



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

ACQUISITION,
TECHNOLOGY
AND LOGISTICS

SEP 05 2007

DPAP/CPF

In reply refer to:
CPF Tracking Number: 2007-O0008

MEMORANDUM FOR COMMANDER, UNITED STATES TRANSPORTATION
COMMAND (USTRANSCOM)
(COMMAND ACQUISITION)

SUBJECT: Civil Reserve Air Fleet (CRAF) Program - Class Deviation from FAR Part 31

I hereby authorize a class deviation from FAR Part 31 for contracts awarded in conjunction with the Civil Reserve Air Fleet (CRAF) program that meet the conditions detailed in Attachment A.

This class deviation applies to all contracts awarded from the date of this deviation through September 30, 2008.

If you have any questions regarding this memorandum, please contact Ms. Robin Schulze, Senior Procurement Analyst at 703-602-0326, or via email at Robin.Schulze@osd.mil.

Shay Assad
Director, Defense Procurement
and Acquisition Policy

Attachments:

- A. Deviation to FAR Part 31 - Contract Price Principles and Procedures
- B. CAS Waiver
- C. 10 U.S.C. § 2324 (e) - Specific Costs Not Allowable



Deviation from FAR Part 31 -Contract Cost Principles and Procedures

This deviation applies to Government contracts awarded in conjunction with the CRAF program. This deviation waives the requirements of FAR Part 31 for contracts in which ALL of the following conditions are met:

- a. The contract is awarded under the CRAF program;
- b. The contract either:
 - (i) Is exempt from the application of the Cost Accounting Standards (CAS); or
 - (ii) Meets the criteria for a waiver from the Cost Accounting Standards (CAS) as provided for at Attachment B of this memorandum, and CAS has been waived for the contract.
- c. If the contract is exempt or receives a CAS waiver, the contract requires that the accounting practices used to prepare the proposals for the initial contract and any modifications:
 - (i) comply with pronouncements of the Uniform System of Accounts (USAR) reported to Department of Transportation (DOT) IAW 14 Code of Federal Regulations (CFR) 241; USTRANSCOM ratemaking procedures contained in carrier cost package instructions; and USTRANSCOM Roundtrip (S1)/One-way (S2) monthly mileage and fuel reports; and
 - (ii) are consistent with the contractor's written and established practices for measuring, assigning, and allocating costs.
- d. The business segment performing the contract is not, at the time of contract award, currently performing on any other contract that is subject to the provisions of FAR Part 31;
- e. The contract requires that the actual costs used for purposes of establishing the initial fixed rates/price and any modifications thereto exclude the types of costs listed at 10 U.S.C. § 2324(e) (and any revisions to this statute as of the date of contract award), which is included as Attachment C to this memorandum. Any reasonable method of estimating such costs is sufficient to meet this requirement.
- f. The contract provides the Government with access to all records related to the accounting practices used to determine the costs and the supporting data for any estimates of unallowable costs.

Waiver of Cost Accounting Standards

See Tab B

10 U.S.C 2324 (e): Specific Costs Not Allowable. -

(1) The following costs are not allowable under a covered contract:

(A) Costs of entertainment, including amusement, diversion, and social activities and any costs directly associated with such costs (such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities).

(B) Costs incurred to influence (directly or indirectly) legislative action on any matter pending before Congress, a State legislature, or a legislative body of a political subdivision of a State.

(C) Costs incurred in defense of any civil or criminal fraud proceeding or similar proceeding (including filing of any false certification) brought by the United States where the contractor is found liable or has pleaded nolo contendere to a charge of fraud or similar proceeding (including filing of a false certification).

(D) Payments of fines and penalties resulting from violations of, or failure to comply with, Federal, State, local, or foreign laws and regulations, except when incurred as a result of compliance with specific terms and conditions of the contract or specific written instructions from the contracting officer authorizing in advance such payments in accordance with applicable provisions of the Federal Acquisition Regulation.

(E) Costs of membership in any social, dining, or country club or organization.

(F) Costs of alcoholic beverages.

(G) Contributions or donations, regardless of the recipient.

(H) Costs of advertising designed to promote the contractor or its products.

(I) Costs of promotional items and memorabilia, including models, gifts, and souvenirs.

(J) Costs for travel by commercial aircraft which exceed the amount of the standard commercial fare.

(K) Costs incurred in making any payment (commonly known as a "golden parachute payment") which is -

(i) in an amount in excess of the normal severance pay paid by the contractor to an employee upon termination of employment; and

(ii) paid to the employee contingent upon, and following, a change in management control over, or ownership of, the contractor or a substantial portion of the contractor's assets.

(L) Costs of commercial insurance that protects against the costs of the contractor for correction of the contractor's own defects in materials or workmanship.

(M) Costs of severance pay paid by the contractor to foreign nationals employed by the contractor under a service contract performed outside the United States, to the extent that the amount of severance pay paid in any case exceeds the amount paid in the industry involved under the customary or prevailing practice for firms in that industry providing similar services in the United States, as determined under the Federal Acquisition Regulation.

(N) Costs of severance pay paid by the contractor to a foreign national employed by the contractor under a service contract performed in a foreign country if the termination of the employment of the foreign national is the result of the closing of, or the curtailment of activities at, a United States military facility in that country at the request of the government of that country.

(O) Costs incurred by a contractor in connection with any criminal, civil, or administrative proceeding commenced by the United States or a State, to the extent provided in subsection (k).

(P) Costs of compensation of senior executives of contractors for a fiscal year, regardless of the contract funding source, to the extent that such compensation exceeds the benchmark compensation amount determined applicable for the fiscal year by the Administrator for Federal Procurement Policy under section 39 of the Office of Federal Procurement Policy Act (41 U.S.C. 435), as amended.



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

OFFICE OF FEDERAL
PROCUREMENT POLICY

August 31, 2007

Mr. Shay D. Assad
Director, Defense Procurement and Acquisition Policy
Department of Defense
Washington, D.C. 20301

Dear Mr. Assad:

This responds to your August 15, 2007 letter to the Cost Accounting Standards (CAS) Board, requesting a waiver for contracts entered into under the Civil Air Reserve Fleet (CRAF) program administered by the United States Transportation Command (US TRANSCOM).

On August 30, 2007, the CAS Board approved the requested waiver subject to the conditions set forth in the enclosure.

In granting this waiver, the CAS Board recognizes that the air carrier industry has a set of established accounting practices that are used by regulatory authorities to monitor financial and operating data. The Board believes that the enclosed waiver conditions, which include requirements for contractors to consistently follow these established industry accounting practices, provide adequate protection for the Government. If any contractor selected for a contract under the CRAF program does not agree to the conditions of this waiver, the contractor will be subject to the CAS requirements, provided it otherwise satisfies the CAS applicability criteria.

Please notify this office, within ninety days after the close of each fiscal year, of the extent and use of this waiver.

Sincerely,

Paul A. Denett
Chair, Cost Accounting Standards Board

Enclosure

Enclosure

Waiver of Cost Accounting Standards

The Cost Accounting Standards are hereby waived for contracts entered into under the authority of the CRAF program that meet all of the following conditions:

1. The business segment performing the contract is not, at the time of contract award, currently performing on any other contract that is subject to the Cost Accounting Standards.
2. The contract must include clauses that:
 - a. Requires the carrier to prepare the proposal for the initial contract and modifications thereto using accounting practices that (i) comply with pronouncements of the Uniform System of Accounts (USAR) reported to Department of Transportation (DOT) IAW 14 Code of Federal Regulations (CFR) 241; USTRANSCOM ratemaking procedures contained in carrier cost package instructions; and USTRANSCOM Roundtrip (S1)/One-way (S2) monthly mileage and fuel reports and (ii) are consistent with the carrier's written and established practices for measuring, assigning, and allocating costs;
 - b. Requires the carrier to disclose, in writing, its established accounting practices for measuring, assigning, and allocating costs to contracts for which CAS has been waived, and to consistently use those disclosed practices to prepare proposal(s);
 - c. Requires the carrier to provide advance disclosure to the Government of any planned cost accounting practice change not less than 60 days prior to implementation of the change; and
 - d. Provides for an adjustment to the contract price if it is later found that the price was increased because the carrier used accounting practices that were in noncompliance with USAR provisions and USTRANSCOM Ratemaking instructions, or were inconsistent with the carrier's written and established practices. The amount of the adjustment shall be the difference between the carrier's negotiated rate using noncompliant cost accounting practices and the rate that would have been negotiated had the carrier used compliant cost accounting practices, multiplied by the number of miles awarded to the carrier. The Government shall be entitled to a credit or cash recovery (at the Government's option) for the amount of the increased price plus interest. The interest shall be computed from the date the payment was made by the Government until the date of repayment by the contractor. The interest rate shall be at the rate specified at 26 U.S.C. 6621(a)(2).

e. Provides the Contracting Officer and his authorized representative access to all relevant contractor records, including but not limited to the accounting practices and cost records in use at the time of the contract award and at the time of modifications thereto and records related to actual fuel usage and fuel cost adjustments that are paid under the contract.

3. The contract must also include the following clause:

The actual costs used for purposes of establishing any price under the contract must exclude all statutory and contractually unallowable costs. Any reasonable method of estimating such costs is sufficient to meet this requirement. Should any unallowable costs be included in the carrier's negotiated rate, the Government shall be entitled to recover the amount of those unallowable costs plus interest from the date payment was made by the United States to the date of repayment by the carrier, in accordance with 26 U.S.C. 6621 (a)(2) and 10 U.S.C 2324.



UNITED STATES TRANSPORTATION COMMAND
508 SCOTT DRIVE
SCOTT AIR FORCE BASE, ILLINOIS 62225-5357

ACQ 10 2007

**MEMORANDUM FOR DIRECTOR DEFENSE PROCUREMENT AND
ACQUISITION POLICY**

FROM: USTRANSCOM -TCAQ

SUBJECT: Civil Reserve Air Fleet (CRAF) Contract – Cost Accounting Standards (CAS) Waiver Request and Related Far Deviation Request

1. References:

- a. Current CRAF Rate Package
- b. Current CRAF Rate Package Instructions
- c. Electronic Link: 14 CFR, Part 241
- d. CRAF Memorandum of Understanding (MOU) and Attachment - Draft
- e. FY07 Final Uniform Rates and Rules
- f. CRAF Milestones

2. This request for CAS waiver is submitted for review and endorsement by Director of Defense Procurement and Acquisition Policy (DPAP) and, upon DPAP approval, forwarding to the Cost Accounting Standards Board for their determination. The Contracting Officer determined that contracts awarded under the CRAF program would be subject to full CAS coverage as defined by 48 CFR 9903.201-2(a) and that a waiver is required in order to facilitate the procurement of program services without service interruption.

3. The CAS waiver is requested for a period of two years beginning with the Fiscal Year (FY) 2008 contracts. USTRANSCOM requires this two year waiver period to facilitate the award of the FY 08 contracts and completion of the analysis, selection and implementation of an alternative acquisition strategy that does not require waiver from CAS for award of the FY 10 contracts. It is anticipated that subsequent procurements will be structured so as to meet one or more of the criteria exemption from CAS at 48 CFR 9903.201-1(b) and, therefore, no additional CAS waivers will be required.

USTRANSCOM is concerned that an alternate acquisition strategy may not be fully implemented in time for the FY 09 contacts award and this would negatively impact the

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critical mission of the CRAF. U. S. Air Force, Air Mobility Command (AMC) transferred contract responsibility to USTRANSCOM on 1 January 2007. Upon review of the contract documentation, USTRANSCOM discovered CAS had neither been incorporated into the contracts nor waived. After further analysis, USTRANSCOM determined the CRAF contract did not meet the criteria for a CAS exemption. And in order to implement an acquisition strategy for future CRAF contracts that meets the criteria for CAS exemption and is appropriate to CRAF operational requirements, several requirements of the contracts, such as fuel cost adjustments, will require additional analysis and possible revision. We have been unable to accomplish this analysis to date. Since assuming responsibility for the program in Jan 07, USTRANSCOM resources have been focused on standing up the organization to support the CRAF program/contract, solicitation and negotiation of proposals, developing FY 08 CRAF rates and supporting the requests for CAS waiver and other related waivers. An award past 7 September 2007 jeopardizes the program and mission execution.

USTRANSCOM has begun exploring alternative acquisition strategies. These strategies must be researched, vetted, and approved within USTRANSCOM. After internal approval, the strategies must then be coordinated with agencies external to USTRANSCOM. If USTRANSCOM makes significant changes to the acquisition strategy, a ripple effect will result, requiring policy revisions, USTRANSCOM supplement rewrite, and possibly public notice requirements. USTRANSCOM is working diligently to ensure a CAS-exempt acquisition strategy will be in place for the FY 09 awards, but cannot guarantee it will come to fruition. To ensure successful mission execution for this vital national defense program, it is prudent to obtain waiver coverage for the FY 09 contracts.

USTRANSCOM requests the waiver be granted for two years. If USTRANSCOM is successful in implementing an alternative acquisition strategy that does not require a CAS waiver prior to the FY 09 contract awards, the CAS waiver will not be used for the additional year. See CAS Business Point Paper, Attachment 1 for alternative strategy development milestones.

4. The proposed CAS waiver has been coordinated through USTRANSCOM JA and there are no legal objections.
5. The CAS waiver would apply only to the contracts awarded under CRAF program and would not apply to any contract awarded to a carrier performing a CAS-covered contract or subcontract at the time of award of a CRAF contract. In addition, accounting practices used to prepare proposals for pricing the initial contract and any modifications must comply in all respects with the Uniform System of Accounts (USAR) of the Department of Transportation, USTRANSCOM ratemaking procedures and instructions, and the carrier's written and established cost accounting practices.
6. This CRAF CAS waiver request includes the attached business case addressing the benefits and risks of waiving CAS for the CRAF program. The CAS Waiver Business

Point Paper was prepared to address specific elements to this contract that make it uniquely different from other contracts and industries doing business within DoD.

7. USTRANSCOM Acquisition representatives are available to respond to your questions and comments with respect to this submission. The point of contact is Susan Sembenotti (618-256-4278).



GAIL M. JORGENSEN
Acting Director, Acquisition

Attachment:
CAS Waiver Business Point Paper

cc:
DCAA HQ
ADUSD/TP(COL Robert S. Guarino)

CAS WAIVER BUSINESS POINT PAPER
CIVIL RESERVE AIR FLEET (CRAF)
UNITED STATES TRANSPORTATION COMMAND

USTRANSCOM requests a waiver from all Cost Accounting Standards (CAS), and a deviation from related Federal Acquisition Regulation (FAR), to include FAR Part 31 provisions for the upcoming CRAF acquisitions. The program has an estimated value of \$2.5 billion annually for fiscal Year (FY) 2008. CRAF is an Indefinite Delivery Indefinite Quantity (IDIQ), contract, in which, USTRANSCOM has been designated the Single Manager Operating Agency for airlift service within DoD. This contract is subject to CAS under 48 CFR 9903.201-1 and has been determined by the Contracting Officer to be non-commercial based on the significant amount of DoD-specific requirements identified in the CRAF Performance Work Statement that directly supports national defense. This non-commercial determination will be revisited in the future as USTRANSCOM is currently looking into the feasibility of moving towards a FAR Part 12 acquisition. There are a number of issues requiring resolution before this could occur but the goal is to transition to FAR Part 12. Atch 1 includes alternative strategy development milestones.

Based on extensive market research, CAS requirements would hinder carriers from participating in CRAF and would negatively impact the Department of Defense's airlift capability both in peacetime and in time of emergency or war. The following discussion addresses how applying CAS would only overlay an administrative burden for both the carriers and USTRANSCOM with no recognizable benefit.

Several factors that pertain directly to the airline industry negate any value of applying CAS to CRAF contracts. Airline carriers who participate in the CRAF program are required by Section 401 of the Federal Aviation Act of 1958, as amended under Federal Aviation Regulation (14 CFR 121), to be certified air carriers. Carriers so certified are required to comply with the Uniform System of Accounts and Reports (USAR) and 14 CFR 241, Section 407(d). USTRANSCOM believes the USAR accomplishes the cost measurement and assignment objectives of the CAS, i.e., providing uniformity and consistency among carriers in the airline industry. The USAR is a regulation system which requires certified carriers to submit their financial and operational data to the Department of Transportation (DOT). This data is required to be certified by a corporate official.

The USTRANSCOM instructions to carriers, specifically the International USTRANSCOM Ratemaking Methodology (attachment 2), specifies the methods to be used in allocating indirect costs for all participating carriers and no other methods are acceptable in the ratemaking process. Therefore, we believe these requirements accomplish the CAS Board's objective of achieving uniformity and consistency with respect to cost allocations.

The nature of the CRAF contract effort, coupled with specific contract requirements of this acquisition, and USAR provisions mitigate any increased risk that would otherwise result from a CAS waiver. To support USTRANSCOM's position for a waiver and satisfy criteria outlined in FAR 30.201-5(c), this BPP will detail the following areas:

1. Background

2. Contract program structure
3. Rate-Making Process
4. USAR
5. General Deviation from FAR Part 31
6. Risk Mitigation for Waiving CAS
7. Conclusion

The first three paragraphs listed above, will exhibit the complex and unique characteristics of the CRAF contract and the airline industry. In particular, the benefits of using a uniform rate to meet requirements and enable USTRANSCOM to react promptly during cargo and passenger airlift surges. The remaining paragraphs will demonstrate how USAR supports uniform rate procedures while providing the Government a fair and reasonable price.

I. Background: The purpose of the CRAF program is to establish an industrial mobilization base of support aircraft in time of emergency or war. This is accomplished through a voluntary contractual program where civilian air carriers agree to augment organic military airlift capacities to support mobilizations in time of emergencies in exchange for peacetime DoD business. This wartime requirement includes long and short-range international service for DoD passenger and cargo business. A contingency rate is set for aeromedical rates since this program has no peace time business.

The Civil Aeronautics Act of 1938 recognized the relationship between the DoD and the airline industry. An objective of the Civil Aeronautics Act was to encourage and develop an airline industry to meet the future and present needs of foreign and domestic commerce, postal service and the National Defense. The Federal Aviation Act of 1958 established the Federal Aviation Agency as the regulator of safety and the Civil Aeronautics Board as an economic regulator of the airline industry. In 1960 the DoD implemented presidential approved courses of action that directed the DoD to procure airlift only from carriers under the economic regulation of the Civil Aeronautics Board. The CAB provided economic regulation that established minimum rates for DoD business up until the Airline Deregulation Act of 1978. Historically, before the deregulation of the airline industry in 1978, the Civil Aeronautics Board (CAB) set uniform minimum rates for the industry and DoD contracts which protected carriers from the threat of bankruptcy.

The CAB, and its authority to regulate carrier rates in accordance with 14 CFR 288, was terminated by the Airline Deregulation Act of 1978. However, the USAR established by the CAB was retained by the Bureau of Transportation Statistics (BTS) under the direction of the DOT. However, with the demise of CAB, DoD did not have a regulating agency to set minimum rates to use in the contract for DoD business. The Military Airlift Command (MAC) assumed the responsibilities of contracting peacetime business in support of the CRAF program. Subsequently, MAC became the Air Mobility Command (AMC) and in January 2007, the responsibility was transferred over to USTRANSCOM.

After the CAB was terminated, the Government needed a process to set fair and reasonable uniform rates in support of the CRAF program. Since this was a transition period from a regulated industry and time was limited, MAC, continued to use CAB methodologies in

establishing DoD uniform rates while studying other options of maintaining a robust CRAF program and acquiring peacetime business at fair and reasonable rates.

Air Force studied alternative methods for pricing CRAF contracts and MAC conducted an in-house cost benefit analysis to review the impact of competitive pricing on DoD peacetime business and the maintenance of a CRAF program. Industry also provided studies and proposed preferences for pricing of the CRAF program and DoD peacetime business. As a result of these reviews, neither the Government nor the CRAF carriers were able to identify an adequate alternative to the CAB's established ratemaking methodology. Several subsequent studies have come to the same conclusion -- a uniform rate is the best approach for maintaining a viable CRAF program and acquiring peacetime DoD business at fair and reasonable rates based on carrier's cost who participate in the CRAF peacetime airlift business. Since 1979, the Government has been using the methods established by CAB to set rates on CRAF acquisitions.

USTRANSCOM currently incorporates the economic theories of the CAB ratemaking, through a Memorandum of Understanding (MOU) that establishes guidelines, which emulates the CAB economic philosophies. The Government's goal is to establish uniform rates for DoD business, using the Department of Transportation's unified system of accounts and reports (USAR) to provide uniformity and consistency, much like the CAB did when it conducted its' regulatory ratemaking process. USTRANSCOM does not conduct a sole source negotiation, but rather, negotiates a bottom line rate with each carrier and then executes a certificate of current cost and pricing data for that negotiated price. Each individual carrier's rate is then weight averaged based on carrier's CRAF revenues into a single worldwide rate applicable to all CRAF carriers.

The economic theory of a uniform rate is to create an incentive for all carriers to become more cost efficient. Carriers increase profits by reducing overall operating cost. Inefficient carriers may make little to no profit while efficient carriers will maximize profits.

2. Contract Award/Program Structure: As mentioned previously, the CRAF program is a partnership between the DoD and civil air carriers whereby peacetime business is given to carriers that place aircraft in the Civil Reserve Air Fleet for use in times of emergency. This capability is required to augment the military capacity of AMC during peacetime and the establishment of a mobilization base of aircraft that will be available to DoD to respond to progressively ascending requirement levels. Currently, there are three levels/stages of activation:

- Stage I: Lesser regional contingency
- Stage II: Single major regional contingency, and
- Stage III: Multiple major regional contingencies

The commander, USTRANSCOM, with the approval of the Secretary of Defense or the Secretary's designee, may activate any stage of CRAF during national emergencies and defense-oriented situations when expanded civil augmentation of military airlift activity is required. Once activation of a stage is approved, Commander, USTRANSCOM may activate and deactivate the segments (e.g., international, aeromedical), sections (e.g., long or short range) or elements (passenger and/or cargo) within the stage as required.

During the course of the CRAF program, there have been two activations. The first activation was in support of Operation Desert Shield/Storm in 1991, in which both the passenger and cargo elements were activated through stage II. The most recent activation was from February through June 2003 in support of Operation Enduring Freedom/Iraqi Freedom. During this activation, only the passenger element was mobilized through stage I. These two activations highlighted the importance of having a uniform rate. Contractually and fundamentally, there is no discussion or negotiation of rates from peacetime to contingency, because rates are pre established for CRAF activation. Thus, having a contingency rate eliminates negotiation time and prevents ambiguity and allows the Government to respond quickly to emergencies. The Navy established a VISA program after Desert Shield/Storm for the Sealift industry based on the success of the CRAF program.

Another important aspect of the CRAF program is Mobilization Value Points (MVP). In order to receive contract awards carriers must commit a minimum percent of their fleet to the CRAF program. For passenger aircraft the minimum is 30% and for cargo it is 15%. For each aircraft committed to CRAF, carriers are assigned MVPs in proportion to aircraft performance capability. The use of MVP is then tied to peacetime awards, or rather, the overall MVP percentage for that carrier is based on their fleet committed to CRAF. This determines their percentage of revenue awarded on CRAF for a given year of the contract.

The Government bases contract awards for transportation to CRAF participants based on the number of MVP points assigned. These awards provide for known and determinable amounts of revenue to be received during the contract period in exchange for air transportation service. The goal is provide peacetime dollars proportionate to a carriers CRAF commitment.

3. Rate-Making Process: Contract rates under the CRAF program are established pursuant to the MOU¹ between carriers and USTRANSCOM. This structure emulates the minimum price structure set by CAB during regulation and is constructed using the DOT's uniform standard system of accounts and reports (USAR) to provide uniformity and consistency, much like CAS.

The term of the Ratemaking MOU is in five year increments. The current MOU is being negotiated and will take affect for FY 2008 though FY 2012. Before a carrier can receive an award on the FY 2008 CRAF contract, they must sign the MOU.

Carriers that receive revenues of five million dollars or more in business for one aircraft type as of July of the current contract period are required by the MOU to complete a rate package.² This rate package is a USTRANSCOM policy and is the required format. No other format is allowed at this time to include Table 15-2 under FAR 15.408. Consequently, carriers receiving less than the five million dollar threshold have the option of voluntarily submitting a rate package. Regardless of whether the rate package is required or voluntary, it is considered certified cost and pricing data and 1AW 15.403-4 and 15.406-2 carriers are required to certify. In addition, CRAF is subject to the Truth in Negotiations Act (TINA) at this time. The contracting officer will also be requesting a TINA waiver from USTRANSCOM's HCA.

¹Reference d, from cover letter titled "Current Memorandum of Understanding (MOU) and Methodology - Draft"
²Reference a, from cover letter titled "Current CRAF Rate Package"

Upon completion and submission of rate packages by carriers, which are based on Form 41 data submitted to the department of transportation, the Defense Contract Audit Agency (DCAA) is requested to verify the Form 41 data to the carrier's accounting and operating records. In addition to verifying carrier Form 41 data, DCAA has historically verified data included in carrier proposals for fuel adjustments, accounting for fixed assets, and claims when requested to do so by the contracting officer.

An initial or "Proposed" rate for CRAF is issued in the March-April timeframe. Each of the three classes under passenger and cargo have their own single, weight averaged, rate. These proposed rates are negotiated between the USTRANSCOM analyst and carrier and final negotiations will contribute to the "Final" rate³ released in the June-July timeframe. In addition to points discussed, the Final rate, also, contains changes made to escalation, fuel prices, and other ancillary contributors to the rate. The negotiated rates are weighted based on each carrier's AMC revenues from the base period and consolidated into the fixed rate for each class of aircraft and are incorporated into each IDIQ contract under the CRAF program.

4. Uniform System of Accounts and Reports (USAR): The Government relies on USAR to verify both operational and financial data. As described above, USAR is administered by BTS under the direction of the DOT. BTS separates airlines into three major groups based on their annual operating revenues. The majority of CRAF carriers fall in Groups II and III, which are the two largest groups and have revenues in excess of one-hundred million. These groups submit monthly income statements, quarterly balance sheets, profit and loss statement, changes in financial position and operating expense reports. They also submit fuel reports and annual audit reports in accordance with the ratemaking procedures discussed in paragraph 3 above. In addition under USAR, carriers are required to report financial and operating data separately for each type of aircraft and geographic area served.

We believe that USAR requires that carriers comply with a formal reporting process that provides detailed financial and operating data and information. USAR also incorporates general accepted accounting principles (GAAP) and any new policies that derive from the Financial Accounting Standards Board (FASB) are incorporated unless the director issues an Accounting Directive making an initial determination that implementation of a new pronouncement would adversely affect the Department's programs. Because carriers are required by law to file the BTS Form 41, it is a misdemeanor for carriers to falsify their reports. Due to BTS' reporting procedures and USAR format, USTRANSCOM believes this more than suffices for waiving CAS and eliminates any risk involved due to the stringent reporting procedures and penalties constituted for fraudulent submissions. Furthermore, this method is tailored directly to the airline industry and CRAF carriers, whereas, CAS is a more generalized method tailored toward the manufacturing & services industries. For this reason, USTRANSCOM has concluded that having carriers abide by CAS would only duplicate most of what the BTS requires and would unnecessarily restrict participation in the CRAF program, increase carrier costs and result in duplicate oversight by USTRANSCOM.

Additionally, USTRANSCOM can build a rate from the Form 41 data without carrier input or the separate submission of a rate package. This is done for our aeromedical rate categories and

³ Reference e. from cover letter titled "FY07 Final Uniform Rates and Rules"

recently with our small class cargo rate. For the small cargo class and aeromedical, these rates are on record only and there have not been nor are there anticipated to be any peacetime requirements under these categories. The only time aeromedical service would be used is during an activation of stage II or III. Since the first published rate in 1994, aeromedical has not been activated. For this reason, it would be time consuming for a carrier to submit an annual rate package and subject it to an audit if it will not be utilized. Instead, USTRANSCOM builds a rate from the Form 41 data and presents it to the carriers for comment and negotiation, and the agreed rate becomes final for that contract year. This further demonstrates the importance of USAR to CRAF and illustrates the need for a CAS waiver.

5. General Deviation from FAR Part 31. This deviation applies to Government contracts awarded in conjunction with the CRAF program. This deviation waives the requirements of FAR Part 31 for contracts in which ALL of the following conditions are met:

- a. The contract is awarded under the CRAF program;
- b. The contract either:
 - (1) Is exempt from the application of the Cost Accounting Standards (CAS); or
 - (2) Meets the criteria for a waiver from the Cost Accounting Standards (CAS) as provided for in this BPP, and CAS has been waived for the contract.
- c. If the contract is exempt or receives a CAS waiver, the contract requires that the accounting practices used to prepare the proposals for the initial contract and any modifications:
 - (1) Comply with pronouncements of the Uniform System of Accounts (USAR) reported to Department of Transportation (DOT) IAW 14 Code of Federal Regulations (CFR) 241; USTRANSCOM ratemaking procedures contained in carrier cost package instructions; and USTRANSCOM Roundtrip (S1)/One-way (S2) monthly mileage and fuel reports. These requirements are used for measuring, assigning, and allocating system costs to the CRAF Program; and
 - (2) are consistent with the carrier's written and established practices for measuring, assigning, and allocating costs.
- d. The business segment performing the contract is not, at the time of contract award, currently performing on any other contract that is subject to the provisions of FAR Part 31;
- e. The contract requires that the actual costs used for purposes of establishing the initial fixed rates price and any modifications thereto exclude the types of costs listed at 10 U.S.C. § 2324(e) (and any revisions to this statute as of the date of contract award), which is included at paragraph 6d. Any reasonable method of estimating such costs is sufficient to meet this requirement IAW FAR 31.201-6, Accounting for Unallowable Costs.
- f. The contract provides the Government with access to all records related to the

accounting practices used to determine the costs and the supporting data for any estimates of unallowable costs.

6. Risk Mitigation for Waiving CAS. The contract will include clauses that:

a. Requires the carrier to prepare the proposal for the initial contract and modifications thereto using accounting practices that (i) comply with pronouncements of the Uniform System of Accounts (USAR) reported to Department of Transportation (DOT) IAW 14 Code of Federal Regulations (CFR) 241; USTRANSCOM ratemaking procedures contained in carrier cost package instructions; and USTRANSCOM Roundtrip (S1)/One-way (S2) monthly mileage and fuel reports and (ii) are consistent with the carrier's written and established practices for measuring, assigning, and allocating costs;

b. Requires the carrier to disclose, in writing, its established accounting practices for measuring, assigning and allocating costs to contracts for which CAS has been waived, and to consistently use those disclosed practices to prepare proposal(s);

c. Requires the carrier to provide advance disclosure to the Government of any planned cost accounting practice changes not less than 60 days prior to implementation of the change; and

d. Provides for an adjustment to the contract price if it is later found that the price was increased because the carrier used accounting practices that were in noncompliance with USAR provisions and USTRANSCOM Ratemaking instructions, or were inconsistent with the carrier's written and established practices. The amount of the adjustment shall be the difference between the carrier's negotiated rate using noncompliant cost accounting practices and the rate that would have been negotiated had the carrier used compliant cost accounting practices, multiplied by the number of miles awarded to the carrier. The Government shall be entitled to a credit or cash recovery (at the Government's option) for the amount of the increased price plus interest. The interest shall be computed from the date the payment was made by the Government until the date of repayment by the carrier. The interest rate shall be the rate specified at 26 U.S.C. 6621(a)(2).

d. The actual costs used for purposes of establishing any price under the contract must exclude all statutory and contractually unallowable costs. Any reasonable method of estimating such costs, including a statistical sample of carrier costs projected to the total cost universe, is sufficient to meet this requirement. Should any unallowable costs be included in the negotiated price, the Government shall be entitled to recover the amount of those unallowable costs plus interest from the date payment was made by the United States to the date of repayment by the carrier, in accordance with 26 U.S.C. 6621 (a)(2) and 10 U.S.C 2324.

10 U.S.C 2324 (e): Specific Costs Not Allowable. -

(1) The following costs are not allowable under a covered contract:

- (A) Costs of entertainment, including amusement, diversion, and social activities and any costs directly associated with such costs (such as tickets to shows or sports events, meals, lodging, rentals, transportation, and gratuities).
- (B) Costs incurred to influence (directly or indirectly) legislative action on any matter pending before Congress, a State legislature, or a legislative body of a political subdivision of a State.
- (C) Costs incurred in defense of any civil or criminal fraud proceeding or similar proceeding (including filing of any false certification) brought by the United States where the contractor is found liable or has pleaded nolo contendere to a charge of fraud or similar proceeding (including filing of a false certification).
- (D) Payments of fines and penalties resulting from violations of, or failure to comply with, Federal, State, local, or foreign laws and regulations, except when incurred as a result of compliance with specific terms and conditions of the contract or specific written instructions from the contracting officer authorizing in advance such payments in accordance with applicable provisions of the Federal Acquisition Regulation.
- (E) Costs of membership in any social, dining, or country club or organization.
- (F) Costs of alcoholic beverages.
- (G) Contributions or donations, regardless of the recipient.
- (H) Costs of advertising designed to promote the contractor or its products.
- (I) Costs of promotional items and memorabilia, including models, gifts, and souvenirs.
- (J) Costs for travel by commercial aircraft which exceed the amount of the standard commercial fare.
- (K) Costs incurred in making any payment (commonly known as a "golden parachute payment") which is -
 - (i) in an amount in excess of the normal severance pay paid by the contractor to an employee upon termination of employment; and
 - (ii) is paid to the employee contingent upon, and following, a change in management control over, or ownership of, the contractor or a substantial portion of the contractor's assets.
- (L) Costs of commercial insurance that protects against the costs of the contractor for correction of the contractor's own defects in materials or workmanship.
- (M) Costs of severance pay paid by the contractor to foreign nationals employed by the contractor under a service contract performed outside the United States, to the extent that the amount of severance pay paid in any case exceeds the amount paid in the industry involved

under the customary or prevailing practice for firms in that industry providing similar services in the United States, as determined under the Federal Acquisition Regulation.

(N) Costs of severance pay paid by the contractor to a foreign national employed by the contractor under a service contract performed in a foreign country if the termination of the employment of the foreign national is the result of the closing of, or the curtailment of activities at, a United States military facility in that country at the request of the government of that country.

(O) Costs incurred by a contractor in connection with any criminal, civil, or administrative proceeding commenced by the United States or a State, to the extent provided in subsection (k).

(P) Costs of compensation of senior executives of contractors for a fiscal year, regardless of the contract funding source, to the extent that such compensation exceeds the benchmark compensation amount determined applicable for the fiscal year by the Administrator for Federal Procurement Policy under section 39 of the Office of Federal Procurement Policy Act (41 U.S.C. 435), as amended.

e. The contract includes a clause that provides the Contracting Officer and authorized representative access to all relevant contractor records, including but not limited to the accounting practices and cost records in use at the time of the contract award and at the time of modifications thereto.

7. **Conclusion:** At this time, we believe the best interest of the Government is served by the continued recognition of USAR as the industry's standardized accounting and reporting system, development of uniform rates based on the MOU provisions, and CAB ratemaking methodologies. USTRANSCOM's uniform pricing methodology has a proven track record (27 years) to produce fair and reasonable rates for the CRAF program. The application of CAS would only overlay an administrative burden for the CRAF carrier and Government with no recognizable benefit. Since there is not a significant difference between CAS and the combination of the USAR and CRAF ratemaking instructions, we believe that contracts awarded under the CRAF program should be waived from CAS.

6. Attachments:

1. CRAF Alternative Strategy Development Milestones
2. Current Memorandum of Understanding (MOU) and Methodology - Draft
3. Current CRAF Rate Package
4. FY07 Final Uniform Rates and Rules
5. Current CRAF Rate Package Instructions
6. CRAF Milestones