PRICE NEGOTIATION MEMORANDUM

1. **SUBJECT:**

   a. Solicitation SP0600-04-R-0054-0002 with Amendments 0001-0004, Supply of JP8 to the U.S. military in Iraq. (Purchase Program Number 2.99)

   b. Contract Number: SP0600-04-D-0506

      Company: International Oil Trade Center (IOTC)
      P.O. Box [redacted]
      Amman, Jordan

   c. Bidder Code: I427

   d. Cage Code: SW114

   e. DUNS: still obtaining

   f. Estimated Total Dollar Value: $76,860,000.00

   g. Delivery Period:

      Basic Period: June 15, 2004 through December 31, 2004, plus 30-day carryover

2. **INTRODUCTORY SUMMARY:**

   a. Particulars: The particulars of this procurement are outlined in the Prenegotiation Briefing Memorandum at TAB 23. The offer evaluation at TAB 29 also forms a part of this Price Negotiation Memorandum (PNM). Although this document addresses only the results of negotiations conducted with IOTC, any exceptions taken by offerors competing with IOTC have either been removed, or determined to be minor or insignificant. Results of negotiations and exceptions taken by each successful offeror are included in the individual PNM located at TAB 24 of each offeror's file. Unsuccessful offers are filed at TAB 34 of the Preaward File.

   b. Negotiations: Negotiations on price and terms and conditions were opened on May 26, 2004 and closed on June 8, 2004. Negotiations were conducted by telephone, e-mail and facsimile between the following individuals:

DESC-BZD	IOTC
Sonja Varricchione Contract Specialist	Mr. William Mauco Lead Negotiator
Joy Mullori Contracting Officer	Mr. Harry Sargeant, Jr. Partner/Owner
Donald E. Peschka Chief, Bulk Fuels Division	

3. **NEGOTIATION SUMMARY:**

a. IOTC did not provide a DUNS number with its offer. DESC requested that IOTC apply for a DUNS number. IOTC experienced difficulties in applying for the DUNS number and is still in the process of obtaining one.

b. DESC requested that IOTC submit an Offer Submission Package. IOTC submitted the Package and subsequently completed additional information on the Taxpayers Identification Number.

c. IOTC provided the authorization letter from the Jordanian government and explained the relationship between itself, National Resources Development Company, and Trafigura Ltd all of which are referenced in the offer or have submitted information to DESC in support of IOTC's offer.

d. IOTC advised in its initial offer that it would be unable to deliver the full quantity estimated for the first two weeks of the contract period. However, IOTC withdrew this condition during negotiations and confirmed it would be able to deliver the full quantity estimated for the entire delivery period.

4. **PROPOSED AWARD:**

The following items constitute the products and quantities to be supplied during the basic contract period. Actual performance would commence in late June 2004.

CLIN	PRODUCT	ESTIMATED QUANTITY (USG)	MODE	O/D	RECEIVING ACTIVITY LOCATION/ FOB POINT	EFFECTIVE JAN 1, 2004 BASE UNIT PRICE (USD/USG)	ESTIMATED DOLLAR VALUE
013-KI	Turbine Fuel, Aviation (JP8)	21,960,000	TT	D	Al-Asad, Iraq	$2.10	$46,116,000
014-KI	Turbine Fuel, Aviation (JP8)	14,640,000	TT	D	Al-Taquddem, Iraq	$2.10	$30,744,000
							TOTAL ESTIMATED DOLLAR VALUE: $76,860,000

5. **DELIVERY CONDITIONS:**

All delivery conditions were determined acceptable or withdrawn.

6. **TRADE AGREEMENTS ACT (TAA):** In accordance with DFAR 225.403 (c)(i)(A), a Trade Agreements Act waiver was prepared.

7. **PRICE REASONABLENESS DETERMINATION:**

NOTE: DESC originally attempted to negotiate an international agreement with the Jordanian Government for the purchase and transport of JP8 to the U.S. Military in Iraq. Negotiations failed because the price offered by the Jordanian Government was substantially higher than DESC anticipated receiving through solicitation and purchase in the commercial market. The final price offered by the Jordanian Government was $3.44 comprised of $1.51 for the fuel and $1.93 for the transportation.

Supplies offered by IOTC are technically acceptable and agreement was reached on all terms and conditions as set forth herein. However, the Contracting Officer cannot determine IOTC's final offer price of $2.10 per gallon reasonable as required by FAR 15.402. Although the requirement for JP8 delivered to the U.S. Military in Iraq is urgent and compelling, DESC did synopsize and post the solicitation to FEDBIZOPPS to allow for the fullest amount of competition given the time constraints. DESC notified 11 known offerors via facsimile of the requirement. Six timely offers were received. During negotiations, one offeror withdrew its offer. One offeror was determined unacceptable as the mode of delivery (barge through Khor Al Zubayr port then by truck to the requiring locations) did not meet the requirements of the solicitation. Three offers were determined unacceptable as a result of either a negative Preaward Survey and/or failure to provide by the deadline a proper and acceptable letter of authorization from the Jordanian government, Ministry of Energy, to transport jet fuel in transit through Jordan to Iraq. The solicitation required the authorization prior to contract award and provided the deadline for submitting the letter of June 7, 2004.

IOTC, in conjunction with one of its partners, the National Resources Development Center, obtained the required authorization to transport jet fuel in transit through Jordan for use by the U.S. Military in Iraq. 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 letters 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's initial offered price was $2.80 per gallon. During negotiations, DESC urged IOTC to reduce its price and advised IOTC that this was a competitive procurement. Additionally, DESC informed IOTC that DESC has purchased JP8 delivered in this region in the past and the historic prices were substantially lower than IOTC's offered price. After discussions, IOTC consulted with its partners and submitted a revised unit price of $2.40 per gallon.

In further discussions on price, DESC clarified that the solicitation does not require epoxy-coated trucks, which IOTC was in the process of purchasing with the understanding that it was a requirement. DESC also recommended that IOTC consider lowering its price further because the revised offer price was still considered substantially high compared to DESC's historical and current purchase data. IOTC submitted a second offer price revision of $2.35.

DESC again contacted IOTC to discuss the revised price. DESC provided IOTC with price objectives in an estimated price range of $1.4890088 - $1.5090088, which included product price, as well as transportation based on current contracts in the region, storage, and testing costs. These price objectives are comprised of current contracts and historical data for movements similar to or the same as delivery through Jordan. IOTC provided several reasons for their offer price being well above DESC's price objectives. One reason was the high product price they must pay to their supplier, Jordan Petroleum Company. Jordan Petroleum is the only supplier with fuel in a location that will be able to meet the urgent need of the military to start a supply line through Jordan. Any other supplier would present an unacceptable delay to the start of performance. Another reason is that the insurance costs for delivery to the U.S. military in Iraq are much higher than the insurance for delivery to the civilian population under humanitarian efforts because the risk of attack is higher. Finally, IOTC has entered into a partnership with the National Resources Development Company (NRDC) for logistics support and delivery of the fuel. ~~NRDC is a company partially owned by the Jordanian government and, as such, has been able to~~ obtain the proper authorizations to transport fuel through Jordan. IOTC advised that this partnership was

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an element that has resulted in a higher price, but will provide greater assurance of successful performance of the contract. Subsequent to this discussion and after consulting with its partners NRDC and Trafigura Ltd, IOTC was able to revise its offer price for a third time to $2.10 per gallon.

In order to further analyze the price, DESC requested that IOTC submit a breakdown of the costs that make up the $2.10 unit price. IOTC submitted the costs, which included the product cost, transportation with amortization of new trucks to be obtained, cost of partnership agreements, insurance, financing costs, local operational costs, quality control costs, miscellaneous expenses and a profit margin. Following receipt of this data, DESC and IOTC held a teleconference call, which is detailed below.

Date of Conversation: June 15, 2004

Subject: IOTC's offer price under solicitation SP0600-04-R-0054-0002

Parties involved: DESC – Don Peschka, Joy Mullori, Sonja Varricchione
IOTC – Harry Sargeant, William Mauco

Purpose: Discuss the elements of the JP8 offered price submitted on June 14, 2004

- Supply Cost - $1.33/USG – Mr. Sargeant advised that the $1.33/USG represents the fixed price of JP8 purchased from Jordan Petroleum. In order to provide immediate supply, IOTC will purchase JP8 already on hand from Jordan Petroleum to meet the requirement. This supply is expected to last approximately 15-20 days. Over the course of the contract period IOTC agreed to continue to purchase JP8 from Jordan Petroleum if excess JP8 was produced and available for sale. Mr. Sargeant advised that Jordan Petroleum can only produce 7,000-8,000 MT of JP8 per month. This quantity is not sufficient to cover the requirement and would be supplemented with imported product. However, if the product is available, regardless of current market conditions, the price from Jordan Petroleum to IOTC is $1.33/USG. The supply cost element of $1.33/USG is lower than the $1.51/USG originally offered to DESC by Jordan Petroleum during the negotiations for an International Agreement to support the Al Assad and Al Taquddem requirements.

  As the supply cost is a fixed cost there is a hedging risk to IOTC whenever product must be imported. Importation of product includes the additional cost elements of storage, demurrage, port fees, customs bonds, additive injection costs/risk of injection at a new facility and additional transportation from Aqaba vice Zarqa.

  A break down of these elements was provided as follows:

  - Demurrage – Due to berth congestion at the port of Aqaba vessels incur significant demurrage awaiting a berth. As Jordan Petroleum vessels have priority even if the vessel is berthed, a vessel can be forced to move from the pier to make way for a Jordan Petroleum vessel before discharge is completed. The cost of demurrage is approximately $20,000/day. Trigeant Ltd, the current DESC contractor delivering product from Jordan to the civilian population of Iraq, is experiencing demurrage on vessels for 30-45 days.
  - Storage cost – Storage costs at the Solvochem facility is approximately $0.04/USG

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- Additional transportation – The additional cost of transportation from Aqaba to the requiring locations vice Zarqa to the requiring locations is approximately $1 per barrel.
- Additives and Equipment – The additional cost of additives, additive injectors, and wasted product due to learning the additive injection process is approximately $0.03-0.04/USG. Product sourced from Zarqa is already additized.
- Port Fees and Customs Bonds – Port Fees and Customs bonds total $4-5/MT. The cost of customs bonds is high due to the volume being imported. Most firms involved in issuing the customs bonds cannot cover the volume, thus the additional costs.

- <u>Transportation Costs</u> - $0.45/USG – IOTC purchased 21 epoxy coated trailers from the Jordanian military at a cost of approximately $1.1 million. The cost of these trailers must be amortized over the delivery period, which is only 6 months. Also, IOTC must lease the remaining trucks needed to meet the requirement in order to have a dedicated JP8 truck fleet. Mr. Sargeant also advised that the cost of drivers is higher than for the humanitarian assistance contract as delivering to a military base represents a greater personal safety risk to the drivers. The drivers demand higher salaries for deliveries to the military bases as they feel these locations are military targets unlike the requiring locations for humanitarian assistance fuel.

- <u>Jordanian Partners</u> - $0.091/USG – Mr. Sargeant advised that this cost element represents the fee for NRDC's services under any resultant contract. National Resources Development Company (NRDC) is a division of King Abdullah's Design Center. This company is the commercial arm of the Jordanian Army which is engaged in commercial activities in order to generate funds for the Jordanian Army. (The military is not centrally funded by the Jordanian Government). NRDC holds the exclusive rights to transit petroleum products through Jordan. NRDC will provide facilitation of customs clearance, coordination with Jordan Petroleum at Zarqa, interface with the Ministry of Energy and Natural Resources, coordinate convoy security, provide interpreters and facilitators at the loading facility in Aqaba, and Air Force quality personnel to assist with the additive injection process at Aqaba.

- <u>Trafigura participation</u> - $0.04/USG – Trafigura handles market hedging, arranges vessel logistics for imported cargoes, financing of imported cargoes, and locates cargoes. Additionally Trafigura will find an economical means of trading product that is purchase by IOTC but not consumed by DESC

- <u>Insurance</u> - $0.018/USG – Mr. Sargeant advised that the insurance cost includes the risks to IOTC under the Risk of Loss clause in the solicitation. The risk of loss clause places all risk of loss for product due to theft, loss of life or loss of property to the contractor. This cost elements represents the insurance costs for these risks.

- <u>Financing</u> - $0.018/USG – This represents the financing cost of the operation through their assignment agreement.

- <u>Remaining Cost Elements</u> – The remaining cost elements, Local Operations ($0.012/USG), Quality Control ($0.012/USG), Miscellaneous ($0.009/USG) were not discussed in depth as they did not represent significant cost elements

- <u>Margin</u> - $0.12/USG – Represents profit/buffer against any unforeseen costs and market risks

Mr. Peschka advised Mr. Sargeant of the process for approval of the price negotiations as DESC cannot determine the offered price to be fair and reasonable in accordance with the FAR guidance. Mr. Peschka also

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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 is aware that the pricing issue will be elevated to the Center Senior Procurement Official and the Head of Contracting Agency for a final decision of acceptability. 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.

Additionally, DESC prepared a price analysis in accordance with FAR 15.404-1 to build a comparable price for DESC importing JP8 from DESC stocks into Jordan in transit to Iraq. Product prices are based on current competitively-awarded contracts calculated to a reference price of January 1, 2004. Storage costs and testing costs are based on DESC storage costs for similar storage in Jordan during OIF. Transportation costs are based on the cost of leased trucks in Kuwait to transport fuel to U.S. military bases in Iraq. For product sourced in Bahrain the average of the two line items was used. These prices are revised from the original price objectives passed to IOTC as the original pricing did not include demurrage. Below is the constructed price based on imports from either Europe of the Arabian Gulf.

Shell Aviation LTD SP0600-03-D-0510

Effective 1/1/04 — TK/O/Milford Haven, UK

Award Price	0.762499		
Base Ref.	0.759393		
Differential	0.003106		
Latest Unit Price	0.958985		
New Price	0.962091		
Transportation Cost to Aqaba	0.083048		
	1.045139	Product price	1.045139
		Transportation to Iraq	0.55
		Storage at Aqaba	0.0435898
		Testing	0.00028
		demurrage	0.10
		Total	1.7390088

BAPCO SP0600-04-D-0456

Effective 1/1/04 — TK/O/Sitra Port, Bahrain

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Award Price	0.670000
Base Ref.	0.676607
Differential	-0.006607
Latest Unit Price	0.900833

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New Price		0.894226
Transportation Cost to Aqaba		0.055143
		0.949369
0301		
Award Price		0.679524
Base Ref.		0.676607
Differential		0.002917
Latest Unit Price		0.900833
New Price		0.90375
Transportation Cost to Aqaba		0.055143
		0.958893
	Average	0.954131
	Transportation to Aqaba	0.55
	Storage at Aqaba	0.0435898
	Testing	0.00028
	demurrage	0.10
	Total	1.6480008

The range of pricing depending on the source location is $1.648 - $1.739. IOTC has noted several other cost factors (Jordanian partners, insurance, financing) which are not included in the above price analysis as these costs would not be experienced by the government and comparable pricing data does not exist. A comparison of the IOTC price elements and DESC constructed price did not result in any single factor contributing to the cost differential. While some of IOTC's cost factors are higher than DESC's constructed costs, other cost factors, such as transportation, are lower.

Based on the information provided by IOTC and the price analysis prepared by the contracting office, the Contracting Officer cannot determine the offered price to be reasonable. The differential between IOTC's final proposal revision and the DESC constructed price is $0.3609912.

CENTCOM after being informed of the price has maintained an urgent need for JP8 sourced through Jordan. The Contracting Officer is referring this contract action to the Bulk Fuels, Chief of Contracting for review and further action by the Center Senior Procurement Official (CSPO) followed by a final recommendation for award by the Director, Defense Energy Support Center.

Sonja Varricchione

SONJA VARRICCHIONE
Contract Specialist
Date: June 17, 2004

Joy E. Mullori

JOY E. MULLORI
Contracting Officer, Overseas Bulk Fuels
Date: June 17, 2004

As the Chief of Contracting for Bulk Fuels, I certify that I participated in price negotiations with IOTC and concur with the recommendation that this contracting action be forwarded to the CSPO for further attempts to reduce the price through negotiations.

Donald Peschka

DONALD E. PESCHKA
Chief, Bulk Fuels Contracting
Date: 17 June 2004

Concur ✓ **Non-Concur**________ **Concur**________ **Non-Concur**________

Mark K. Iden

MARK K. IDEN
Director
Bulk Fuels
Date:

DESC-G
Date:

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As CSPO, I conducted price negotiations with IOTC on June 21, 2004 via telephone. After a lengthy discussion with IOTC; they further explained their pricing structure (see attached MFR). Based on this discussion, IOTC was unable to reduce their price; however, I am forwarding this packet to the Director, Defense Energy Support Center for a recommendation for award.

GABRIELLA M. EARHARDT
Center Senior Procurement Official
Date:

I approve _____ disapprove ______ award.

6/27/04
RICHARD J. CONNELLY
Director