving Report," to accept fuel by Government representatives; and
- negotiate a memorandum of agreement with the Army Sustainment Command (ASC) for the Government acceptance of the fuel that IOTC delivered to the DLA Energy fuel support points being operated by KBR under the LOGCAP contract where the Army thought the fuel supplied by IOTC was Government property.

As a result, KBR was allowed to accept fuel under the LOGCAP contract, an inherently governmental function. Our reconciliation of the records for two of those fuel support points identified only minor variances between the quantity of fuel accepted by KBR and the quantity of fuel that IOTC was paid for; however, fuel is a high-risk commodity, analogous to cash, requiring stringent control procedures.

Guidance

See Appendix E for FAR and DFARS guidance on acceptance, contracting officer's representative's responsibilities, and inherently governmental functions.

DLA Energy Used IOTC Contracts to Supply Fuel Through Jordan to Various Locations in Iraq

According to DLA Energy representatives, the Army was having difficulty accounting for its fuel in Iraq and requested assistance from DLA. To fulfill that request, the representatives stated that the Director, DLA, instructed DLA Energy to provide management and oversight for the fuel being supplied to the U.S. troops operating in Iraq. For the period covered under contract SP0600-D-07-0483 (July 2007 to August 2009), DLA Energy had capitalized (or taken over the ownership of) the fuel located at three Defense Fuel Support Points. According to information extracted from the Defense Finance Automated System, the Defense Finance and Accounting Service paid IOTC more than $1.1 billion to deliver fuel to various locations in Iraq under that contract.

As Table 17 shows, more than 75 percent of the fuel (by dollars) was delivered to fuel support points where the responsibility for the ownership of the fuel had already transferred to DLA Energy.

Table 17. Percent of Fuel Delivered to Each Type of Site Under Contract SP0600-D-07-0483

Type of Site	Fuel Cost	Percent
Capitalized		
Al Asad	$599,717,364	
Al Taqaddum*	204,784,936	
Victory Base Complex	55,310,121	
Subtotal	**859,812,421**	**76.8**
Noncapitalized		
Al Taqaddum*	225,690,836	
Korean Village	33,171,691	
Trebil	641,755	
Subtotal	**259,504,282**	**23.2**
Total	**$1,119,316,703**	**100.0**
*DLA Energy capitalized Al Taqqadum on June 1, 2008.		

Contractor Employees Performed Inherently Governmental Functions

DLA Energy used KBR, the LOGCAP contractor, to manage its capitalized Defense Fuel Support Point operations. ASC provides a wide range of logistics support to DoD's combat operations including field support, materiel management, Army pre-positioned stocks, and contingency contracting. At DLA Energy's request, ASC tasked KBR to manage the fuel support points that DLA Energy capitalized in Iraq. Specifically, KBR provided the following support at the DLA Energy-capitalized Defense Fuel Support Points as a part of the tasks it performed under contract DAAA09-02-0007 task orders 139 and 159.

> 9.7. CLASS III BULK (B) OPERATIONS. **The contractor shall establish, operate, and maintain 24 hours a day 7 days a week, a Class III (B) supply point** consisting of fabric collapsible tanks or above-ground hard wall storage tanks physically capable of receiving, storing, (on the ground) and issuing [fuel]...**The contractor shall manage Class III Bulk sites in country and shall perform quantity accountability and determinations on all transfers, receipt, storage, and issue of product IAW [in accordance with] DoD4140.25 and DESC Interim Policies and Instructions.**
>
> 9.7.1.1. **The contractor shall sample and test all Tank Truck (TT) receipts from DESC Direct Delivery (PC&S) and Bulk Delivery contracts prior to off-loading products, using appropriate equipment and methods,** IAW MIL-STD-3004A, *Quality Surveillance for Fuels, Lubricants, and Related*

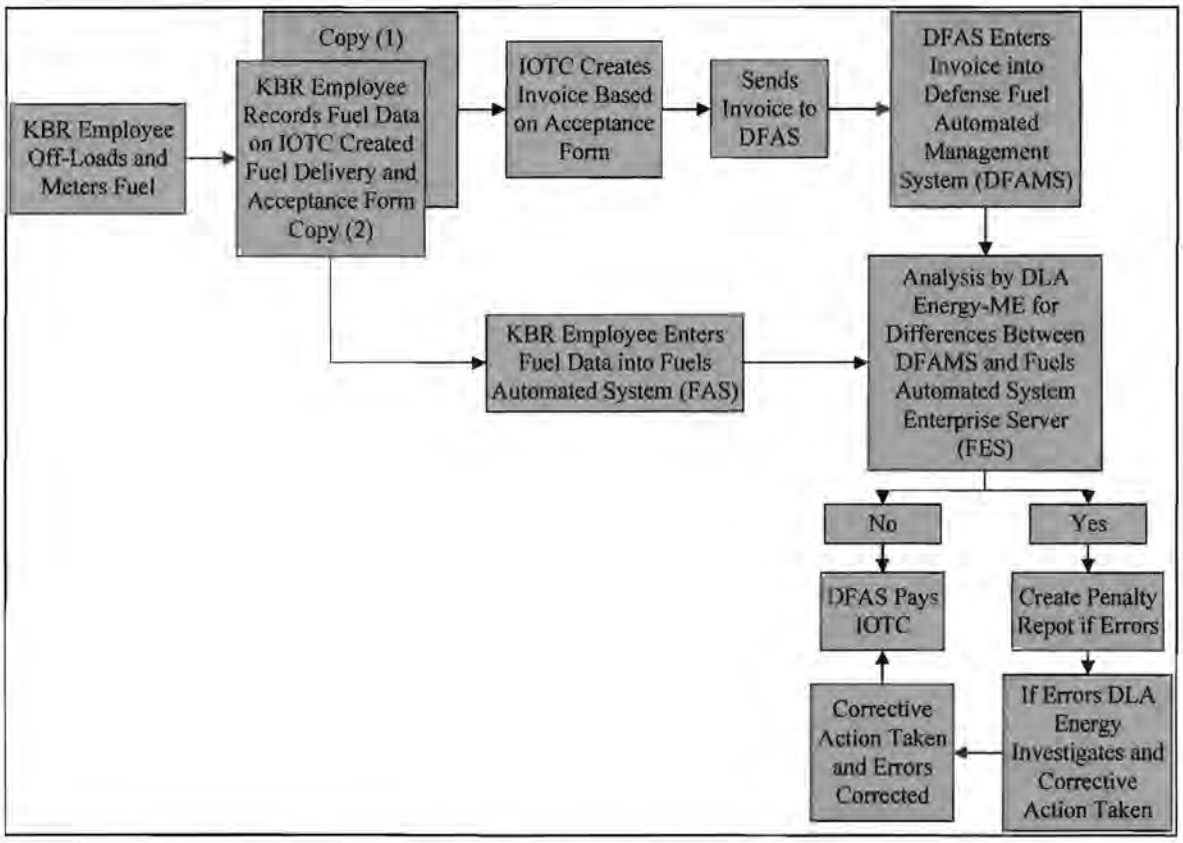
Products, applicable Defense Energy Support Center (DESC) and Army regulations and standards. **The contractor shall meter fuel while off-loading**

. . . . . .

9.7.1.3. **The contractor shall accept product deliveries when test results are within contract specification limits, or Intra-Governmental Transfer Limits if transferred from Government owned stock, without further delaying discharge. [emphasis added]**

As Figure 3 shows, DLA Energy contracting officers inappropriately used KBR, the LOGCAP contractor, to accept the fuel that IOTC delivered to three Defense Fuel Support Points that DLA Energy capitalized. Accepting fuel is an inherently governmental function.

Figure 3. DLA Energy Capitalized Fuel Support Points: Acceptance and Payment Process



Under the terms of its task orders, KBR tested all fuel delivered prior to its off-loading using appropriate equipment and methods. If a product did not meet specifications, the vendor delivery was rejected. If the product met specifications, KBR metered and recorded the fuel off-loaded from IOTC's tanker trucks on an IOTC-created fuel delivery and acceptance form.[8]

[8] See Appendix G for copy of the IOTC-created fuel delivery and acceptance form used to accept fuel.

IOTC created and sent its invoices from the first copy of the form to the Defense Finance and Accounting Service where it was entered into the Defense Fuel Automated Management System. A KBR employee entered the quantity of fuel accepted from a second copy of the form into the Fuels Automated System, which fed the fuel receipt data through the Fuels Automated System Enterprise Server to the Defense Fuel Automated Management System to certify the accuracy of IOTC's invoices. The KBR employee then forwarded the form to DLA Energy-Middle East. The Defense Finance and Accounting Service payment system automatically made payment to IOTC for all invoices whose data matched the information entered by the KBR employees. A Penalty Report was created showing the invoices whose data failed to match the information input by KBR. A DLA Energy-Middle East employee investigated and corrected the issues that caused the discrepancies. After the corrective measures were implemented and fuel acceptance data matched the invoices, the Defense Finance and Accounting Service paid IOTC.

Accepting fuel is an inherently Governmental function.

To assess the accuracy of the fuel receipt data that KBR entered into the Fuels Automated System, we compared the quantity of fuel that the End-of-Month Operating Gain/Loss Computation Report showed that Al Asad and Al Taqaddum received each month to the quantities that the Defense Fuel Automated Management System showed that IOTC was paid for. As Table 18 shows, we found less than 1 percent difference between the quantity of fuel that the report showed KBR received versus the quantity of fuel that IOTC was paid for.

Table 18. Quantity of Fuel Purchased Compared to the Quantity of Fuel Accepted

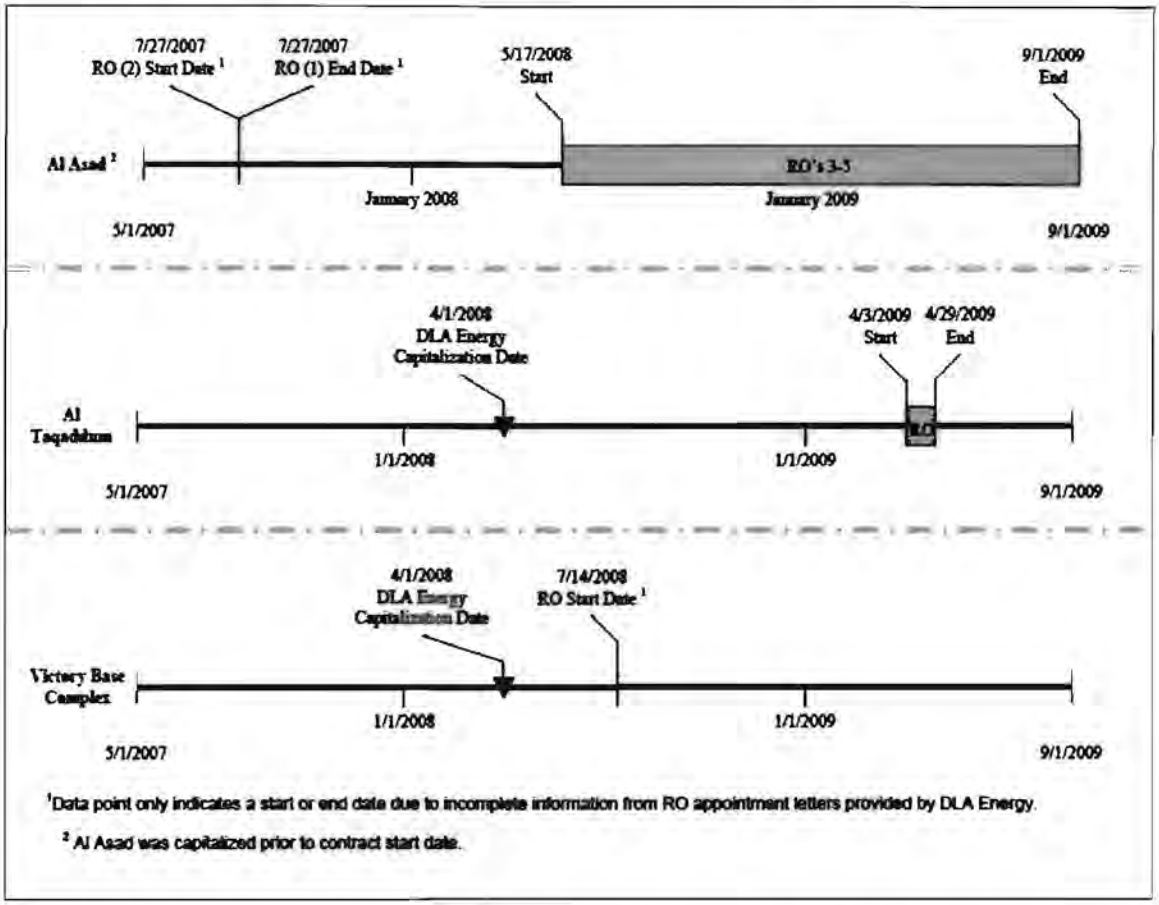
	Gallons		Difference	
	Received	Purchased	Amount	Percent
Al Asad				
Jet Fuel	147,875,337	147,823,181	52,156	.0004
Diesel	7,658,309	7,606,212	52,097	.0068
Gasoline	2,317,010	2,307,524	9,486	.0041
Al Taqaddum				
Jet Fuel	33,865,620	33,896,778	(31,158)	(.0009)
Diesel	2,927,482	2,938,548	(11,066)	(.0038)
Gasoline	535,316	535,224	92	.0002
Total	**195,179,074**	**195,107,467**	**71,607**	**.0004**

Contracting Officers Neglected Responsibility for Fuel Acceptance

DLA Energy contracting officers neglected their "responsibility for acceptance." They did not accept IOTC's fuel themselves, designate qualified individuals to act as their authorized representatives to accept the fuel, or assign the responsibility to a cognizant contract

administration office or ASC, the organization that issued the LOGCAP contract. The contracting officers chose to retain the contract administration function for the Jordan fuel supply contracts and stated that the responsible officers (ROs) managing the energy accounts at the fuel support points that DLA Energy capitalized were accepting the fuel delivered by IOTC. However, we did not find any documentation in the contract file to corroborate that the contracting officers had delegated that authority to the ROs. In addition, even if the responsibility for accepting fuel had been properly assigned to the ROs, duly appointed ROs were not always present at the fuel support points that DLA Energy capitalized (see Figure 4).

Figure 4. Timeline of Responsible Officer Appointments



DLA Energy appears to be confusing the difference between receiving and acceptance. DLA Energy Policy Number DESC-P-7, "Accountability and Custodial Responsibilities for Defense Working Capital Fund (DWCF) Inventory and Government Property," states that ROs "provide diligent care, custody, and protection of Government property," but they do not accept property for the Government. ROs could have been used to accept IOTC's fuel, if they met all of the COR requirements and were appointed and specifically authorized to perform that task by the contracting officer. However, as stated previously, we found no documentation to support that the contracting officers had delegated that authority to the ROs. Further, the acceptance documentation for the 197 deliveries made to Al Taqaddum between

May 2008 and February 2009 did not support that the ROs actually accepted the fuel delivered by IOTC.

Based on the information that was shown on the IOTC fuel delivery and acceptance forms, KBR accepted IOTC's fuel on behalf of the Government. The only information shown on the forms was the detailed data relating to the fuel off-loaded from IOTC's tanker trucks, a KBR employee signature and badge number, and a stamp verifying the authenticity the form. No Government representative validated the accuracy of data that the KBR employees recorded despite it being used to validate the accuracy of the invoices submitted by IOTC for payment. According to DLA Energy personnel, DLA Energy never established a process to verify that the ROs were performing the acceptance function at capitalized fuel supply points.

Our reconciliation of the fuel acceptance and payment records for two of those sites did not identify a significant variance between the quantity of fuel accepted by KBR and the quantity of fuel that IOTC was paid for; however, fuel is a high-risk commodity, analogous to cash, requiring stringent quality control procedures.

If DLA Energy is going to use ROs at its capitalized fuel sites to accept fuel delivered FOB Destination, its contracting officers need to designate and authorize those individuals to perform those tasks in writing and ensure that they are qualified and receive the requisite training to perform those tasks.

Contract Requirements for Fuel Acceptance Not Followed

DLA Energy contracting officers did not adhere to contract terms that required DD Form 250, "Material Inspection Receiving Report," be used to accept the fuel delivered under contract SP0600-D-07-0483. Even though the contract included the following clauses that require the use of DD Forms 250, the contracting officer allowed an IOTC-created delivery and acceptance form to be substituted to accept fuel.

> **E40 Material Inspection and Receiving Report (MAR 2003)**
>
> **(a) At the time of each delivery of supplies or services under this contract, the Contractor shall prepare and furnish to the Government a material inspection and receiving report [Form DD 250] in the manner and to the extent required by Appendix F, Material Inspection and Receiving Report, of the Defense FAR Supplement.**
>
> . . . . . .
>
> **G150.05 Submission of Invoices for Payment – Commercial Items (Bulk) (DESC APR 2006)**
>
> (a) Certification of Receipt.
> (1) F.O.B. Destination Deliveries.
>
> **(i) The Quality Representative (QR) or authorized receiving activity personnel will certify the receipt and forward three copies to the appropriate paying office.** If the receiving activity is not a U.S. organization, the authorized U.S. representative, as indicated in the SIOTH, will certify and distribute the receiving documents. One of the copies of the receiving report submitted for payment must contain the original signature of the QR and will have the following information stamped, printed, or typed on it:

"ORIGINAL RECEIVING REPORT FOR PAYMENT OF INVOICE". **The receiving report must be signed by the QR to certify acceptance of the product prior to submission of the receiving report to the paying office.**

(ii) The receipt for f.o.b. destination fuel may be one of the following documents:

(A) The DD Form 250, Material Inspection and Receiving Report; (Emphasis Added)

. . . . . .

DFARS Appendix F states the DD Form 250 is a multi-purpose report used:

(1) To provide evidence of Government contract quality assurance at origin or destination;
(2) To provide evidence of acceptance at origin or destination;
(3) For packing lists;
(4) For receiving;
(5) For shipping;
(6) As a contractor invoice; and
(7) As commercial invoice support.

The contractor prepares the MIRR, except for entries that an authorized Government representative is required to complete. The contractor shall furnish sufficient copies of the completed form, as directed by the Government representative. **[emphasis added]**

Had DLA Energy adhered to the contract terms that required DD Forms 250 be used to accept fuel, the ASC should have detected that the KBR was inappropriately performing an inherently government function by accepting the fuel delivered by IOTC. The DD Form 250 would have shown the fuel shipment terms were FOB Destination and that Government acceptance was required. In addition, the DD Form 250 has a clearly defined place for a Government representative at the destination point to certify acceptance of the fuel. See Appendix H for a copy of a DD Form 250, "Material Inspection Receiving Report."

DLA Energy needs to comply with the acceptance documentation requirements identified in its contracts.

DLA Energy and Army Sustainment Command Did Not Establish a Memorandum of Agreement

DLA Energy contracting officers also did not negotiate a memorandum of agreement with ASC for the Government acceptance of the fuel being supplied by IOTC as FOB Destination at the DLA Energy fuel support points being operated by KBR. ASC representatives stated the Command believed that all the fuel that DLA Energy was supplying was already owned by the Government. The task order statement of work required the Government to furnish the fuel to KBR as government-furnished property. Specifically, Section 3.5 of task order's statement of work states:

3.5. The Government will furnish the following equipment or material as GFE [Government Furnished Equipment]/GFM [Government Furnished Material]/GFP [Government Furnished Property], or other GFE/GFM/ or GFP as available.

3.5.1. Fuel. (JP8 [Jet Fuel], Jet-A1 [Jet Fuel], DF2 [Diesel], and MOGAS [Gas]) [emphasis added]

Based on that clause, the ASC representatives stated that they believed IOTC's fuel was being delivered FOB Origin where its ownership had already transferred to the Government and KBR was just receiving government-furnished property, as was the case with the fuel DLA Energy was providing through its Kuwait and Turkey fuel supply routes. Further, they were unaware that DLA Energy was relying on KBR's metering of IOTC's fuel deliveries for accepting IOTC's fuel for the Government. DLA Energy should have informed ASC that the fuel supplied under IOTC's contracts were FOB Destination and entered into a memorandum of agreement that required Government employees be used to accept the fuel delivered by IOTC.

Conclusion

Contractor surveillance by contracting personnel under contingency conditions may be difficult due to ongoing military operations, local threat conditions, remote location, broad customer base, and the performance and delivery time involved. DLA Energy's contracting officers were responsible for deciding if they needed an individual to serve as their authorized representative and should have delegated specific authority to a COR to perform the acceptance function. Although a contractor may be used to receive shipments of Government-owned fuel, it may not be used to accept title on behalf of the Government.

Although a contractor may be used to receive shipments of Government owned fuel, it may not be used to accept title on behalf of the Government.

It is important to establish a properly trained cadre of CORs within the organization's major customers supported. CORs are qualified individuals appointed by the contracting officer to assist in the technical monitoring or administration of a contract. Contracting officers are responsible for deciding if they need an individual to serve as their authorized representative. Contracting officers must delegate specific authority to the COR to perform the technical or administrative functions needed to ensure that the contractor provides quality products and services according to their contracts. Contracting officers should work closely with requiring activities to ensure the activities nominate individuals to serve as CORs who have the essential qualifications to effectively perform the assigned functions.

Recommendations, Management Comments, and Our Response

B. We recommend that the Commander, Defense Logistics Agency Energy, require that contracting officers:

1. When using Free-On-Board Destination-type contracts at contractor-run Defense Logistics Agency Energy capitalized fuel support points, either appoint a contracting officer's representative to perform the acceptance function, assign the responsibility to the Defense Contract Management Agency, or enter into a documented

agreement with the organization overseeing the fuel support point contractor that requires that only Government employees accept the fuel.

DLA Energy Comments

The Commander, DLA Energy, partially agreed. The Commander recognized that acceptance is an inherently governmental function, but disagreed DLA had control over the fuel receipt function in Iraq. The Commander stated that in the case of IOTC's contracts, the Army, not DLA, made the decision to rely on the Army support contractor to receive fuel. The Commander further stated that DoD Directive 4140.25, "DoD Management Policy for Energy Commodities and related Services," April 12, 2004, places substantial responsibility for receipt of fuel on the combatant commanders and the Military Services. The Commander added that DLA is currently examining options for ensuring compliance with the requirement that fuel acceptance be performed by Government personnel and will take steps to ensure that, when Government personnel are designated to perform the acceptance function, it is Government personnel performing that function and not contractor personnel.

Our Response

Although the Commander, DLA Energy, partially agreed, the comments are nonresponsive. DLA Energy is confusing the requirements for receipt of Government-owned fuel with accepting title or taking ownership of the fuel on the behalf of the Government from a contractor. The FAR governs the Government's acceptance or rejection of contractor products and services and places this responsibility solely on the contracting officer. DoD Directive 4140.25, section 5.1.8.1, identifies DLA as the organization that is responsible for petroleum integrated-materiel management including: procurement, transportation, ownership, accountability, budgeting, quality assurance, and quality surveillance. Sections 5.4.2, 5.4.5, and 5.5.1 cited by the Commander only discuss the receipt of Military Service and DLA-owned fuel, not its acceptance. Therefore, it was logical for the Army to believe the fuel that IOTC was delivering had already been accepted by DLA Energy personnel and was Government-owned property. We request that DLA Energy provide additional comments in response to the final report on the steps its contracting officers will take to comply with the acceptance requirements outlined in the FAR and ensure that only Government personnel duly appointed by the contracting officer perform the acceptance function when using Free-On-Board-Destination-type contracts at contractor-run DLA Energy-capitalized fuel support points.

2. Develop procedures to ensure that the acceptance documentation requirements identified in its contracts are complied with.

DLA Energy Comments

The Commander, DLA Energy, agreed and stated that DLA will ensure that future solicitations reflect receipt and acceptance procedures in effect during the performance of the contract.

Our Response

Although the Commander, DLA Energy, agreed, the comments are nonresponsive. They do not address the specific procedures that will be developed and used to ensure that the fuel

acceptance documentation requirements identified in DLA Energy's fuel supply contracts are complied with during contract performance. We request the Commander provide additional comments in response to the final report that describe the specific procedures that will be used to ensure that the fuel acceptance documentation requirements identified in DLA Energy's fuel supply contracts are complied with during contract performance.

Appendix A. Scope and Methodology

We conducted this performance audit from July 2009 through September 2010 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.

Our review focused on DLA Energy's decision to award IOTC a series of contracts for the delivery of fuel through Jordan to U.S. troops in Iraq. Specifically, we determined whether prices paid were fair and reasonable, whether an exclusive supply arrangement had an impact on prices, and whether the fuel needs to be supplied through Jordan. During our initial fieldwork, we discovered conditions that caused changes in our audit objectives. The conditions discovered prompted us to perform a review of the internal controls related to the receipt, acceptance, invoicing, and payment process and procedures for the delivery of fuel. The team also gathered and reviewed documentation concerning the four fixed-price fuel supply contracts that DLA Energy issued to IOTC from June 2004 to February 2010 with an estimated total value of about $3.1 billion from the following organizations:

- Defense Finance and Accounting Service (Columbus, Ohio),
- Defense Logistics Agency (Fort Belvoir, Virginia),
- DLA Energy – Retail Management Division (San Antonio, Texas),
- United States Central Command Joint Petroleum Office (MacDill AFB, Florida),
- DLA Energy – Middle East (MacDill AFB, Florida), and
- Army Sustainment Command (Rock Island, Illinois).

Last, we met with representatives of IOTC to obtain pricing data for fuel supplied under DLA Energy contract number SP0600-07-D-0483.

Use of Computer-Processed Data

We used computer-processed data produced by from the Defense Finance and Accounting Services Defense Fuel Automated Management System. We used the data to determine whether IOTC was being paid the correct amount for fuel that they delivered. To verify the reliability of that information, we compared the amount paid to IOTC in the Defense Fuel Automated Management System to the amounts on the IOTC payment vouchers. Nothing came to our attention as a result of performing these comparisons that caused us to doubt the reliability of the computer-processed data obtained from the Defense Fuel Automated Management System. Therefore, we determined that the data were sufficiently reliable for the purposes of our report.

Prior Coverage

The Department of Defense Inspector General (DoD IG), DCAA and GAO have issued three reports discussing internal controls over payments made in Iraq and fair and reasonable pricing of fuel. Unrestricted DoD IG reports can be accessed at http://www.dodig.mil/audit/reports. DCAA reports are issued at the sole discretion of the DoD contracting office. The GAO report can be accessed at the http://gao.gov/docsearch/repandtest.html.

DoD IG

DoD IG Report No. D-2008-098, "Internal Controls Over Payments Made in Iraq, Kuwait, and Egypt," May 22, 2008

DCAA

Audit Report No. 3311-2004K17900055, "Report on Audit of Proposal for Restore Iraqi Oil Task Order No. 5," October 8, 2004

GAO

GAO Report No. GAO-10-357, "Contingency Contracting, Improvements Needed in Management of Contractors Supporting Contract and Grant Administration in Iraq and Afghanistan," April 12, 2010

Appendix B. Congressional Request

ONE HUNDRED TENTH CONGRESS

Congress of the United States

House of Representatives

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
2157 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6143

MAJORITY (202) 225-5051
FACSIMILE (202) 225-4784
MINORITY (202) 225-5074

www.oversight.house.gov

October 16, 2008

The Honorable Robert M. Gates
Secretary
U.S. Department of Defense
1000 Defense Pentagon
Washington, DC 20301

Dear Mr. Secretary:

Last week, officials from the Defense Energy Support Center briefed Committee staff about allegations that the International Oil Trading Company (IOTC), which is owned by Harry Sargeant, has been overcharging the U.S. government under contracts to deliver fuel through Jordan into Iraq. If this briefing and the documents reviewed by the Committee are accurate, Mr. Sargeant's company appears to have engaged in a reprehensible form of war profiteering.

Over the last four years, IOTC has been paid over $1.4 billion by U.S. taxpayers to deliver fuel through Jordan into Iraq and has earned a profit of over $210 million. According to internal Defense Department documents, the prices IOTC has charged the government are not "fair and reasonable." A "price negotiation memorandum" assessing the company's June 2004 contract concluded that the price charged by IOTC, $2.10 per gallon of jet fuel, was at least 36 cents per gallon too high, even taking into account transportation, storage, and other expenses.

Other contractors offered to deliver fuel at lower prices. When the Defense Department awarded IOTC the June 2004 contract, IOTC was the highest bidder of six offers, with an initial bid over twice as high as the lowest offer. None of the five lower bidders were awarded the contract, however, because they were unable to obtain a "letter of authorization" to transport fuel from the Jordanian government. As a March 2004 "Preaward Survey" reported, IOTC's "major strength is the backing of the Royal Family." In effect, this backing gave IOTC a monopoly on the delivery of fuel through Jordan.

Mr. Sargeant and IOTC appear to have taken full advantage of their ties to the Jordanian royal family. Under federal procurement law, it is illegal to award a contract to a company whose prices are not "fair and reasonable." Senior officials in the Defense Energy Support Center (DESC) twice made personal appeals to Mr. Sargeant to lower his $2.10 per gallon price, but Mr. Sargeant refused. The price negotiation memorandum described one of these appeals:

> [The DESC division chief] asked Mr. Sargeant if there was any way IOTC could reduce the offered price. Mr. Sargeant advised that the offered price was as low as they could go and still insure proper performance. ... Mr. Sargeant was also advised of the possible public scrutiny associated with the award price in light of the recent controversy over fuel prices paid by KBR from Kuwait. Mr. Sargeant is aware of this risk and is comfortable that their price accurately reflects IOTC's cost of performance.

According to the documents provided to the Committee, U.S. Central Command was advised of IOTC's unreasonable prices but "maintained an urgent need for JP8 [jet fuel] sourced through Jordan." For this reason, "the IOTC pricing issue was elevated" to the chief procurement officer in DESC and the agency's director. They were informed that "the Contracting Officer (CO) and the Division Chief were unable to determine the offered price to be fair and reasonable in accordance with the requirements of the FAR," the federal acquisition regulation. Nonetheless, they approved the contract because "CENTCOM confirmed that it had an urgent military need for a JP8 supply route through Jordan."

The contract awarded to IOTC in June 2004 was rebid in March 2005 and December 2006. In neither instance was IOTC the low bidder, but the contracts were awarded to IOTC because it remained the only bidder with a letter of authorization from the Jordanian government. In April 2005, Mr. Sargeant advised a contracting official that the letter of authorization awarded to IOTC "is a sensitive issue in Jordan and they would prefer to keep it as low profile as possible."

At least twice, State Department officials and officials at the Jordanian Embassy in Washington inquired whether the Defense Department needed assistance in asking Jordan to issue letters of authorization to potential competitors of IOTC, but these overtures were rebuffed. In June 2004, Defense Department officials told an official at the Jordanian Embassy that "his assistance would not be necessary at this time."

I have been conducting oversight of procurement problems in Iraq since the war began over five years ago. The IOTC contracts stand out for the extent of the company's apparent profiteering. Of the $210 million in profits received by the company, at least one third — $70 million — appears to have benefited a single individual: Mr. Sargeant. If the IOTC contracts had been awarded to the lowest bidders, the taxpayers could have saved over $180 million.

Background

The prolonged occupation of Iraq generated an unexpected need to import fuel into the country for use by U.S. troops and Iraqis. To meet this need, the Defense Department issued an emergency contract on May 3, 2003, to the Halliburton subsidiary KBR to purchase and import

fuel into Iraq, primarily from Kuwait and Turkey.[1] Overall, KBR charged the Defense Department more than $351 million to import over 131 million gallons of fuel into Iraq and received a maximum fee of 7% of its costs.[2]

Beginning on October 15, 2003, I began raising concerns about KBR's exorbitant fuel charges.[3] As I pointed out in multiple subsequent letters, independent experts expressed grave doubts about the reasonableness of KBR's price, calling it "highway robbery" and noting that they could not "construct a price that high."[4] Ultimately, the Defense Contract Audit Agency questioned $171 million in charges under this contract because KBR "failed to support the reasonableness of prices paid for fuel."[5]

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[1] U.S. Army Corps of Engineers, *Information Paper: Business Case by USACE for the Use of Altanmia as a Supplier of Fuel under the RIO Contract* (Jan. 6, 2004).

[2] Minority Staff, House Committee on Government Reform, *Halliburton's Gasoline Overcharges* (July 21, 2004).

[3] Letter from Reps. Henry A. Waxman and John D. Dingell to OMB Director Joshua Bolten (Oct. 15, 2003).

[4] *See, e.g.*, Letter from Reps. Henry A. Waxman and John D. Dingell to Lt. Gen. Robert Flowers, U.S. Army Corps of Engineers (Oct. 21, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell to National Security Advisor Condoleezza Rice (Oct. 29, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell to Lt. Gen. Robert Flowers, U.S. Army Corps of Engineers (Nov. 5, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell and Sen. Joseph Lieberman to Defense Department Inspector General Joseph E. Schmitz (Nov. 25, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell to National Security Advisor Condoleezza Rice (Dec. 10, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell to Defense Secretary Donald H. Rumsfeld (Dec. 19, 2003); Letter from Reps. Henry A. Waxman and John D. Dingell to Lt. Gen. Robert Flowers, U.S. Army Corps of Engineers (Jan. 6, 2004); Letter from Rep. Henry A. Waxman to National Security Advisor Condoleezza Rice (Jan. 15, 2004); Letter from Reps. Henry A. Waxman and John D. Dingell and Sen. Joseph Lieberman to Defense Department Inspector General Joseph E. Schmitz (Jan. 16, 2004); Letter from Reps. Henry A. Waxman and John D. Dingell to Defense Department Inspector General Joseph E. Schmitz (Feb. 24, 2004); Letter from Rep. Henry A. Waxman to Rep. Tom Davis, Chairman, Government Reform Committee (Nov. 10, 2004); Letter from Rep. Henry A. Waxman to Secretary of State Condoleezza Rice (Feb. 17, 2005).

[5] *See, e.g.*, U.S. Department of Defense, Defense Contract Audit Agency, *Report on Audit of Proposal for Restore Iraqi Oil Task Order No. 5* (Audit Report No. 3311-2004K17900055) (Oct. 8, 2004). *See also* Minority Staff, House Committee on Government

On December 30, 2003, the Defense Department relieved KBR of its fuel importation responsibilities and assigned this duty to the Defense Energy Support Center within the Pentagon.[6] In order to diversify the sources of fuel being imported into Iraq, DESC issued solicitations for fuel importation from three countries: Kuwait, Turkey, and Jordan.[7] Ultimately, Mr. Sargeant's company, the International Oil Trading Company (IOTC), would receive four contracts from DESC to deliver fuel to Iraq through Jordan.

IOTC is a privately held limited liability company registered in Florida. After news reports in May 2008 alleged the company was significantly overcharging U.S. taxpayers, the Committee wrote to the company president, Harry Sargeant, and the Secretary of Defense, Robert Gates, seeking information and documents about the company and its contracts.[8] In response to these requests, the Committee received and reviewed over 11,000 pages of documents. The Committee staff met with representatives of Mr. Sargeant on September 17 and October 1, 2008, and with DESC officials on October 8, 2008.[9]

IOTC's First Contract

DESC first solicited bids on a contract to deliver fuel to Iraq through Jordan in January 2004.[10] The value of this contract was estimated at $77 million. Three companies submitted competitive bids on this contract. In March 2004, DESC awarded the contract to the low bidder, a Jordanian company known as Shaheen Business Investment Group (SBIG). SBIG, however, was unable to begin delivering fuel under the contract within one month. In April, DESC re-awarded the contract to Mr. Sargeant's company, which had the second-lowest bid.[11]

Reform, *Halliburton's Questioned and Unsupported Costs in Iraq Exceed $1.4 Billion* (June 27, 2005).

[6] Defense Logistics Agency, *Defense Energy Support Center to Help Restore Iraqi Oil* (Dec. 30, 2003).

[7] Defense Energy Support Center, *Fact Sheets* (Mar. 15, 2004).

[8] Letter from Chairman Henry A. Waxman to Harry Sargeant, President of the International Oil Trading Company (June 17, 2008); Letter from Chairman Henry A. Waxman to Secretary of Defense Robert M. Gates (June 17, 2008).

[9] At Mr. Sargeant's request, I also met with Mr. Sargeant on June 20, 2008.

[10] Defense Department Solicitation SP0600-04-R-0054 (Jan. 21, 2004).

[11] Defense Energy Support Center, *Price Negotiation Memorandum*, SPO0600-04-D-0490, Trigeant, Ltd. (Apr. 8, 2004).

During the process of awarding the contract, DESC added an amendment to the contract requiring all bidders to obtain a "Letter of Authorization" from the Jordanian government allowing the company to transport fuel through the country. The amendment stated:

> This contract shall not be binding until the contractor submits to the contracting office a letter from the Jordanian government which permits the contract to bring fuel though Jordanian territory in transit to Iraq.[12]

At the October 8, 2008, briefing, DESC officials told the Committee that they were informed by U.S. Embassy officials in Jordan that this requirement was based in Jordanian law.[13] According to a report issued by the Library of Congress, however, Jordanian law does not require an authorization letter to transport fuel through the country.[14] On the contrary, the report states that Jordanian law allows "goods of foreign origin" to be "transported through Jordan in transit from one entry to another exit point at the borders" without "restriction or prohibition."[15] In fact, prior to 2004, the Pentagon had imported fuel directly through Jordan without being required to obtain a letter of authorization from the Jordanian government.[16]

Mr. Sargeant's company was the only non-Jordanian company to obtain an authorization letter. Mr. Sargeant reportedly formed a partnership with two Jordanians to bid on the contract: Mustafa Abu-Naba'a, who is listed as a co-owner of Mr. Sargeant's company, and Mohammad Al-Saleh, who is the brother in law of Jordan's King Abdullah II.[17] Mr. Al-Saleh claims that he

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[12] Defense Department Solicitation SP0600-04-R-0054, Amendment 11 (Mar. 9, 2004).

[13] Defense Energy Support Center, Staff Briefing for Committee on Oversight and Government Reform (Oct. 8, 2008). *See, e.g.*, E-mail from Richard Eason, Economic Section, U.S. Embassy, Jordan, to John Walker, Contracting Officer, Defense Energy Support Center (May 21, 2007) (forwarding information from the Jordanian Energy Ministry confirming the existence of the letter of authorization requirement).

[14] Memorandum from Library of Congress to Henry A. Waxman, Chairman, House Oversight and Government Reform Committee (Sept. 19, 2008) (LL File No. 2008-01528).

[15] *Id.*

[16] Defense Energy Support Center, Staff Briefing for Committee on Oversight and Government Reform (Oct. 8, 2008).

[17] Fax from IOTC to Defense Energy Support Center submitting offer on Solicitation SP0600-04-0R-0054-0002 (May 16, 2004) (listing Mr. Sargeant, Mr. Al-Saleh, and Mr. Abu Naba'a as co-owners of IOTC); Florida Secretary of State, 2007 Limited Liability Company Annual Report for International Oil Trading Company, LLC (Apr. 26, 2007) (listing Mr. Sargeant and Mr. Abu Naba'a as "managers" of IOTC).

"arranged for the Jordanian Ministry of Energy and Mineral Resources to issue a letter of authorization to IOTC."[18]

On March 4, 2004, the Defense Department official conducted a preaward survey of Mr. Sargeant's company, which at the time was called "Trigeant." This survey reported:

> Trigeant's major strength is the backing of the Royal Family. This backing was instrumental in the demonstration of Trigeant capability to meet the delivery date by securing approval to through put product.[19]

IOTC's Second Contract

In May 2004, the Defense Energy Support Center began the bidding process on a second contract to deliver fuel through Jordan to Iraq, this time for use by U.S. troops. Six offers were submitted. Mr. Sargeant's company, IOTC, submitted a bid of [redacted] per gallon. This was the highest bid by far. The lowest bid was [redacted] per gallon. The other four bidders all submitted bids less than [redacted] per gallon.[20]

None of the other five bidders were able to obtain an authorization letter from the Jordanian government, however, leaving Mr. Sargeant's company as the only company permitted

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[18] *Al-Saleh v. Sargeant,* Case No. 2008CA010187XXXXMB (Fl. Cir. Ct. 2008) (Complaint) (Mr. Al-Saleh is now suing Mr. Sargeant and Mr. Abu-Naba'a, claiming that they "conspired to swindle [Mr. Al-Saleh] out of one-third of the profits from the group's valuable contracts with the Government of the United States"). On June 17, 2008, the Committee requested from Mr. Sargeant all documents relating to efforts by him or his company to obtain an authorization letter from the Jordanian government. Letter from Henry A. Waxman, Chairman, House Oversight and Government Reform Committee, to Harry Sargeant (June 17, 2008). In a meeting on October 1, 2008, Mr. Sargeant's counsel suggested that there were no documents responsive to this request and that Mr. Sargeant knew very little about how the letter was obtained from the Jordanian government. Meeting between Mark Touhey, Counsel for IOTC, and Staff, House Oversight and Government Reform Committee (Oct. 1, 2008). Mr. Sargeant has provided no documents in response to the Committee's request to show how he communicated with Jordanian officials to obtain the authorization letter.

[19] Department of Defense, Preaward Survey of Prospective Contractor, Technical: Trigeant (Mar. 4, 2004).

[20] Defense Energy Support Center, Abstract of Initial Offers, Southern Iraq, RFP SP0600-04-F-0054-0002 (May 28, 2004).

to perform the contract.[21] At one point, an official at the Jordanian Embassy in Washington, D.C., offered to help the Defense Department obtain an authorization letter on behalf of one of the other five bidders. In response, an official at the Defense Energy Support Center "advised that his assistance would not be necessary at this time because DESC did have competition and other viable offers."[22]

During May and June 2004, DESC conducted price negotiations with Mr. Sargeant. In these negotiations, Mr. Sargeant lowered his initial bid from [redacted] to $2.10 per gallon. Nonetheless, it became evident to DESC officials that Mr. Sargeant knew he had an exclusive arrangement with the Jordanians and was taking advantage of it. On June 17, 2004, a memo written by a DESC contracting official explained:

> IOTC may have reasonably anticipated no competition and that no other offer could meet the requirements of the solicitation as the Jordanian Minister of Energy advised IOTC that the Ministry would not issue any additional letters authorizing the transport of jet fuel for this solicitation. ... [T]he Contracting officer cannot reasonably conclude that IOTC's offer was submitted with the expectation of competition.[23]

Because the contracting officer determined that Mr. Sargeant's bid was made without true competition, the contracting officer requested a breakdown of Mr. Sargeant's costs. She found that his price of $2.10 per gallon was at least 36 cents higher than it should be, even taking into account all reasonable expenses.[24] Under the Federal Acquisition Regulation, the U.S. government is generally prohibited from issuing contracts unless the price offered is "fair and reasonable."[25] The contracting officer concluded that Mr. Sargeant's prices were too high to make an award. She wrote:

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[21] Defense Energy Support Center, Staff Briefing for Committee on Oversight and Government Reform (Oct. 8, 2008).

[22] Defense Energy Support Center, Memorandum for Record on June 8, 2004, Telephone Conversation between DESC and Embassy of Jordan (June 16, 2004).

[23] Defense Energy Support Center, *Price Negotiation Memorandum*, Contract SP0600-04-D-0506 (June 17, 2004).

[24] *Id.*

[25] Federal Acquisition Regulation § 15.402(a).

> [T]he Contracting Officer cannot determine IOTC's final offer price of $2.10 per gallon reasonable as required by FAR [Federal Acquisition Regulation] 15.402.[26]

After the contracting officer closed negotiations, the contracting officer's superior, a division chief at Defense Energy Support Center, contacted Mr. Sargeant personally to request that he lower his price, noting that he had an effective monopoly contract. Despite this direct entreaty, Mr. Sargeant refused. The "price negotiation memorandum" issued on June 17, 2004, describes this encounter:

> [The DESC division chief] asked Mr. Sargeant if there was any way IOTC could reduce the offered price. Mr. Sargeant advised that the offered price was as low as they could go and still insure proper performance. ... Mr. Sargeant was also advised of the possible public scrutiny associated with the award price in light of the recent controversy over fuel prices paid by KBR from Kuwait. Mr. Sargeant is aware of this risk and comfortable that their price accurately reflects IOTC's cost of performance.[27]

In the face of Mr. Sargeant's refusal to lower his prices, officials at the Defense Energy Support Center contacted military commanders at U.S. Central Command, who warned that the U.S. military had "an urgent need for JP8 [jet fuel] sourced through Jordan."[28] Because of this military urgency, the matter was elevated internally within DESC. Within four days, the chief procurement official met with Mr. Sargeant personally to ask again that he lower his price. Again, however, Mr. Sargeant refused. The chief procurement officer wrote a memo describing their meeting:

> As CSPO [the center's senior procurement official] I conducted negotiations with IOTC to discuss the elements of their offered price. Mr. Sargeant reiterated and confirmed the various elements of price that were previously provided to the CO [contracting officer] and the Division Chief. ...
>
> Mr. Sargeant expressed that to budget without demurrage (i.e. reducing offered price) would expose IOTC to significant liability and IOTC would not be able to perform (Mr. Sargeant stated he would rather not offer than take on this risk).[29]

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[26] Defense Energy Support Center, *Price Negotiation Memorandum, Contract SP0600-04-D-0506* (June 17, 2004).

[27] *Id.*

[28] *Id.*

[29] Memorandum of Conversation between Center Senior Procurement Official, Defense Energy Support Center, and Harry Sargeant (June 21, 2004).

After this conversation, the chief procurement official also concluded that "the offered price cannot be determined fair and reasonable in accordance with FAR 15.403-3(a)(4) and DLAD 15.404-2."[30] Because of the military's compelling need for the fuel, however, he forwarded this information to his superior, writing: "I am forwarding the packet with recommendation of award to the Director, Defense Energy Support Center."[31]

The DESC director personally approved the award on June 22, 2004.[32] In explaining his decision, the director issued a memorandum on July 21, 2004, setting forth the "justification for other than full and open competition" and specifically citing the "urgent military need" expressed by CENTCOM. The memo stated:

> Six offers were received. However, only International Oil Trade Center (IOTC) was determined acceptable because it was the only offeror able to provide, prior to close of negotiations, the required letter from the Jordanian government authorizing it to transit fuel through Jordan to Iraq. CENTCOM confirmed that it had an urgent military need for a JP8 supply route through Jordan.[33]

IOTC's Third Contract

On March 15, 2005, the Defense Energy Support Center solicited bids on an extension of the June 2004 fuel contract. This time, four competitive bids were submitted. Although IOTC's bid was the second highest, none of the other companies were able to produce an authorization letter, again leaving IOTC as the only eligible offeror.[34]

During the bidding process, both the Jordanian Energy Minister and Mr. Sargeant urged DESC to keep IOTC's authorization letter secret. On May 12, 2005, an official at the U.S. Embassy in Jordan sent an e-mail to a DESC contracting official explaining that Jordan's Energy

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[30] *Id.*

[31] *Id.*

[32] Defense Energy Support Center, *Price Negotiation Memorandum, Contract SP0600-04-D-0506* (June 17, 2004) (signed and approved by DESC director on June 22, 2004).

[33] Defense Energy Support Center, *Justification for Other than Full and Open Competition for an Alternate Supply Route for JP8 Through Jordan to Iraq Under Authority of 10 U.S.C. 2304(C)(2), Solicitation SP0600-04-R-0054-0002* (July 21, 2004).

[34] Defense Energy Support Center, Staff Briefing for Committee on Oversight and Government Reform (Oct. 8, 2008).

Minister "requested that we keep this information quiet for political reasons."[35] On April 21, 2005, Mr. Sargeant sent an e-mail to the same contracting official explaining that "this is a sensitive issue in Jordan and they would prefer to keep it as low profile as possible!!"[36]

When IOTC's competitors began reporting difficulties obtaining letters of authorization, an official at the U.S. Embassy in Amman offered to help. On May 5, 2005, an official at the U.S. Embassy in Amman wrote to the DESC contracting officer in charge of the contracts:

> My recommendation is that DESC proceed with the tendering process. Once DESC has reviewed the bid packets and agreed on a short-list, we can then seek LOAs [letters of authorization] from the Energy Minister. ... Please keep us posted on the bidding schedule and on when DESC has decided on a shortlist or a winning bidder. We will then seek LOAs from the Energy Ministry. We are eager to ensure that the flow of fuel supplies to our troops in Iraq remains steady.[37]

In response, a DESC contracting official wrote:

> Rather than have you seek LOAs from the GOJ [Government of Jordan] on any of these firms, I would ask that you confirm LOAs once we have received them from the offerors and again if possible find out if the current LOA for IOTC is considered valid by the Minister of Energy for the follow on contract should IOTC be in line for the award.[38]

In April and May 2005, DESC contracting officials conducted price negotiations with IOTC. Although Mr. Sargeant offered a lower price per gallon than he had previously, his price was still outside the range deemed "fair and reasonable" in June 2004.[39] This time, however,

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[35] E-mail from Richard Eason, Economic Section, U.S. Embassy, Jordan, to John Walker, Contracting Officer, DESC (May 12, 2005).

[36] E-mail from Harry Sargeant to John Walker, Contracting Officer, Defense Energy Support Center (Apr. 21, 2005).

[37] E-mail from Richard Eason, Economic Section, U.S. Embassy, Jordan, to John Walker, Contracting Officer, DESC (May 5, 2005).

[38] E-mail from John Walker, Contracting Officer, Defense Energy Support Center, to Richard Eason, Economic Section, U.S. Embassy, Jordan (May 9, 2005).

[39] IOTC offered a price of [redacted] per gallon of jet fuel, which included [redacted] to cover the cost of fuel and a [redacted] margin for IOTC's profit and expenses. Defense Energy Support Center, *Price Negotiation Memorandum, Contract SP0600-05-D-0497* (May 26, 2005). In June 2004, DESC had determined that a margin of 84 cents was acceptable. Defense Energy Support Center, *Price Negotiation Memorandum, Contract SP0600-04-D-0506* (June 17, 2004) (finding that

DESC did not conduct a detailed analysis of IOTC's price. Instead, it deemed IOTC's price fair and reasonable because IOTC had submitted its bid with the "reasonable expectation" of "adequate competition."[40] On May 26, 2005, the DESC awarded IOTC the contract.[41] DESC later exercised two six-month options on this contract, extending IOTC's contract through June 2007.

IOTC's Fourth Contract

On December 15, 2006, the Defense Energy Support Center solicited bids on a fourth contract to deliver fuel to Iraq through Jordan. Seven companies submitted bids, of which four were determined to be competitive. Of these four competitive bids, IOTC's price was the second highest. Once again, however, only IOTC could provide a letter of authorization, so IOTC was the only offeror eligible for the contract.[42] On May 3, 2007, DESC awarded the contract to IOTC.[43]

In January 2007, the U.S. Ambassador to Jordan, David Hale, spoke directly with the Jordanian Energy Minister about IOTC's letter of authorization.[44] However, the Committee has no evidence that Ambassador Hale asked the Energy Minister to waive the authorization requirement or issue authorization letters for IOTC's competitors.

One of IOTC's competitors, [redacted] filed protests with the Government Accountability Office. [redacted] argued it should have received the contract because its bid was approximately [redacted] less expensive than IOTC's.[45] [redacted] also argued that the

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IOTC's price of $2.10, which included [redacted] for fuel costs and a margin of [redacted] was 36 cents higher than the acceptable price).

[40] Defense Energy Support Center, *Price Negotiation Memorandum, Contract SP0600-05-D-0497* (May 26, 2005).

[41] *Id.*

[42] Defense Energy Support Center, Staff Briefing for Committee on Oversight and Government Reform (Oct. 8, 2008).

[43] Defense Department Contract SP0600-07-D-0483 (May 3, 2007).

[44] E-mail from Richard Eason, Economic Section, U.S. Embassy, Jordan, to John Walker, Contracting Officer, Defense Energy Support Center (Jan. 18, 2007).

[45] Letter from Christopher M. Johnson, Counsel to [redacted] to Government Accountability Office (May 14, 2007).

requirement for a letter of authorization was "unduly restrictive."[46] In response to these protests, the Defense Energy Support Center agreed to reconsider the award. It then determined again that "IOTC USA was the only firm which provided required Letter of Authorization."[47]

When [redacted] again protested the decision, officials at DESC took several actions. First, they agreed to release a list from the Jordanian Ministry of Energy of companies that "would be eligible to receive a Letter of Authorization."[48] Of the five companies on the list, four were Jordanian companies that did not bid on any of the four Defense Department fuel contracts. The fifth was IOTC.[49] Second, DESC agreed to issue a new solicitation rather than exercise the first one-year option under IOTC's contract.

The new solicitation did not improve the situation, however. Both bidders on the new solicitation, including [redacted] and a second company, were unable to obtain letters of authorization. As a result, DESC abandoned the competition and decided to exercise its option to extend its contract with IOTC.[50]

Once again, [redacted] protested.[51] In an e-mail to DESC, an [redacted] official explained the problem:

[redacted]

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[46] Defense Energy Support Center, *Price Negotiation/Source Selection Memorandum, SP0600-07-R-0700, JP8, DT2, & MUJ from Jordan to Western Iraq* (June 8, 2007) (summarizing [redacted] protests and DESC's responses).

[47] *Id.*

[48] E-mail from Farouq Al-Hiyari, Secretary General, Jordanian Ministry of Energy and Mineral Resources, to Kristen Pisani, Economic Section, U.S. Embassy, Jordan (Oct. 30, 2007).

[49] *Id.*

[50] Defense Energy Support Center, *Price Negotiation/Source Selection Memorandum, SP0600-08-R-0701, JP8, DT2, & MUJ from Jordan to Western Iraq* (Feb. 24, 2008).

[51] [redacted] Protest of [redacted] Defense Energy Support Center: Solicitation # SP0600-08-R-0701 – Supply and Delivery of JP8, Diesel Fuel and Gasoline from Jordan to Iraq (Mar. 12, 2008) (submitted to GAO); *see also* [redacted] Protest of Solicitation # SP0600-08-R-0701 – Supply and Delivery of JP8, Diesel Fuel and Gasoline from Jordan to Iraq (Nov. 15, 2007) (submitted to DESC).

[redacted][52]

Eventually, [redacted] gave up its protests. In an e-mail explaining its decision, a company official wrote:

[redacted][53]

IOTC's Profits

According to documents provided to the Committee by Mr. Sargeant, the IOTC contracts have been exceptionally lucrative for IOTC. In total, his company has been paid over $1.4 billion under the four contracts and has collected profits of over $210 million.[54] The company's profit margin has been over 14%.

Under the first contract, Mr. Sargeant's company was paid $41 million, but ended up with a net loss of $2.4 million after DESC reduced its requirements and left IOTC with excess fuel.[55] Under the second contract, IOTC was paid $154 million and made $17 million in profits.[56] Under the third contract, IOTC was paid $710 million and made $121 million in

[52] E-mail from [redacted] to John Walker, Contracting Officer, Defense Energy Support Center (Dec. 10, 2007).

[53] E-mail from [redacted] to John Walker, Contracting Officer, Defense Energy Support Center (May 19, 2008).

[54] IOTC, Trigeant/International Oil Trading Center/International Oil Trading Company Government Contracts 2004-2008 (undated chart).

[55] Defense Energy Support Center, Staff Briefing for Committee on Oversight and Government Reform (Oct. 8, 2008) (listing value of contract); IOTC, Trigeant/International Oil Trading Center/International Oil Trading Company Government Contracts 2004-2008 (undated chart) (listing IOTC's net profit).

[56] IOTC, Trigeant/International Oil Trading Center/International Oil Trading Company Government Contracts 2004-2008 (undated chart).

profits.[57] Under the fourth contract, which is ongoing, IOTC has been paid more than $560 million and has made over $74 million in profits.[58]

Mr. Sargeant's personal gain from these four contracts may have been $70 million or higher. According to Mr. Sargeant's former partner, Mr. Al-Saleh, Mr. Sargeant initially received one-third of the company's profits.[59] Mr. Al-Saleh alleges that Mr. Sargeant and the third partner, Mustafa Abu-Naba'a, improperly denied Mr. Al-Saleh his share of the profits. If this is true, this may have increased Mr. Sargeant's share of the profits to 50%.

The payments to IOTC significantly exceeded the amounts that would have been paid if DESC had awarded the contracts to the lowest bidders. The Committee staff has calculated that if DESC had awarded the contracts to the lowest bidders in June 2004 contract, June 2005 contract, and May 2007, the taxpayers could have saved $183 million. This is over 87% of the profits made by IOTC and Mr. Sargeant.

Conclusion

When KBR was under contract with the Defense Department to import fuel from Kuwait into Iraq, the company's profits were limited to a maximum of 7% of costs. Even these profits were heavily criticized as excessive. But when IOTC assumed part of this work and began importing fuel from Jordan, the company more than doubled this profit margin to over 14%, collecting more than $210 million under contracts worth $1.4 billion. At least $70 million of these profits appear to have gone to one person: Mr. Sargeant.

In 2004, DESC officials recognized that IOTC's charges were neither reasonable nor fair and personally intervened to ask Mr. Sargeant to lower his prices. He refused. His company had an effective monopoly over fuel shipments through Jordan, and it appears that he took deliberate advantage of this monopoly to enrich himself and his company at the expense of U.S. taxpayers and our military. If this is true, it represents the worst form of war profiteering.

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[57] *Id.*

[58] *Id.*

[59] *Al-Saleh v. Sargeant*, Case No. 2008CA010187XXXXMB (Fl. Cir. Ct. 2008) (Complaint).

I respectfully request that you investigate this matter and report back to the Committee on your findings and the steps you will take to protect the interests of U.S. taxpayers.

Sincerely,

Henry A. Waxman
Chairman

cc: Tom Davis
Ranking Minority Member

Appendix C. Secretary of Defense Letter

SECRETARY OF DEFENSE
1000 DEFENSE PENTAGON
WASHINGTON, DC 20301-1000

JAN 27 2009

The Honorable Edolphus Towns
Chairman, Committee on Oversight
and Government Reform
U.S. House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

This responds to Chairman Henry Waxman's letter of October 16, 2008 (enclosed) expressing concerns that the International Oil Trading Company is overcharging the U.S. government under contracts to deliver fuel through Jordan into Iraq. I appreciate and share the Committee's expectation that all contractors must behave ethically and legally while supporting the Department of Defense's requirements. In light of these concerns, I am requesting that the Department of Defense Inspector General conduct an independent audit of the applicable defense contracts and the issues highlighted in Chairman Waxman's letter.

Once these reviews are completed, the Department will report the results to the Committee.

Sincerely,

Enclosure:
As stated

cc:
The Honorable Darrell E. Issa
Ranking Member

Appendix D. Response to Congressional Issues

Issue 1: Did the USCENTCOM have an urgent need for a fuel supply route through Jordan?

Audit Results: According to USCENTCOM's Joint Petroleum Office, it had an urgent need for a third fuel supply route into Iraq during the early phases of combat operations. The military units operating in Iraq required more fuel to meet their mission requirements. The Kuwait fuel supply route was already operating at its peak capacity, and due to logistical issues, the quantity of fuel that USCENTCOM could obtain from the North Atlantic Treaty Organization pipeline through Turkey was limited and unreliable. Consequently, a third fuel supply route was needed and, due to the political realities of the region, going through Jordan was the only alternative.

Issue 2: No competitive market existed.

Audit Results: Although numerous companies submitted proposals for the contract requirements, IOTC was the only company capable of satisfying the responsibility requirements included in the various solicitations issued for these contracts. Therefore, we question whether there was ever adequate price competition for these procurements.

Issue 3: IOTC appears to have engaged in a reprehensible form of war profiteering.

Audit Results: It is difficult to determine whether IOTC engaged in war profiteering. Based on our analysis of the amount that IOTC paid its suppliers for the jet fuel delivered under contract SP0600-07-D-0483, IOTC's actual product costs tracked to the price that DLA Energy agreed to pay for the fuel supplied under the contract. However, it is hard to evaluate how reasonable the nonfuel components of IOTC's prices were because DLA Energy did not obtain cost proposals from the offerors or field pricing assistance. Nevertheless, it should be noted that the nonfuel per gallon price for IOTC's last three contracts ranged from [redacted] nonfuel price that was evaluated during the price negotiations for contract SP0600-04-D-0506 and resulted in IOTC receiving about $160 to $204 million (or 6 to 7 percent) more than what can be supported by price analysis.

Appendix E. Guidance

Federal Acquisition Regulation

Responsible Prospective Contractors. FAR Subpart 9.1, "Responsible Prospective Contractors," requires that contracts only be awarded to responsible prospective contractors. The contracting officer is responsible for researching and determining whether a contractor is deemed responsible. FAR Subpart 9.104-1, "General Standards," states to be determined responsible, a prospective contractor must:

> (a) Have adequate financial resources to perform the contract, or the ability to obtain them (see 9.104-3(a));
>
> (b) Be able to comply with the required or proposed delivery or performance schedule, taking into consideration all existing commercial and governmental business commitments;
>
> (c) Have a satisfactory performance record (see 9.104-3(b) and Subpart 42.15). A prospective contractor shall not be determined responsible or nonresponsible solely on the basis of a lack of relevant performance history, except as provided in 9.104-2;
>
> (d) Have a satisfactory record of integrity and business ethics (for example, see Subpart 42.15);
>
> (e) Have the necessary organization, experience, accounting and operational controls, and technical skills, or the ability to obtain them (including, as appropriate, such elements as production control procedures, property control systems, quality assurance measures, and safety programs applicable to materials to be produced or services to be performed by the prospective contractor and subcontractors). (See 9.104-3 (a).)
>
> (f) Have the necessary production, construction, and technical equipment and facilities, or the ability to obtain them (see 9.104-3(a)); and
>
> (g) Be otherwise qualified and eligible to receive an award under applicable laws and regulations (see also inverted domestic corporation prohibition at FAR 9.108.

Pricing Policy. FAR Subpart 15.402, "Pricing Policy," requires contracting officers to purchase supplies and services from responsible sources at fair and reasonable prices. To the extent that cost or pricing data are not required by FAR subpart 15.403-4, the contracting officer must generally use the following order of preference in determining the type of information required:

- no additional information from the offeror, if a price is based on adequate competition, except as provided by FAR Subpart 15.403-3(b);
- information other than cost or pricing data; and
- cost or pricing data.

Adequate Price Competition. In accordance with FAR subpart 15.403-1(c)(1), a price is based on adequate price competition if:

> (i) Two or more responsible offerors, competing independently, submit priced offers that satisfy the Government's expressed requirement and if --

(A) Award will be made to the offeror whose proposal represents the best value (see 2.101) where price is a substantial factor in source selection; and

(B) There is no finding that the price of the otherwise successful offeror is unreasonable. Any finding that the price is unreasonable must be supported by a statement of the facts and approved at a level above the contracting officer;

(ii) There was a reasonable expectation, based on market research or other assessment, that two or more responsible offerors, competing independently, would submit priced offers in response to the solicitation's expressed requirement, even though only one offer is received from a responsible offeror and if --

(A) Based on the offer received, the contracting officer can reasonably conclude that the offer was submitted with the expectation of competition, e.g., circumstances indicate that --

(1) The offeror believed that at least one other offeror was capable of submitting a meaningful offer; and

(2) The offeror had no reason to believe that other potential offerors did not intend to submit an offer; and

(B) The determination that the proposed price is based on adequate price competition, is reasonable, and is approved at a level above the contracting officer; or

(iii) Price analysis clearly demonstrates that the proposed price is reasonable in comparison with current or recent prices for the same or similar items, adjusted to reflect changes in market conditions, economic conditions, quantities, or terms and conditions under contracts that resulted from adequate price competition.

FAR Subpart 15.403-3(b), "Adequate price competition," requires that additional information be obtained when unusual circumstances exist that hinder a contracting officer's ability to conclude that the offered price is reasonable. Specifically,

When adequate price competition exists (see 15.403-1(c)(1)), generally no additional information is necessary to determine the reasonableness of price. However, **if there are unusual circumstances where it is concluded that additional information is necessary to determine the reasonableness of price, the contracting officer shall, to the maximum extent practicable, obtain the additional information from sources other than the offeror. In addition, the contracting officer may request information to determine the cost realism of competing offers or to evaluate competing approaches. [emphasis added]**

FAR Subpart 15.403-1, "Prohibition on obtaining cost or pricing data," states:

(iii) The following requirements apply to minor modifications defined in paragraph (3)(ii) of the definition of a commercial item at 2.101 that do not change the item from a commercial item to a noncommercial item:

. . . . . .

(C) For acquisitions funded by DoD, NASA, or Coast Guard such modifications of a commercial item are not exempt from the requirement for submission of cost or pricing data on the basis of the exemption provided for at FAR 15.403-1(c)(3) if the total price of all such modifications under a particular contract action exceeds the greater of the threshold for obtaining cost and pricing data in 15.403-4 [$650,000] or 5 percent of the total price of the contract at the time of contract award. [emphasis added]

Acceptance. FAR Subpart 46.5, "Acceptance," defines what constitutes acceptance and identifies when acceptance can take place. Specifically, FAR Subpart 46.501 states:

> Acceptance constitutes acknowledgement that the supplies or services conform with applicable contract quality and quantity requirements, except as provided in this subpart and subject to other terms and conditions of the contract. **Acceptance may take place before delivery, at the time of delivery, or after delivery, depending on the provisions of the terms and conditions of the contract.** Supplies or services shall ordinarily not be accepted before completion of Government contract quality assurance actions (however, see 46.504). **Acceptance shall ordinarily be evidenced by execution of an acceptance certificate on an inspection or receiving report form or commercial shipping document/packing list. [emphasis added]**

FAR Subpart 46.502, "Responsibility for Acceptance," assigns the responsibility for acceptance of supplies or services to the contracting officer, but allows contracting officers to assign the responsibility to a cognizant contract administration office or another agency.

> **Acceptance of supplies or services is the responsibility of the contracting officer. When this responsibility is assigned to a cognizant contract administration office or to another agency (see 42.202(g)), acceptance by that office or agency is binding on the Government. [emphasis added]**

Contracting Officer's Representative. Contracting officers may designate qualified personnel as their authorized representatives to assist in either, technical monitoring or administration of a contract. The Defense Acquisition University defines a COR as:

> **an individual who is designated and authorized in writing by the contracting officer to perform specific technical or administrative functions on contracts or orders.** The term COR includes any individual (military or civilian) performing these types of functions on contracts regardless of the term used to describe their position or assignment (e.g., alternate CORs, assistant CORs, Contracting Officers' Technical Representatives (COTRs), task order monitors, task order managers, performance assessment monitors, etc.). These individuals serve a critical role in assuring contractors meet the performance requirements of contracts in terms of cost, quality, quantity, and schedule. **Only contracting officers have the authority to delegate these functions. [emphasis added]**

The Defense Federal Acquisition Regulation Supplement Subpart 201.6, "Career Development, Contracting Authority and Responsibilities," requires CORs to have their authority designated in writing and should be qualified by training and experience commensurate with the responsibility delegated by the contracting officer.

Inherently Governmental Function. FAR Subpart 7.5, "Inherently Governmental Functions," prescribes policies and procedures to ensure that inherently governmental functions are not performed by contractors. FAR subpart 7.503(c) identifies accepting contractor products or services as an example of an inherently governmental function.

> **(c) The following is a list of examples of functions considered to be inherently governmental functions or which shall be treated as such.** This list is not all inclusive:
>
> . . . . . .

(12) In federal procurement activities with respect to prime contracts-

. . . . . .

(v) Administering contracts (including ordering changes in contract performance or contract quantities, taking action based on evaluations of contractor performance, and **accepting or rejecting contractor products or services) [emphasis added]**

The "Contingency Contracting: A Joint Handbook For The 21st Century," that the Defense Procurement and Acquisition Policy issued to provide a consolidated source of information for contingency contracting officers also identifies the inappropriateness of contractors accepting products or services for the Government. Specifically, Chapter 6, "Contract Administration," of the handbook states:

It is important to know that government support contractors are not authorized to accept or sign for the government in any situation. [emphasis added]

Defense Federal Acquisition Regulation Supplement

Additional Information to Support Price Reasonableness. DFARS PGI 215.403-3, "Requiring information other than cost or pricing data," provides additional guidance to contracting officers when cost or pricing data are not required, and the contracting officer does not have sufficient data or information to determine price reasonableness. Specifically, it states:

To the extent that cost or pricing data are not required by FAR 15.403-4 and there is no other means for the contracting officer to determine that prices are fair and reasonable, the offeror is required to submit "information other than cost or pricing data" (see definition at FAR 2.101). In accordance with FAR 15.403-3(a), the offeror must provide appropriate information on the prices at which the same or similar items have previously been sold, adequate for determining the reasonableness of the price. The following clarifies these requirements:

(1) Information other than cost or pricing data. **When cost or pricing data are not required, the contracting officer must obtain whatever information is necessary in order to determine the reasonableness of the price.** The FAR defines this as "information other than cost or pricing data." **When TINA [Truth In Negotiations Act] does not apply and there is no other means of determining that prices are fair and reasonable, the contracting officer must obtain appropriate information on the prices at which the same or similar items have been sold previously, adequate for evaluating the reasonableness of the price.** Sales data must be comparable to the quantities, capabilities, specifications, etc., of the product or service proposed. Sufficient steps must be taken to verify the integrity of the sales data, to include assistance from the Defense Contract Management Agency, the Defense Contract Audit Agency, and/or other agencies if required. **[emphasis added]**

Requirement for Cost Analysis and Consideration of the Need for Field Pricing Assistance. DFARS PGI 215.404-1, "Proposal Analysis," requires that a cost analysis be performed when sufficient information cannot be obtained to perform price analysis. It also requires contracting officers to consider the need for field pricing support. Specifically,

DFARS PGI 215.404-1(c), "Cost Analysis," states:

> **(i) When the contracting officer cannot obtain sufficient information to perform a price analysis in accordance with the pricing steps in FAR 15.404-1 (b), a cost analysis is required.**
>
> **(ii) When a solicitation is not subject to TINA and a cost analysis is required, the contracting officer must clearly communicate to the offeror the cost information that will be needed to determine if the proposed price is fair and reasonable.**
>
> . . . . . .
>
> **(iv) The contracting officer must always consider the need for field pricing support from the Defense Contract Management Agency, the Defense Contract Audit Agency, and/or other agencies. [emphasis added]**

FAR Subpart 15.404-2(a), "Field pricing assistance," and DFARS PGI 215.404-2, "Information to support proposal analysis," identify situations when the contracting officer should consider requesting field pricing assistance. Specifically,

- FAR Subpart 15.404-2(a) states:

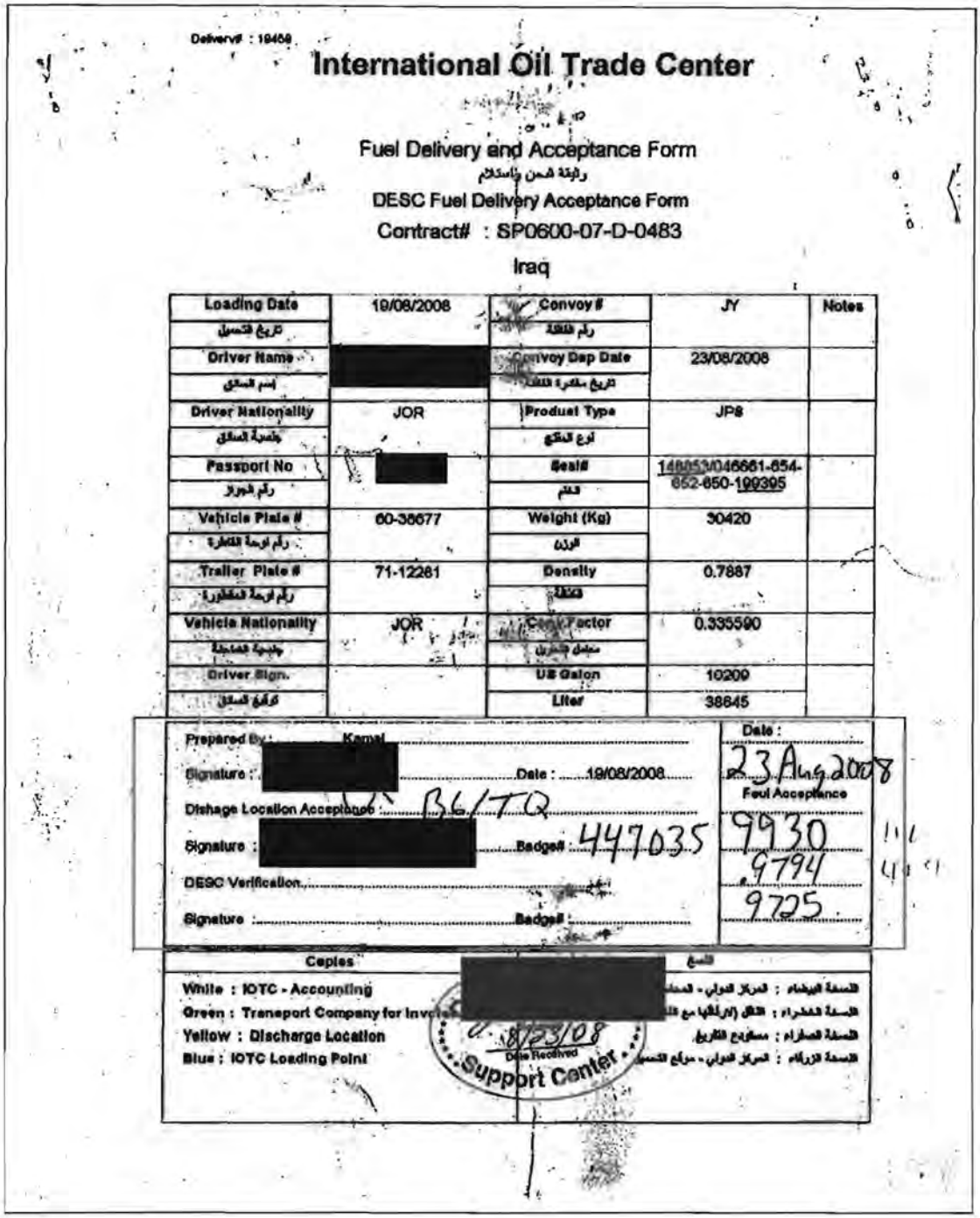
> **(1) The contracting officer should request field pricing assistance when the information available at the buying activity is inadequate to determine a fair and reasonable price. [emphasis added]** The contracting officer must tailor requests to reflect the minimum essential supplemental information needed to conduct a technical or cost or price analysis.

- DFARS PGI 215.404-2(a) states:

> **(i) The contracting officer should consider requesting field pricing assistance-**
>
> > **(A) Fixed-price proposals exceeding the cost or pricing threshold; [emphasis added]**

Appendix F. Additional Information on Contractor Protests

Appendix G. International Oil Trading Company-Created Fuel Delivery and Acceptance Form



Delivery# : 19459

International Oil Trade Center

Fuel Delivery and Acceptance Form

وثيقة شحن وتسلم

DESC Fuel Delivery Acceptance Form

Contract# : SP0600-07-D-0483

Iraq

Loading Date تاريخ التحميل	19/08/2008	Convoy # رقم القافلة	JY	Notes
Driver Name إسم السائق	[redacted]	Convoy Dep Date تاريخ مغادرة القافلة	23/08/2008	
Driver Nationality جنسية السائق	JOR	Product Type نوع المنتج	JP8	
Passport No رقم الجواز	[redacted]	Seal# الختم	148053/046661-654-652-650-199395	
Vehicle Plate # رقم لوحة القاطرة	60-38677	Weight (Kg) الوزن	30420	
Trailer Plate # رقم لوحة المقطورة	71-12281	Density الكثافة	0.7887	
Vehicle Nationality جنسية الشاحنة	JOR	Conv. Factor معامل التحويل	0.335590	
Driver Sign. توقيع السائق		US Galon Liter	10209 38645	

Prepared By : Kamal

Signature : [redacted] Date : 19/08/2008

Dishage Location Acceptance : BKTQ

Signature : [redacted] Badge# : 447035

DESC Verification

Signature : Badge# :

Date : 23 Aug 2008

Feul Acceptance

9930

9794

9725

Copies

White : IOTC - Accounting

Green : Transport Company for Invoice

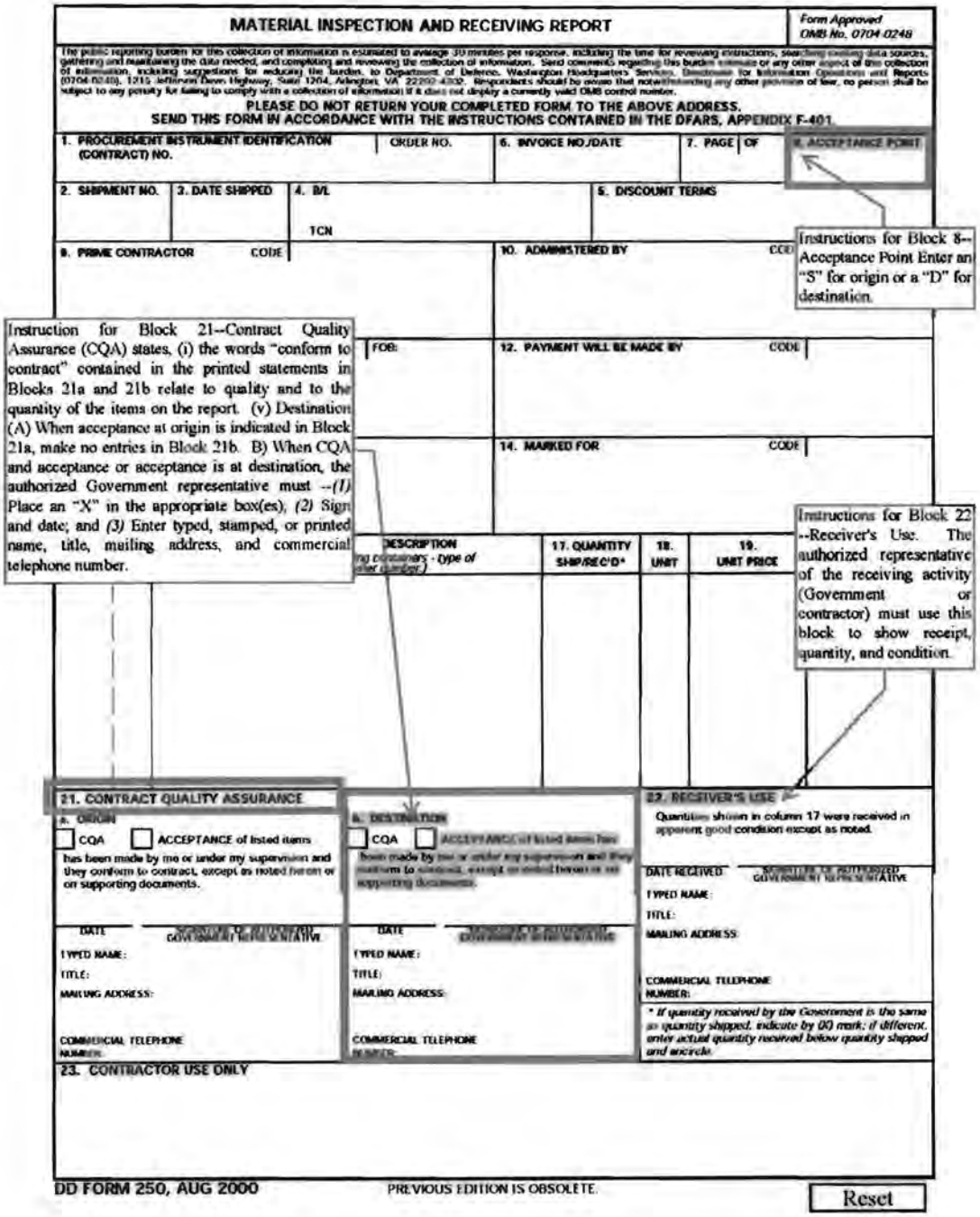
Yellow : Discharge Location

Blue : IOTC Loading Point

[redacted]

8/23/08 Date Received Support Center

Appendix H. DD Form 250, Material Inspection and Receiving Report



MATERIAL INSPECTION AND RECEIVING REPORT

Form Approved
OMB No. 0704-0248

The public reporting burden for this collection of information is estimated to average 30 minutes per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing the burden, to Department of Defense, Washington Headquarters Services, Directorate for Information Operations and Reports (0704-0248), 1215 Jefferson Davis Highway, Suite 1204, Arlington, VA 22202-4302. Respondents should be aware that notwithstanding any other provision of law, no person shall be subject to any penalty for failing to comply with a collection of information if it does not display a currently valid OMB control number.

PLEASE DO NOT RETURN YOUR COMPLETED FORM TO THE ABOVE ADDRESS.
SEND THIS FORM IN ACCORDANCE WITH THE INSTRUCTIONS CONTAINED IN THE DFARS, APPENDIX F-401.

1. PROCUREMENT INSTRUMENT IDENTIFICATION (CONTRACT) NO. | ORDER NO. | 6. INVOICE NO./DATE | 7. PAGE | OF | 8. ACCEPTANCE POINT

2. SHIPMENT NO. | 3. DATE SHIPPED | 4. B/L / TCN | 5. DISCOUNT TERMS

9. PRIME CONTRACTOR CODE | 10. ADMINISTERED BY CODE

FOB: | 12. PAYMENT WILL BE MADE BY CODE

14. MARKED FOR CODE

DESCRIPTION (ng containers - type of other number) | 17. QUANTITY SHIP/REC'D* | 18. UNIT | 19. UNIT PRICE

21. CONTRACT QUALITY ASSURANCE

a. ORIGIN
☐ CQA ☐ ACCEPTANCE of listed items
has been made by me or under my supervision and they conform to contract, except as noted hereon or on supporting documents.
DATE | SIGNATURE OF AUTHORIZED GOVERNMENT REPRESENTATIVE
TYPED NAME:
TITLE:
MAILING ADDRESS:
COMMERCIAL TELEPHONE NUMBER:

b. DESTINATION
☐ CQA ☐ ACCEPTANCE of listed items has been made by me or under my supervision and they conform to contract, except as noted hereon or on supporting documents.
DATE | SIGNATURE OF AUTHORIZED GOVERNMENT REPRESENTATIVE
TYPED NAME:
TITLE:
MAILING ADDRESS:
COMMERCIAL TELEPHONE NUMBER:

22. RECEIVER'S USE
Quantities shown in column 17 were received in apparent good condition except as noted.
DATE RECEIVED | SIGNATURE OF AUTHORIZED GOVERNMENT REPRESENTATIVE
TYPED NAME:
TITLE:
MAILING ADDRESS:
COMMERCIAL TELEPHONE NUMBER:
* If quantity received by the Government is the same as quantity shipped, indicate by (X) mark; if different, enter actual quantity received below quantity shipped and encircle.

23. CONTRACTOR USE ONLY

DD FORM 250, AUG 2000 PREVIOUS EDITION IS OBSOLETE. Reset

Instructions for Block 8--Acceptance Point Enter an "S" for origin or a "D" for destination.

Instruction for Block 21--Contract Quality Assurance (CQA) states, (i) the words "conform to contract" contained in the printed statements in Blocks 21a and 21b relate to quality and to the quantity of the items on the report. (v) Destination (A) When acceptance at origin is indicated in Block 21a, make no entries in Block 21b. B) When CQA and acceptance or acceptance is at destination, the authorized Government representative must --*(1)* Place an "X" in the appropriate box(es), *(2)* Sign and date; and *(3)* Enter typed, stamped, or printed name, title, mailing address, and commercial telephone number.

Instructions for Block 22 --Receiver's Use. The authorized representative of the receiving activity (Government or contractor) must use this block to show receipt, quantity, and condition.

Defense Logistics Agency Comments

DEFENSE LOGISTICS AGENCY
HEADQUARTERS
8725 JOHN J. KINGMAN ROAD, SUITE 2533
FORT BELVOIR, VIRGINIA 22060-6221

DEC 15 2010

IN REPLY REFER TO DLA Energy

MEMORANDUM FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL

SUBJECT: Response to draft report *Competition Issues and Inherently Governmental Functions performed by Contractor Employees on Contracts to Supply Fuel to U.S. Troops in Iraq*, Report No. D2009-D000CH-0244

Defense Inspector General audited Defense Logistics Agency (DLA) Energy at the request of the Chairman of the House Committee on Oversight and Government Reform.

The purpose of this memorandum is to provide DLA's responses to the Department of Defense Inspector General audit report recommendations.

We would like to thank the DoDIG staff for their time and expertise during the audit.

Nancy M. Heimbaugh

NANCY M. HEIMBAUGH
Senior Procurement Executive

DEFENSE LOGISTICS AGENCY
DEFENSE ENERGY SUPPORT CENTER
8725 JOHN J. KINGMAN ROAD, SUITE 4950
FORT BELVOIR, VIRGINIA 22060-6222

IN REPLY
REFER TO DLA Energy-DI

MEMORANDUM FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL

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We would like to thank the DoDIG staff for their time and expertise during the audit.

PATRICK J. DULIN
Deputy Commander

DEFENSE LOGISTICS AGENCY

REPLY TO DOD IG DRAFT REPORT: COMPETITION ISSUES AND INHERENTLY GOVERNMENTAL FUNCTIONS PERFORMED BY CONTRACTOR EMPLOYEES ON CONTRACTS TO SUPPLY FUEL TO U.S. TROOPS IN IRAQ, REPORT NO. D2009-D000CH-0244

This provides the Defense Logistics Agency's (DLA) comments on the Department of Defense Inspector General's (DoD IG) draft report, Project No. D2009-D000CH-0244. The draft report covers a series of DLA contracts awarded to International Oil Trading Company (IOTC) for fuel delivered from Jordan to Iraq. We initially note that the draft report cannot address the allegation that IOTC was a "war profiteer", since the DoD IG did not review the specific costs and profit that IOTC actually incurred and realized.

Recommendation A1. We recommend the Director, Defense Logistics Agency Energy, require contracting officers: When contracting for both commercial and noncommercial products and services on the same contract, incorporate Federal Acquisition Regulation clause 52.215-2, "Audit and Records-Negotiation," in the solicitation issued to provide for Defense Contract Audit Agency audit rights for noncommercial products and services being acquired.

DLA response: Concur as written. It is DLA's practice and policy to include these clauses for all products and services that it determines to be noncommercial. DLA non-concurs with the implication that the fuel contracts from Jordan that were the subject of this audit contained any noncommercial products or services.

Recommendation A2. We recommend the Director, Defense Logistics Agency Energy, require contracting officers: Obtain appropriate cost or pricing data and necessary field pricing assistance to support price reasonableness determinations for proposed fuel prices in a contingency operation environment when competition is questionable and a comparable commercial market does not exist.

DLA response: Partially concur as written. DLA policy will be issued in January 2011 to implement agency-wide the provisions of the Defense Procurement and Acquisition Policy Memorandum, dated November 24, 2010, Subject: Improving Competition in Defense Procurements.

Additionally, DLA has, consistent with the September 14, 2010, Under Secretary of Defense (Acquisition, Technology and Logistics) Memorandum, subject: Better Buying Power: Guidance for Obtaining Greater Efficiency and Productivity in

Defense Spending, placed a renewed focus on obtaining the information needed to ensure that contract prices are fair and reasonable.

Federal Acquisition Regulation (FAR) 15.403-1(b)(3) and (c)(3) prohibit the contracting officer from obtaining certified cost or pricing data when purchasing an item that meets the definition of a commercial item. Pursuant to FAR 15.403-3, the contracting officer obtained "information other than cost or pricing data" from IOTC as part of the price reasonableness determination for two of the four contracts at issue, and conducted an extensive analysis of the prices for all four contracts. DLA recommends that the draft report credit the contracting officer for obtaining the same "information other than cost or pricing data" to support the price reasonableness determination for the 2009 IOTC contract that was obtained for the 2004 contract.

DLA non-concurs with the implication that the contracts contained any non-commercial products or services. DLA re-examined the facts and circumstances of these contracts and confirmed that the contracting officer correctly determined that the item being purchased, fuel on an FOB destination basis for delivery to Iraq, was a commercial item. The determination of whether a product is a commercial item is within the sound discretion of the contracting officer. The FAR definition of commercial item does not exclude items purchased in, or delivered to, war zones. The commercial item definition focuses on the item purchased, not where it is to be used. Statute and regulation support the view that commercial items can be used to support contingency operations. See 41 USC 428a (d), FAR 13.500(e).

Offerors, including IOTC, had to establish a supply chain that included purchase of the fuel, transportation, storage, loading and unloading of the fuel, and trucking the fuel to destination. The IG states that there is no commercial market for the delivery of fuel into a war zone. However, Iraq's refining capacity did not meet the country's need and Iraq had to import fuel for its civilian use, which was then transported by truck to locations throughout the country. Thus, truck transportation was a commercial service in Iraq, even during war time. Notwithstanding the determination for these contracts, DLA will remind contracting officers that such situations should be closely reviewed before any commerciality determination is made.

Recommendation B1. We recommend the Director, Defense Logistics Agency Energy, require contracting officers: When using Free-On-Board Destination-type contracts at contractor-run Defense Logistics Agency Energy capitalized fuel support points, either appoint a contracting officer's representative to perform the acceptance function, assign the responsibility to the Defense Contract Management Agency, or enter into a documented agreement with the organization overseeing the fuel support

point contractor that requires that only Government employees accept the fuel.

DLA response: Partially concur. DLA recognizes that acceptance is an inherently governmental function. DLA designated Government officials to review and accept product delivered under the contracts. DLA non-concurs with the implication that it had control over the fuel receipt function in Iraq. DLA had no such control. The governing directive places substantial responsibility for receipt of fuel on the Combatant Commands and Military Services. Pursuant to DoD Directive 4140.25, DoD Management Policy for Energy Commodities and Related Services (2004), Section 5.4.2, the Combatant Commands shall: "Plan and manage, in coordination with the Director, DLA, the intra-theater and inter-theater receipt, storage, and distribution of petroleum products." Section 5.4.5 provides that the Combatant Commands shall: "Establish and maintain a quality program for receipt, storage, and issue of Military Service and DLA-owned products in accordance with [DoD 4140.25-M, DoD Management of Bulk Petroleum Products, Natural Gas, and Coal]." Section 5.5.1 mandates that the Military Services will: "Provide for the operation of petroleum facilities under their cognizance; control the receipt, issue, and management of petroleum stocks at operating locations in coordination with the DLA."

DLA is currently examining options for ensuring compliance with the requirement that acceptance be performed by Government personnel. DLA will take steps to ensure that, when Government personnel are designated to perform the acceptance function, it is in fact these personnel performing that function and not contractor personnel.

It should be noted, however, that in the case of the IOTC contracts, DLA did not make the decision to rely on the Army support contractor to receive fuel. It was the Army that made the fuel receipt decisions.

Recommendation B2. We recommend the Director, Defense Logistics Agency Energy, require contracting officers: Develop procedures to ensure that the acceptance documentation requirements identified in its contracts are complied with.

DLA response: Concur. DLA will ensure future solicitations reflect receipt and acceptance procedures in effect during the performance of the contract.

DLA Additional Comments

The draft IG report incorrectly states that DLA paid $160 to 240 million more to IOTC than could be supported by price analysis. This claim is not supported by analysis performed in accordance with FAR requirements. The contracting officer

utilized the techniques and procedures identified in the FAR to analyze prices and determined that the prices were fair and reasonable.

The contracting officer's primary concern is the overall price the Government will actually pay. A fair and reasonable price determination does not require agreement be reached on every element of cost, nor is it required that the agreed price be within the contracting officer's initial negotiation position. To support the fair and reasonable price determination for the contracts, the DLA contracting officer compared proposed prices received in response to the solicitation, previously proposed prices and previous contract prices for similar items, and information other than certified cost or pricing data from IOTC and relied upon advisory recommendations provided by DLA support offices.

For this IG audit, DLA provided detailed information to the IG to explain the fuel market, industry pricing, and price analysis for fuel contracts in general. However, the draft report relies on what it calls the non-fuel component of IOTC's first contract to state that all future contracts should have contained that same figure, and that any figure above that could not be supported by price analysis. However, the non-fuel components of fixed-price contracts can vary over the course of four years, depending on the offeror's costs and perceived performance risks. Based on the available facts, there is no basis to conclude that the non-fuel component of the contract prices was other than fair and reasonable.

It should be noted that IOTC's contract award prices declined for each of the three contracts negotiated after the first contract award, which the draft audit report credits as having been documented properly. In addition, in many instances during the contract performance periods, the prices that DLA Energy negotiated with IOTC for deliveries into a war zone were less than prices on the West Coast of the United States.

The draft report also uses an alternative calculation by comparing IOTC's prices with the lowest price received under each solicitation. This approach, however, does not take into account that these lower priced offers were from offerors who the contracting officer determined were not capable of performing the contracts, a conclusion not questioned in the draft report. These prices thus cannot serve as any sort of benchmark against which to compare IOTC's contract prices. The overpayment analysis is also unsupported by an analysis of IOTC's actual costs. We note that IOTC cooperated with congressional investigators, who concluded that IOTC's profits over the duration of the contracts may have been 14 per cent. The FAR does not limit profit in a fixed-price contract.

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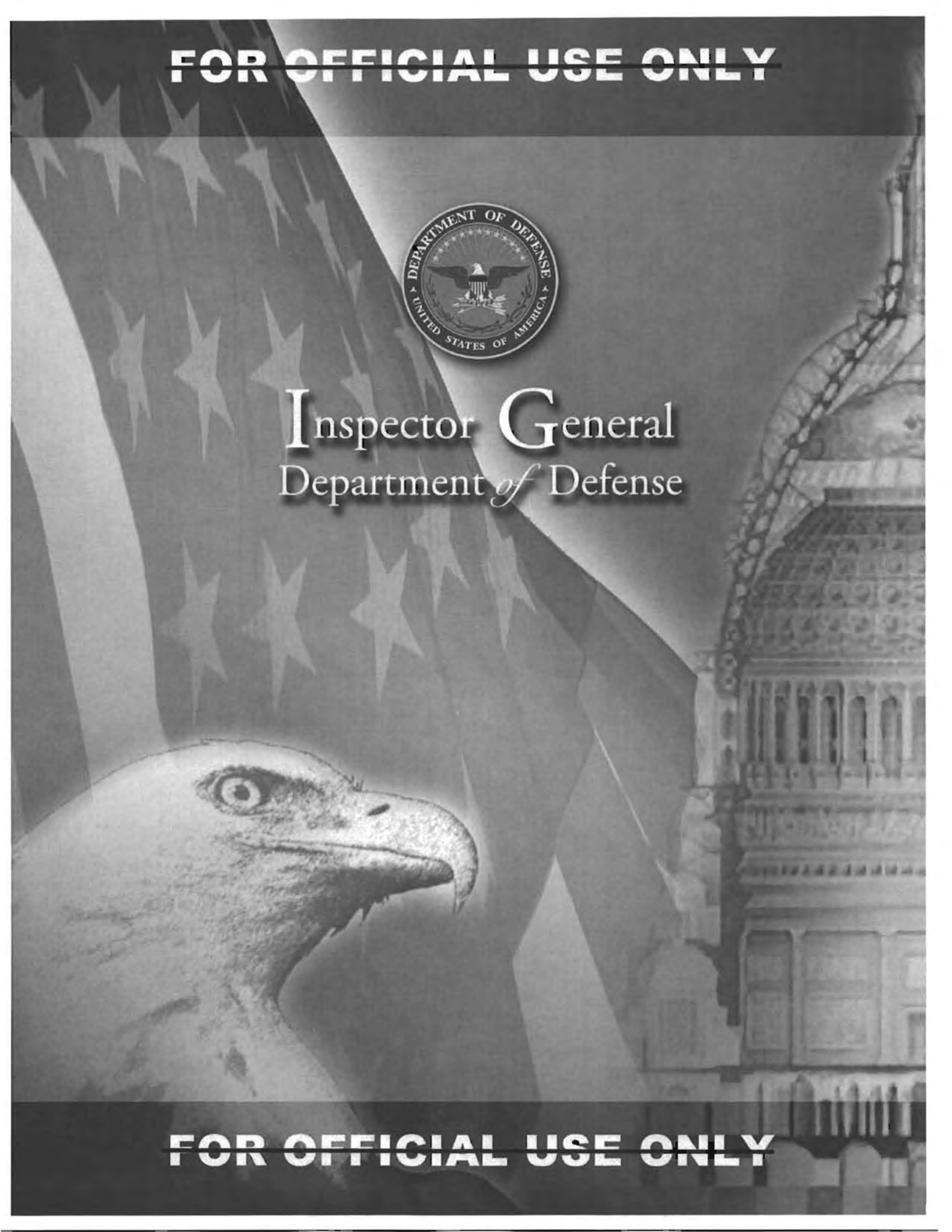

Inspector General
Department of Defense

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