DEPARTMENT OF THE AIR FORCE
HEADQUARTERS SPACE AND MISSILE SYSTEMS CENTER (AFMC)
LOS ANGELES, CA

12 OCT 2000

MEMORANDUM FOR RECIPIENTS OF SMC/PK INFORMATION LETTERS

FROM: SMC/PKX

SUBJECT: Award Fee Funding

1. The attached SAF/AQC memorandum, dated 23 Aug 00, provides guidance on award fee funding and discusses the findings of a recent AFAA Report on the same subject. In addition, the memorandum discusses and provides excerpts from the soon to be released policy on award fee funding; Air Force Instruction (AFI) 65-601, *Budget Guidance and Procedures*, Volume 1, Chapters 8 and 13.

2. In summary, award fee funds are committed as a contingent liability, **not obligated**. Award fees are funded by establishing a contingent liability at the beginning of each award fee period and subsequently obligating the award fee amount earned after final determination of the Fee Determining Official (FDO).

3. It is requested that you ensure award fee funds are **not obligated** until the FDO has made a final determination. Please disseminate this information letter to all your personnel.

4. Any questions may be directed to Ms. Bobbie Aikels, SMC/PKXF, at ext. 3-6984 or Ms. Pat Herrick, SMC/PKXF, at ext. 3-6986.

GAIL VRANICAR
Chief
Resource Management Division
Directorate of Contracting

Atch:
SAF/AQC Memo, 23 Aug 00

cc:
SMC/JAQ
/FM
All Price Analysts
SPO Directors

CY 00-B

DEPARTMENT OF THE AIR FORCE
WASHINGTON, DC

Office Of The Assistant Secretary

2 3 AUG 2000

MEMORANDUM FOR ALMAJCOM-FOA-DRU (CONTRACTING)

FROM: SAF/AQC
1060 Air Force Pentagon
Washington, DC 20330-1060

SUBJECT: Air Force Audit Agency (AFAA) Report No. 98064024, 27 Mar 00, Award Fee Management on Commercial Activity Contracts

Award fees are funded by establishing a contingent liability at the beginning of the award fee period and subsequently obligating the award fee amount after approval from the fee determining official. Maintaining potential award fee funds as commitments (contingent liabilities) ensures funds are accurately and properly identified in Air Force accounting records and reduces the potential for overstating obligations. AFAA Report No. 98064024, dated 27 Mar 00, entitled "Award Fee Management on Commercial Activity Contracts," identified improper procedures for funding of award fees and inaccurate guides. Therefore, please rescind all MAJCOM/FOA/DRU policies, instructions, and/or guidance from Award Fee Guides, Supplements, Pamphlets and Handbooks that allow or permit the obligation of award fee funds at the beginning of an award fee period.

The AFAA report cites several findings regarding the administration of award fee funds. Specifically, award fee officials did not commit funds to establish a contingent liability for the potential award fee amount for each period. Instead, the entire award fee amount was recorded as obligations, or actual liabilities at the start of each award fee period. This practice resulted in a significant overstatement of obligations. In some instances, no action was initiated to deobligate award fee funds which could have been used elsewhere. The audit report stated that contracting activities/centers relied on MAJCOM/FOA/DRU Award Fee Guides or other similar guides that incorrectly allowed the obligation of award fee funds at the beginning of the period. Additionally, the report found that obligating award fee funds at the beginning of the period became a method of "protecting" unobligated award fee funds from being diverted to other priorities.

SAF/FM has implemented new policy that will soon be released in a revision of Air Force Instruction (AFI) 65-601, *Budget Guidance and Procedures*, Volume I, Chapters 8 and 13. The new policy in paragraphs 8.3.1 and 13.4.3 states, "Until the determination has been made that a contractor is due an award fee, the award fee funds are committed as a contingent liability, not obligated. (See DoD 7000.14R, Vol 3, Chapter 8, Paragraph 080202)." Attached are excerpts from the pending revision of AFI 65-601.

If you have any question regarding this matter, my point of contact is Maj Skip Solis, SAF/AQCO, DSN 425-7024, COMM (703) 588-7024, email: skip.solis@pentagon.af.mil.

TIMOTHY A. BEYLAND
Acting Deputy Assistant
Secretary (Contracting)
Assistant Secretary (Acquisition)

Attachment:
Excerpts from AFI 65-601

cc:
SAF/AQXA
AFAA/MSP
SAF/FMBMM

13.4.1. Limit reapplying of funds in the second year to cost growth within scope or to requirements which are a bona fide need of the appropriation year as defined by DFAS-DE 7000.4-R. Commands should identify funds above programmed requirements to be obligated in the first year to SAF/FMBIZ and SAF/AQXR, so the Air Force can reapply funds to other priority programs.

13.4.2. MAJCOM Headquarters will control exceptions to incremental programming and financing during execution.

13.4.3. Award fee requirements are planned and budgeted for as a part of the total weapon system cost. Award fees are a bona fide need of the same fiscal year and appropriation that finances the related effort on which the award fee is based. To comply with RDT&E incremental funding policy, award fee requirements must be budgeted for and funded with the same fiscal year funds as the increment of associated effort. **Until the determination has been made that a contractor is due an award fee, the award fee funds are committed as a contingent liability, not obligated.** (See DoD 7000.14-R, Vol. 3, Chapter 8, Paragraph 080202)

13.5. Delineating Funding Responsibility Between RDT&E and Procurement Appropriations:

13.5.1. See volume 2A, chapter 1, of DoD 7000.14-R, for guidance on the types of costs RDT&E and related appropriations finance. Also see Chapter 8 of this AFI.

13.5.2. Normally, you should cite RDT&E and procurement funds on separate contracts. However, if that is not practical, you should specify separate tasks in the contract (contract line items) so you'll have documentation on contract accounts and voucher payments tied to specific appropriations.

13.5.3. **General Criteria:** When, after consideration of the following criteria, there is doubt as to the proper assignment of costs between appropriations, the issue should be resolved in favor of using RDT&E funding (DoD 7000.14-R, Volume 2A, Chapter 1, paragraph 010212.B).

13.6. Family Housing. Do not use RDT&E to construct, operate, and maintain family housing at R&D installations or activities.

13.7. Tenant Activities. See chapter 7.

13.8. Managing Uncommitted and Unobligated Balances in RDT&E. Apply the following to make sure approved R&D programs are timely and effective.

13.8.1. HQ USAF may withdraw uncommitted balances at the end of the first year of availability.

13.8.2. Finance validated current and first prior fiscal year cost increases within the program element of the approved program. If the approved program is insufficient, then request reprogramming within Air Force approval authority.

13.8.3. Finance validated cost increases for an expired year within the allocation for the multiple-year period. If funds are not available, the MAJCOM will ask SAF/FM for more money to cover the deficit. Follow procedures in Chapter 6.

13.8.4. The RDT&E appropriation is legally available for up to 2 years for a new obligation. You may incur obligations at any time during the 2 years, if the related action concerns an item authorized in the program authorization and budget authorization (PA or BA) documents issued for the appropriation year. But get SAF/FMBIZ's written approval (and coordinate all requests with AFMC/FM) before using

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8.1.2. Use these appropriations for **new obligations only** for the 3 fiscal years designated in the appropriation act and identified, in the Treasury Department's official symbols and titles for federal accounts. For example, appropriation 570/23010 is available for obligation from 1 October 1999 through 30 September 2002, after which it expires for new obligations. When the appropriation expires, use it only to liquidate obligations and make authorized obligation adjustments for 5 more years under its original Treasury symbol. (See **Chapter 6**.)

8.1.3. If you cannot obligate specific programs within the period for which funds were justified and approved, you must budget any additional funding required to complete them in future years as new requirements.

8.1.4. **3011 Appropriation, Procurement of Ammunition.** This appropriation, also referred to as BP35, provides for procurement of direct and indirect munitions and related equipment (except guided missile warheads). BP35 includes rockets, cartridges, practice bombs, general purpose bombs, spare and repair parts, modifications, flares, small arms, and other miscellaneous items. Items included in the miscellaneous category include Explosive Ordnance Disposal (EOD) demolition explosives, and explosive tool kits (to exclude EOD robots), grenades, nuclear trainers, etc. The 3011 Appropriation (BP35), formerly BP8100 in the Other Procurement, Air Force Appropriation (OPAF) (3080) through FY94, became a separate appropriation in FY95.

8.2. Depot Level Reparables (DLR):

8.2.1. Air Force item managers pay for DLR parts from the Defense Working Capital Fund (DWCF), Supply Management business area. This includes replenishment spares previously procured in the Aircraft Procurement (3010, BP 1500), Missile Procurement (3020, BP 2500) and Other Procurement (3080, BPs 8200, 8300, 8400). Air Force operational activities will use local O&M funds to purchase DLRs from the DWCF.

8.2.2. Don't use the DWCF to pay for:

8.2.2.1. Initial and replenishment spares for munitions coded and managed items financed from the 3010 (BP 1600), 3020 (BP 2600) and 3011(BP 3500) appropriations. Initial spares are also excluded from DWCF.

8.2.2.2. Non-stock listed items, e.g., classified and Contractor Logistics Support (CLS) programs.

8.2.3. Use the DWCF, Reparable Support Division. AFMC will reimburse the DWCF from the central procurement appropriations (3010, 3020 and 3080), based on delivery of the items to the DWCF.

8.3. Full Funding. See DoD 7000.14-R, Vol 2, for guidance on full funding, advance procurement, multiyear procurement, advance Economic Order Quantity, and Engineering Change Orders/Engineering Change Proposals.

8.3.1. **Award fee requirements** are planned and budgeted for as part of the total weapon system cost. Award fees are a bona fide need of the same fiscal year and appropriation that finances the related effort on which the award fee is based. They are inherently inseparable from the work with which they are associated. Therefore, DoD full funding policy mandates award fee requirements be budgeted in and funded with the same appropriation and in the same fiscal year as the associated effort. **Until the determination has been made that a contractor is due an award fee, the award fee funds are**

committed as a contingent liability, not obligated. (See DoD 7000.14-R, Vol. 3, Chpt. 8, Para. 080202.A.)

8.4. Weapon System Engineering. MAJCOMs, installations, Air Force Materiel Command (AFMC Centers) and program offices must select the correct funding category for weapon system engineering. In general, funding covers engineering for development, production, and maintenance.

8.4.1. **Development Engineering.** Use the RDT&E appropriation.

8.4.2. **Production Engineering.** To fund production engineering for items in production, use the applicable budget program (weapon system, modification, support equipment, etc.) from the procurement account which funds production of the end item. The phrase "items in production" means the end item in production is funded in the year the production engineering is to take place. Because weapon system development and production engineering often overlap, you must properly categorize development and production tasks. In general, development engineering tries to achieve or improve system performance; production engineering tries to correct deficiencies in the approved production baseline. Ultimately, you must apply this guidance case by case.

8.4.3. **Maintenance Engineering.** Use the Operation and Maintenance appropriation which funds the operational support of the system or equipment.

8.4.3.1. Maintenance engineering efforts may result in the need to redesign a product or substantially improve its performance (flight characteristics, mission performance parameters, reliability, capacity, etc.). The redesign would be a development engineering task because it improves system performance.

8.4.3.2. You must carefully categorize production and maintenance tasks, which often overlap. In general, production engineering tries to correct deficiencies in a production baseline; maintenance engineering tries to identify deficiencies discovered in postproduction operational service. You will need to decide case by case.

8.5. Exceptions:

8.5.1. Use RDT&E to fund all efforts to improve engine components (a combination of maintenance and development engineering) per Congressional direction (see **Chapter 13**).

8.5.2. Use DWCF to fund development, production, and maintenance engineering services that support an operational commodity item managed by the DWCF Supply business Area. But don't use the DWCF if the engineering effort results from a weapon system production or modification improvement. For example, charge the cost of the engineering effort to the DWCF if the commodity manager needs to reverse engineer the item to improve supportability or competition, or wants to improve the reliability or maintainability of the item itself. If engineering is necessary to do an improved configuration change, charge the engineering cost to the procurement account that bears the cost of the configuration change.

8.6. Modification Engineering. See Section G of this chapter.

Section 8B—*Aircraft (57*3010)*

8.7. Aircraft Structural Integrity Program (ASIP). To fund ASIP tasks for: