SUMMARY OF MAJOR CHANGES

All changes are denoted by blue font.

Substantive revisions are denoted by an asterisk (*) symbol preceding the section, paragraph, table, or figure that includes the revision.

Unless otherwise noted, chapters referenced are contained in this volume.

Hyperlinks are denoted by **bold, italic, blue, and underlined font**.

The previous version dated December 2010 is archived.

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<td>150102</td>
<td>Added an “Authoritative Guidance” paragraph to comply with the Department of Defense Financial Management Regulation Revision Standard Operating Procedures.</td>
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<td>150205</td>
<td>Reduced the amount of allowable exceptions Components can utilize to change the standard price throughout the fiscal year without approval from the Office of the Under Secretary of Defense (Comptroller), Program/Budget office.</td>
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<td>150206</td>
<td>Provided clarification on the organization that may authorize discount pricing.</td>
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CHAPTER 15

SUPPLY MANAGEMENT ACTIVITIES

1501  GENERAL

150101.  Purpose

This chapter provides the policy to guide budget formulation and execution for supply management activities of the Defense Working Capital Fund (DWCF). All policy and supporting guidance promulgated within is applicable to all Department of Defense (DoD) working capital funds (WCF).

*150102.  Authoritative Guidance

The financial management policy and related requirements prescribed in this chapter are in accordance with the applicable provisions of:


B.  10 U.S.C. § 2210, “Proceeds of sales of supplies: credit to appropriations;”

C.  10 U.S.C. § 2306, “Kinds of contracts;”


I.  31 U.S.C. § 3905, “Payment provisions relating to construction contracts;”

J.  The Office of Management and Budget (OMB) Circular A-11, Part 4, “Instructions on Budget Execution;”


L.  Defense Federal Acquisition Regulation Supplement (DFARS) 217.74.
1502 PRICING OF INVENTORY ITEMS

150201. Budgeting

Policies used in the budget development of prices for supply management activity items are contained in Volume 2B, Chapter 9, “DWCF Budget Justification Analysis.”

150202. Standard Price

A. Standard price is the price that DoD customers are charged for DoD Inventory Control Point (ICP)-managed items (excluding subsistence), or Integrated Material Management (IMM) items. The authoritative source of standard prices for the DoD is the Federal Logistics Information System (FLIS), accessible through WebFLIS. Prices are computed based on various factors, including replenishment cost of the item, plus surcharges to recover costs for transportation, inventory loss, obsolescence and maintenance, depreciation, and supply operations. Each cataloged inventory item with an assigned national stock number and, under DoD ICP management, must have a selling price for sales to all authorized customers. See DoDM 4140.68 for more details about standard pricing for non-consumable items.

B. Non-DoD customers providing direct support to DoD related mission requirements must also be charged the standard price. The selling price to all other non-DoD customers will be as prescribed in Volume 2B, Chapter 9. Exceptions to this policy are authorized in paragraph 150205.

C. DWCF activities must institute selling prices at the lowest practical item level in order to promote cost visibility/management and to motivate cost effective customer/supplier behavior.

D. The standard price of each item must be determined annually in advance of the execution year to allow for publication in the FLIS, accessible through WebFLIS, before the price is effective. The standard sales price becomes effective for billing purposes on the first day of the fiscal year. A standard price cannot change during the fiscal year without prior approval.
from the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)), Program/Budget (P/B), Revolving Funds Directorate except as stated in paragraph 150205. The dollar amount of unfilled customer orders accepted at the previous fiscal year’s standard price must be adjusted (upon notification to and confirmation from the customer) to reflect the latest standard price when notice of the price change is received.

E. All local procurements must be cataloged and assigned a standard price including any retail\(^1\) level cost recovery element. For more information about Demand and Supply Planning, see DoDM 4140.01, Volume 2.

F. The DWCF establishes selling prices in the budget that are normally stabilized or fixed during execution to mitigate the impact of unforeseen fluctuations that would affect customers’ ability to execute programs approved by the Congress. For more information about full recovery of costs and the setting of prices, see Volume 2B, Chapter 9.

G. The standard price must also contain the total materiel costs, see Volume 2B, Chapter 9. Total materiel costs for Supply Management Activities include:

1. Materiel costs (without inflation) to be included in this cost recovery element are the net of losses and gains from incoming and outgoing shipments, physical inventory adjustments, inventory losses as a result of shrinkage, theft, deterioration, damage contamination, defective items if not reimbursed by supplier, obsolescence, and adjustments to reconcile internal records.

2. Materiel Inflation (normal inflation) is the dollar amount of the standard rate of inflation as published by the OMB. The Product Cost Growth Factor is a cost element to account for any anticipated price growth beyond standard inflation.

3. Loss/damage/washout/obsolescence is a cost element that is associated with any costs that are expected to be incurred for these types of situations where a replacement unit is required. Activities that manage maintenance and repair missions on an exchange carcass basis incur replacement cost for carcass losses and washouts. Lost carcasses (for example, in transit to the customer or to the supply system) must be investigated and necessary internal controls strengthened as required by Volume 12, Chapter 7. Carcass washouts, also called “condemnations” are carcasses that, during the initial inspection, are determined to be repairable but during the repair process are determined to be unrepairable and are also determined to require replacement. If the carcass is determined to be unrepairable because of cannibalization or other malicious damage caused by the customer, the customer must be charged the difference between the exchange price and the current standard price and this cost must not be included in the surcharge element. Maintenance activities must maintain all documentation in accordance with Volume 1, Chapter 9.

\(^{1}\) Retail: According to the DoDM 4140.01-V2, retail level: is the level of inventory below the wholesale level, either at the consumer level for the purpose of directly providing material to ultimate users or at the intermediate or region level to supply consumer levels at a region or geographical area.
H. In a system that supports exchange pricing, the price charged to customers returning a Depot Level Reparable part that needs repair, and purchasing a serviceable one (new or repaired), equates to the latest repair price plus wash out costs (condemnations) per item plus pricing elements necessary to recover other operating costs. (Note: If no carcass (unserviceable item) is returned, the customer must be charged the full standard price.) For additional information related to supply turn-ins, see Volume 4, Chapter 4.

I. Supply management operations also incur non-materiel costs (overhead cost and pricing adjustments). The non-materiel costs also include adjustments for prior year operating results, approved surcharges, and other factors. The Cost Recovery Rate utilizes a calculation that reflects the markup on total materiel costs required to recover operating costs, calculated by dividing total non-materiel costs by total materiel costs. This represents the percentage markup on materiel costs required to operate the supply activity. These cost elements are displayed on the SM-5a “Markup on Materiel Cost” exhibit (see Volume 2B, Chapter 9).

1. The provisioning cost element is provided when a weapon system was originally fielded under a contractor logistics support agreement. The component may decide to fund the provisioning action in the standard price of the item if the contractor fails to perform or a decision is made at the component level to transfer program management to a DWCF supply activity. The component may also decide to fund this action using contract authority without an immediate reimbursement if a funding source can be identified and used for reimbursement by the time of first delivery and the OUSD(C), P/B, Revolving Funds Directorate has preapproved the action. Preapproved reimbursable transactions of this type must be recorded as “other income” and will not be included in the standard price.

2. Inventory augmentation costs finance the acquisition of inventories that are required over and above demand replacement (excluding mobilization requirements, which are financed by appropriations) to maintain the approved level of materiel support. Inventory Augmentation is normally funded by direct appropriation (see Volume 2B, Chapter 9), but may be included as a cost recovery element if approved by the OUSD(C), P/B, Revolving Funds Directorate. Cash solvency must be considered in determining the recovery method for Inventory Augmentation.

3. Losses that are unusual or nonrecurring in nature, such as those due to armed hostilities, riot, or significant damage due to fire, flood, earthquake, storms, or other abnormal events are not normal inventory losses and should not be included in the cost recovery element for inventory expenses. DWCF Activities should seek approval from the OUSD(C), P/B, Revolving Funds Directorate to fund losses that are unusual or nonrecurring in nature.

J. The standard sales price of an item must include recovery of operating costs including payroll, personnel travel, transportation, defense agency billings, other DWCF purchases, operating materials and supplies, rent/communications/utilities, depreciation, transportation and other service contracts.
K. Infrastructure costs must be identified separately and may include capital programs (depreciation, capital surcharges) and systems sustainment recovery elements. For more information, see Volume 2B, Chapter 9.

L. Other cost recovery elements, as approved by the OUSD(C), P/B, Revolving Funds Directorate during the budget review, may be added to the price. These elements typically include Accumulated Operating Results adjustments, cash surcharges, and fund management adjustments.

M. The purpose of the cost recovery elements is to balance total revenues with total net operating costs. Total net operating costs must not include requirements funded by appropriations, such as amounts appropriated for war reserve materiel or emergency or national defense stockpiles (see Volume 4, Chapter 4). The costs to be accounted for within the recovery elements must encompass:

1. The costs of operating wholesale ICPs and wholesale supply depots must be financed by the supply management activity. Such costs include civilian labor and benefits, military labor, supplies, purchased services, and reimbursements to other Defense agencies that provide support to supply management operations. The cost of performing equivalent functions at the retail level (installation/area supply support) may be included in the cost assessed by the wholesale activities if the retail activity is managing the distribution of Defense Logistics Agency, General Services Administration or any other government agency where an additional rate would not be applicable.

2. The costs incurred by separate activities and functions that exist primarily to benefit the mission of a wholesale ICP and/or a wholesale supply depot. Mission support cost pools must be established that identify costs incurred in activities and functions that directly provide benefits to wholesale ICPs and wholesale supply depots. These cost pools will include all costs (civilian labor and benefits, supplies, purchased services, and other costs) incurred in functions such as line management (command and control), staff management (policy functions), and centralized service functions (e.g., procurement, accounting, personnel, automated data processing). The portion of such overhead cost pools that directly benefit the supply management activity mission must be allocated to, and reimbursed by, the supply management activity. The allocation must be prorated on the relationship of the cost of the benefits provided to the supply management activity, to the cost for all activities or functions.

3. Shipping and transportation, including costs for packing, crating, handling, transportation, and, where appropriate, port loading, and unloading. Items may be shipped from a stocking point (issues) or to a stocking point (returns).

(a) Transportation costs include transportation for items issued by the supply management activity. To the extent that first destination transportation is not included in the acquisition cost, an estimate of the cost must be included in this element. Second destination transportation (SDT) costs should be based on the assumption of average cost as adjusted by projected changes in the budget year. The SDT costs financed by a supply management activity generally include transportation within the Continental United States.
(CONUS) and between overseas locations. An additional transportation charge must be assessed for expedited delivery.

(b) The costs of providing and managing commissary items, including related operating costs incurred to support the mission of commissaries, must be identified as commissary operating costs. These costs include, but are not limited to, costs incurred to support commissaries at a headquarters or regional level. Commissary operating costs must be charged to, and reimbursed by, appropriations made available to the DWCF for commissaries and the commissary trust revolving fund see DoDI 1330.17.

(c) Costs include shipping and transportation costs only for items approved by an item manager for return from DoD customers to the supply management activity. The supply management activity must reimburse transportation and other shipping costs only for items approved by an item manager for return from customers. The supply management activity must not pay the shipping and transportation cost for items that have not been approved by an item manager for return from customers.

(d) Costs to be included are shipping and transportation costs for the return of reparable exchange carcasses from customers. Customers will not be charged separately for carcass returns because supply activities factor shipping and transportation costs for customer returns of carcasses into cost recovery projections.

(e) Costs to be included are shipping and transportation costs for Lateral Redistribution Orders (LRO) of stock when directed by an item manager. The ICP or IMM must reimburse the supplying/holding activity for the costs of packing, crating, handling, and transportation to move materiel when a shipment is made at the direction of an ICP/IMM.

4. If a supply management activity experiences a sudden decrease in volume of customer orders, it may require additional revenue in order to liquidate contract authority associated with inventory ordered from vendors. Resources may be obtained through either transfer or direct appropriation to the revolving fund, or by supply management activity establishment of a cost recovery element (or combination of both). When undelivered order stock levels have stabilized to a level appropriate for the new volume of demand, any cash surcharge will be eliminated.

N. A cost recovery element used by a retail level supply activity:

1. Will include inventory (materiel) expenses. Inventory expenses applicable to the retail-managed items are the net impact of gains and losses at the retail level, obsolescence, and shelf-life deterioration.

2. May include other cost recovery elements, when approved by the OUSD(C), P/B, Revolving Funds Directorate.
150203. Foreign Military and Private Party Sales

As prescribed in Volume 15, “Security Cooperation Policy”, the selling price of DWCF items to Foreign Military Sales customers must be the current DWCF price for that item. Private Parties (State and Local Governments, and Non-Governmental entities not under a Department of Defense contract) that are authorized to obtain DWCF Supply Management support will be charged the Cost of the Item plus the applicable Cost Recovery Rate.

150204. Lateral Redistribution of Stock

When another activity has stock on-hand to fill an order, a Supply Management Activity may direct an LRO to that activity to issue stock directly to the customer. As provided in DoDM 4140.01, Volume 5, “DoD Supply Chain Materiel Management Procedures: Delivery of Materiel,” billing procedures associated with LROs directed by an item manager will ensure a supply holding activity is reimbursed for both the standard price of the materiel and the standard packing, crating, handling, and transportation costs associated with a LRO. The item manager will bill the customer for the standard price of the materiel and reimburse the supply holding activity via the ICP/IMM for the standard price of the materiel and the standard packing, crating, handling, and transportation costs. DoD Components facilitating LROs must record outlays of Fund Balance with Treasury as a disbursement. Recording a negative collection is prohibited. Since these are intra-agency transactions, it is critical that trading partners working together utilize the correct codes at the detailed transaction level. For more information, see the Deputy Chief Financial Officer policy memorandum, “Accounting Treatment of Lateral Redistribution Activities (FPM 20-05).”

150205. Authorized Changes of Standard Prices

DWCF Activities must set product prices on an annual basis per the requirements established in paragraph 150202. Prices cannot be changed during a fiscal year without justification to, and prior written approval of the OUSD(C), P/B, Revolving Funds Directorate. All approved price changes will be grouped by the item manager and released for updates to the supply management activity’s pricing catalog not to exceed once a month. The only exceptions to the price changes requirement for prior approval are:

A. Unit of issue changes;
B. First time buys;
C. Contract Modifications; and
D. Discounted product prices (see paragraph 150206).
*150206. Discount Pricing

A. Product prices must reflect the full cost of the product and the related management activity unless the following conditions are met, and submitted to OUSD(C), P/B, Revolving Funds Directorate for approval:

1. Requests to discount item prices must be accompanied by documented approval of the request from within the DoD Component and an analysis of the anticipated cost (profit/loss) impact as a result of changing prices.

2. Reductions from standard prices may be made upon determination that there is an actual difference in utility or desirability of an item because of age, condition, or model for items being phased out of the system, items no longer being procured, items with limited remaining shelf life, items in a less than “fully serviceable” condition, and items in long supply, i.e., assets stratified as “potential reutilization stock.”

3. See Volume 4, Chapter 4, for policies to be used in the development of exchange transaction prices for supply management activity items.

150207. Pricing for Additional/Premium Service

A. Components may establish and offer variable levels of service related to a product, at variable prices, to allow customers the opportunity to economize according to their needs. Appropriate fees may be established annually and may vary according to the item/class of items. Refunds (credits) will be made available for those instances where a customer has paid for a level of service that was not provided. This policy authorizes an additional charge for customers who ask, and are willing to pay, for enhanced service; **it does not authorize reduced charges.** Individual orders may be assessed an additional cost based on the following elements:

1. Expedited delivery.

2. Delivery outside the CONUS based on destination.

3. Depot handling fees related to order issues only. The fee(s) will include a minimum charge for low priced orders, a standard charge for bin item issues, a standard charge for normal bulk item issues, and special charges for unusual bulk item issues, e.g., special handling and extraordinary quantities.

4. Other additional/premium charges as approved by the OUSD(C), P/B, Revolving Funds Directorate.
1503 CONTRACT AUTHORITY FOR SUPPLY MANAGEMENT OPERATIONS

150301. Background

   A. Based on the authority in 10 U.S.C. § 2210, obligations may be incurred against anticipated reimbursements, without regard to fiscal year limitations. As defined in OMB Circular A-11, Contract Authority is a type of budget authority that permits you to incur obligations in advance of an appropriation, offsetting collections, or receipts to make outlays to liquidate the obligations.

   B. Contract Authority is apportioned budget authority, which can be legally obligated. Contract Authority, however, is not funded and is apportioned and allocated without a supporting Treasury cash balance. Consequently, contract authority must always be replaced or liquidated by subsequent or other budgetary resources. Contract Authority is apportioned to the DWCF Capital Programs and the Supply Management Operating Programs for the current fiscal year of the Apportionment only, and closes for new obligations if not used within the fiscal year it is apportioned.

150302. Budgetary Resources

   A. Budgetary resources for supply management activities available for use during the current fiscal year consist of any congressionally appropriated and re-appropriated amounts made available; the net of any non-expenditure transfers and internal distributions of budgetary authority into and out of the supply management activity and other Federal Government accounts (cash transfers); balances made available from the previous fiscal year contract authority; and apportioned anticipated contract authority. Normally, supply management activities may obligate based on two primary sources: contract authority and appropriated funds for war reserve/mobilization purposes.

   B. Liabilities (accounts payable) are typically payable from the Fund Balance with Treasury within the terms of the Prompt Payment Act, 31 U.S.C. §§ 3901-3905. Unfunded (unliquidated) contract authority should be considered a long-term liability for supply management activities because budgetary resources required for payment of these contracts have not yet materialized through customer orders or appropriations from Congress.

   C. Unobligated balances of contract authority and appropriations are not available for use in the subsequent year until they are reapportioned and reflected on the supporting financing schedule as an increase to the limit imposed for obligation authority on an approved apportionment in the new fiscal year.

   D. The OMB may approve and apportion anticipated contract authority in the amount of the approved supply management activity-operating program.

   E. The OMB apportions contract authority on the SF-132, “Apportionment and Reapportionment Schedule.” The OUSD(C), PB office allots contract authority on the Annual Operating Budgets.
F. Apportioned contract authority is either obligated or returned. Obligated contract authority is substituted with the receipt of customer orders, and then liquidated with the collection of revenue associated with the fulfillment of those orders. Typically, spending authority from offsetting collections coming from revenue collected from filled customer orders is used to liquidate contract authority. Sometimes, appropriations can be used to liquidate contract authority rather than spending authority from offsetting collections.

G. Customer orders received are requisitions and other orders accepted for items to be furnished on a reimbursable basis. Budgetary resources provided from a customer order are available to fund obligations provided that, in the case of orders from the public, an advance has been collected.

150303. Contract Authority and Cash Management

A. Although the responsibility for cash management is at the component level, the liquidation of contract authority is only authorized by collections from customer orders or by an appropriation to liquidate contract authority. Cash collections from supply management activities are the primary funding source approved for the liquidation of contract authority unless otherwise approved in writing by the OUSD(C), P/B, Revolving Funds Directorate.

B. Supply management activities may also submit requests as part of the component’s budget request, for appropriations for the sole use of liquidating contract authority if a change in customer demands warrants this action. Similarly, any proposed negative surcharges identified in the budget justification materiel, other than Accumulated Operating Results recovery, must be pre-approved in writing by the OUSD(C), P/B, Revolving Funds Directorate.

1504 MULTIPLE-YEAR CONTRACTS

150401. Overview

A. Multiple-year contracts permit the purchase on one contract of more than one annual program increment of items to obtain a maximum economic advantage. For example, an Economic Order Quantity (EOQ) in a multiple-year contract may exceed a normal annual requirement and yet be advantageous to the Government. Supply management activities are authorized to use multiple-year contracts to procure items from a single contractor.

B. Sole source items with a stable demand projection that are procured from a single contractor must be evaluated to determine if the items should be acquired by means of a multiple-year contract. As with multiple-year contracts funded by procurement appropriations, the supply management activity may purchase items in an amount corresponding to the economic order quantities deemed appropriate for procurement in each year.

C. Components, parts, and raw material for use in manufacture of items being acquired under a multiple-year contract may be procured in quantities exceeding the current annual requirement when it is more economical and cost effective to do so. This is referred to as advance EOQ procurement. Advance EOQ procurements integral to multiple-year contracts must be
funded in the most economical manner. They may be funded fully in single year increments on a termination liability basis, or included in a multiple-year contract along with the nonrecurring contract costs.

D. Under 10 U.S.C. § 2306, the DoD is authorized to enter into multiple-year contracts containing cancellation clauses that may include both nonrecurring and recurring costs. This law specifies congressional reporting requirements based on cancellation ceilings. Further, annual DoD appropriations acts may contain specific language requiring limitations on the use of multiple-year contracts. A single proposed multiple-year contract in excess of $100 million or $10 million in estimated termination liability must be submitted to the OUSD(C), P/B, Revolving Funds Directorate for approval prior to awarding the contract. Each separate option to extend a multiple-year contract must be considered as a single multiple-year contract for the purposes of this approval requirement.

150402. Obligations

A. The supply management activity must obligate the minimum amount required for the period of the contract.

1. If the contract provides for annual terms with options to extend the terms in subsequent years, the obligation must be for the amount required to be procured by the Government in the first year. The obligation for each option year must be recorded when the option is exercised.

2. If the contract provides for minimum quantities over a period of more than one year, the obligation must be recorded for the sum of all of the minimum quantities times the agreed price. If the contract provides for minimum dollar amounts for a period of more than one year, the obligation must be recorded for the sum of the minimum dollar amounts.

3. The bona fide needs rule, derived from 31 U.S.C. § 1502(a), applies to appropriations limited to a definite period of time. Although the bona fide needs principle does not statutorily restrict a supply management activity from incurring obligations against contract authority for requirements of the subsequent fiscal year, contract authority conferred to the activity for a year may impose limitations on execution of obligations. Also, because supply management activities use contract authority to incur obligations to acquire stock or order items for delivery to customers, and do not execute budgetary resources dependent on receipt of funded customer orders, the timing of a supply management activity’s obligations against contract authority do not govern, establish, or reflect whether the customer’s order to the supply management activity is a bona fide need of the customer appropriation charged.

150403. Cost of Items

The cost of items procured by multiple-year contracts must be the amount paid for each item. If termination costs are incurred or if minimum guaranteed amounts are not met for items procured, the additional costs paid under the terms of the contract must be recorded as supply management activity materiel obligations.
1505 BUDGETARY ACCOUNTS

150501. Overview

Budgetary accounts are used to control and account for obligation authority received from appropriations and contract authority apportioned by OMB. Supply management activities are subject to apportionment, as required by the Antideficiency Act, in accordance with the procedures prescribed in OMB Circular A-11, “Instructions on Budget Execution” and Volume 3, Chapter 19.

150502. Allotments

The general provisions of the annual Appropriations Act provide that, “Except in amounts equal to the amounts appropriated to DWCF in this Act, no obligations may be made against a DWCF to procure war reserve materiel inventory unless the Secretary of Defense has notified the Congress prior to any such obligation.” Obligation authority for mobilization purposes must be allotted and allocated separately as a direct program. Operating obligations consist of all obligations that do not meet the criteria defined for mobilization; they must be allotted and allocated separately as a reimbursable program. Obligations must be accounted for and reported separately as mobilization and operating.

150503. Budget Execution

For supply management activities, balances for budgetary accounts are displayed on the SF-133 and the DFAS Accounting Report 1307 part VII (see Volume 3 Chapter 19).