Chapter Five

RECOMMENDATIONS

In this chapter, we recommend changes to the DLR price structure and the cost recovery method that will yield a more flexible price structure that can accommodate changes in support strategies. This price structure will reduce the misalignment of customer incentives and Air Force costs discussed in the preceding chapter, and improve the Air Force's ability to achieve proper allocation of support resources. In addition, implementation of our recommendations will increase the visibility of various support costs and facilitate their recovery.

Appendix A contains a supporting discussion of the recommendations from the economics and accounting literatures for optimal internal transfer prices.

PRICING STRATEGIES

Price systems can be designed to support various levels of decision making and to achieve different ends. One approach is to structure prices to enforce *centrally determined* strategic decisions. Here, prices skew customers' incentives toward taking predetermined "best" actions. Another approach is to promote *customer* decision-making—that is, structure prices to give customers incentives to make decisions that minimize the costs of meeting Air Force support goals. In either approach, customers will make decisions based on the costs they face for each support alternative; however, in the latter case, customers face the costs to the Air Force for each alternative.

In principle, either approach to decisionmaking and its attendant price structure could be designed to lead to the same support outcome. The conditions required are availability to both central authorities and customers of accurate information on costs and other considerations, stability of these factors over time, and alignment of customers' and central decisionmakers' goals. When these conditions are not satisfied, one approach will be preferred over the other.

When information is less readily available to the customer than to central decisionmakers (e.g., when a new reparable component is introduced to the Air Force), centralized decisionmaking is preferred. For this reason, the Air Force makes initial level-of-repair decisions centrally. Over time, customers may develop better information as they gain experience with a system because they have a greater ability to detect changes in local repair costs, conditions of use, and frequency of failure. Thus, there are payoffs from setting prices *as if* customers were making the decisions, providing them with incentives to identify level-of-repair decisions that should be revisited.[1] However, when customers' and central decisionmakers' goals are not aligned—maybe there are noncost considerations that customers should, but are unlikely to, account for—prices must be adjusted to reflect them. For example, if a DLR should be repaired centrally for mobility reasons, the price should be set so that transacting with the fund is the least expensive option for customers.

Under DoD financial management policy, all costs associated with stock-funded activities must be recovered from customers. However, the costs that have to be recovered are not always equal to the costs customer actions impose on the Air Force, and these latter costs are the costs germane to current decisions. For example, when an item is in excess supply, the price that gives customers the right incentive may be close to zero because broken items will not (and should not) be repaired or replaced. However, under current policy, the acquisition costs of the excess serviceable items must be recovered despite the fact that these costs are unaffected by current repair decisions.

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[1]If an item is only repaired locally and, hence, there is no DLR price, customers will not have sufficient information to reassess the level-of-repair decision for that item. If the depot also does not have the information to reassess, automatic periodic reviews may be needed.

There are two general approaches to recovering costs that are unaffected by current decisions. One approach is to increase DLR prices sufficiently to recover these costs; the other is to recover the fixed costs through separate charges. The Air Force recovers fixed costs by increasing DLR prices, allocating these costs to prices in proportion to the acquisition cost of DLRs. As discussed in Chapter Four, this approach has the disadvantage of creating a wedge between prices and the costs that customers impose on the supply system; accurate visibility of costs by NSN or other aggregation is not possible. It also has the disadvantage of making customers advocates of services that they may value at less than their cost.[2]

Alternatively, fixed costs can be apportioned to prices in inverse proportion to the sensitivity of demand to prices. This allocation scheme—termed "Ramsey pricing"—distorts decisions less than the Air Force's approach.[3] For example, items with potential alternative sources of repair would be priced at the market price (which will be close to marginal cost in competitive markets), but the prices of items that can only be repaired at the depot would be set much higher than marginal cost to recover fixed costs.[4] Even though some prices might be seen as excessively high, level-of-repair decisions are unaffected because wings have no alternative sources of repair. However, Ramsey pricing also has several disadvantages. As with current Air Force DLR pricing, Ramsey pricing bundles the costs of DLR repair services with other services. Also, accurate visibility of costs by NSN or other aggregation is not possible. Finally, it has extensive information requirements—which items are sensitive to prices and which are not—and might be difficult to administer.

The approach we recommend is to establish separate charges to customers for costs unaffected by current repair decisions. This approach would more closely match DLR prices with marginal repair

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[2]See Eccles (1985, 1991) and Eccles and White (1988) for a discussion of the use of full cost transfer prices by commercial firms.

[3]For a discussion of Ramsey pricing, see the appendix in Camm and Shulman (1993).

[4]The Air Force uses a similar strategy in the transportation business area (called the TRANSCOM Working Capital Fund); it sets airlift rates to be competitive with commercial carriers' rates. However, this pricing scheme differs from Ramsey pricing in two ways: costs exceeding airlift rates are recovered through direct appropriations rather than from customers and airlift rates may be less than marginal cost.

costs and would improve visibility of other costs. This method of cost recovery is not perfect; there can be ambiguity about whether selected costs are completely fixed or vary with the rate of repair, and the establishment of additional charges places burdens on the accounting systems. However, recovering these costs separately from DLR prices helps customers make decisions that are cost-effective for the Air Force and allows customers more flexibility in the long run in choosing the services they wish to pay for.

RECOMMENDED STRUCTURE OF DLR PRICES

Our pricing recommendations are based on two central ideas:

> *Decisionmakers can make the most cost-effective resource allocation choices when the prices they face reflect the costs those choices impose on the Air Force.*
>
> *The costs of all stock-funded activities should be recovered from customers.*

We apply these ideas to stock funding of DLRs in two ways. First, customers should be charged separately for services and fixed costs unrelated to the rate of repair. Second, DLR prices should reflect only the additional (marginal) cost incurred by the support system in response to a customer transaction.[5] The exchange price should include only those costs that vary with the rate of repair and, under certain conditions, should reflect the condition of the unserviceable carcass.

Our specific recommendations concerning the structure of DLR prices are presented in order of priority and are summarized in Table 5 at the end of the chapter. Technical analysis supporting our recommendations is found in Appendix B.

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[5]In the same spirit, see Hirshleifer (1956), Benke and Edwards (1980), Kaplan and Atkinson (1989), and Rogerson (1995).

DLR Prices Should Not Include a Surcharge

Recommendation 1: Costs unrelated to rate of repair should be recovered from customers, but not through DLR prices.

Many support costs are related to repair but are fixed during the year. Examples include costs that were underrecovered the previous year, capital equipment, system program office staffing at ALCs, and technological and industrial support of product directorates. There are also variable costs that are unrelated to the rate of repair such as equipment specialist services, engineering support, software maintenance and development for operational applications, and other services provided on demand.

Recovering these costs from customer commands through charges that are independent of DLR prices has three advantages over the existing approach. First, the wedge between marginal costs and DLR prices is virtually eliminated, thereby reducing customer incentives to take actions that increase costs to the Air Force. Second, the visibility of the costs of strategic support decisions and customer support services can be improved. In the case of customer services, this visibility allows customers to determine if the benefit of a given service warrants its cost and, when it does, establishes the customer as a proponent. Finally, the dependence of cost recovery on the accuracy of demand forecasts is significantly reduced, improving the match between costs and revenues.[6]

Recommendation 1a: Fixed or sunk costs should be allocated to customer commands through periodic charges according to the cost source to the extent feasible.

By definition, fixed costs are not affected by wing behavior. Thus, fixed costs that can be linked to individual customer commands should be allocated to those commands. Some of these costs result from previous long-run strategic decisions made by commands and thus influence future decisions. For example, NSN-specific costs—costs that would disappear if that item were no longer repaired at

[6]This is a common strategy in public utility pricing. For example, Southern California Edison has a two-part price structure that consists of a flat fee each billing period to cover the cost of basic services and a charge per kWh to cover variable costs.

depot level—should be charged to commands in proportion to use. Weapon system-specific costs should be identified as such and charged to the commands operating the weapon system in proportion to ownership, thereby facilitating the evaluation of the weapon system's annual costs. Losses/gains from the previous year should be allocated among the commands according to the source of the under- or overrecovery to the extent this can be determined. Those costs that cannot be linked to decisions made by individual commands will need to be allocated arbitrarily among all the customer commands.

The components of the command charges need to be clearly identified because many of these costs are not fixed over a horizon of several years—they are affected by level-of-repair decisions and decisions about the continuing presence of specific NSNs and weapon systems in the Air Force inventory.

Implementation. Because command budgets are set at the beginning of each fiscal year, the frequency of payments from the commands should not influence decisionmaking. That is, as long as the total amount to be paid during the year is fixed, it should not matter whether a command makes one lump-sum payment at the beginning of the year, four equal quarterly payments, or more frequent payments. The payment plan that is easiest to implement should be adopted.

> *Recommendation 1b: Prices should be established for customer services that are unrelated to the rate of repair.*

Currently, customers do not see the costs of individual nonrepair services they demand when these costs are recovered through the surcharge. (See examples of such costs in Recommendation 1 above.) Therefore, customers are not able to weigh the benefits of these services against their costs. Prices reflecting the costs of providing these services would generate improved information about which services should be expanded and which reduced or eliminated.

DLR Prices Should Reflect the Marginal Cost of Transactions

> *Recommendation 2: Exchange prices should include all costs that vary with the rate of repair and no other costs. Similarly, standard prices should include all costs that vary with the rate of acquisition and no other costs.*

If the corporate Air Force and internal customers share the same goals, customer incentives are more closely aligned with those of the Air Force when DLR prices reflect only the additional costs that will be incurred in a transaction. Customers will not necessarily choose the lowest cost repair when there are noncost considerations; however, they will see the true costs and benefits of repair at each level and will make trade-offs that are appropriate not only for themselves but for the Air Force as a whole.

Costs that vary with the rate of repair include direct material and labor, pipeline inventory, transportation, and condemnations (when necessary). There are also some indirect and overhead costs that can be nonarbitrarily allocated by NSN to the rate of repair. For example, if the number of payroll personnel varies with the number of repair personnel and the number of repair personnel varies with the rate of repair, then payroll costs should be treated on a per-repair-person basis just as direct labor costs are.

Costs that vary with the rate of acquisition of new DLRs include purchase price (FAC), procurement pipeline inventory, transportation, and all indirect and overhead costs that can be nonarbitrarily allocated by NSN. These costs will typically be incurred when customer purchases of serviceable DLRs result in the acquisition of new DLRs to replenish the inventory.

Pipeline inventory costs currently are not visible to customers, although they are clearly related to the rate of repair. Except for items in long supply, unserviceable DLRs create demands for additional inventories to fill the pipelines for those items. The longer the average time items remain unserviceable, the greater the pipeline demand.

The DLR exchange price should include a pipeline inventory charge to recover the cost of the inventory necessary to support the average number of days between the time an unserviceable item leaves the

wing until it is returned to supply as a serviceable item. Similarly, the standard price should include a pipeline inventory charge to recover the cost of the inventory necessary to support the average number of days between the time that an item that will be condemned leaves the wing until a new unit is procured and entered into the supply system.[7]

The surcharge recovers the cost of transporting DLRs between the depot and bases. Rather than arbitrarily allocating these transportation charges through a surcharge, the costs should be borne by the individual customers imposing the costs on the support system. Thus, transportation costs should be included in DLR prices on an NSN-by-NSN basis.

Implementation. When pipeline inventory costs are small relative to marginal repair costs, the cost of including pipeline inventory charges in DLR prices may exceed the benefits. (Typically, this will apply to long-lived and/or short-cycle-time items.) On the other hand, if it is possible to calculate pipeline inventory costs using automated financial systems, it may be less costly to include these costs in prices for all DLRs rather than selected ones.

Because transportation times and charges vary little within a regional theater relative to between theaters, it may be that only one pipeline inventory cost and transportation cost per theater should be calculated for each NSN.

> *Recommendation 2a: When customers cannot affect the condition of a returned carcass, the DLR exchange price should be set equal to the average cost of a transaction for the NSN and not reflect the condition of the carcass. This average cost of the transaction should include repair costs and replacement costs, weighted by their respective probabilities. Thus, the carcass price should equal the standard price minus the average cost of a transaction.*

Customers can affect the condition of a returned carcass in three primary ways: excess usage, local organic repair (which enables

[7]When only a fraction of the condemned items is replaced, the procurement pipeline inventory should be weighted by that fraction.

cannibalization and sorting), and local contract repair. When customers cannot influence the condition of a carcass arriving at the depot—for example, an avionics LRU that is sealed and not subject to wing-level screening or an LRU with no alternative source of repair—the exchange price for that NSN should be set equal to the average marginal repair cost plus associated costs that vary with the rate of repair. Charging different prices depending on the carcass condition will not influence carcass conditions in these cases and may be costly to implement.[8]

The replacement costs of condemned items can be recovered in three ways. In the short run, all three approaches would recover replacement costs. However, these approaches differ in their ease of implementation and the incentives they provide commands to desire ownership of DLRs.

- One approach is to charge each wing the replacement cost when a returned carcass must be condemned and replaced. This might lead wings or commands to insist on ownership of specific DLRs. For example, if an item can be repaired only a limited number of times before it must be condemned, then commands may want to protect themselves from paying for a condemnation when other commands were responsible for previous repairs of that particular item.
- Another approach is to recover replacement costs through periodic charges to customer commands based on flying hours (possibly adjusted for each command's past replacements per flying hour). This would avoid the problems raised above while ensuring that condemnation costs are recovered from customers.
- A third approach is to average the NSN-specific replacement cost into the exchange price paid by the wing. This approach also avoids problems raised in the first approach but is easier to implement within the current financial system than the second approach. However, there is the possibility that averaging the cost

[8]Carcass condition may be affected by mission rather than behavior, and for these NSNs there should be command-specific exchange prices. For example, equipment in one command may be subject to salt air and, thereby, may always require more extensive repairs than the same equipment operated by other commands.

of replacement items with repair costs may provide customers with incentives to seek to *create* alternative sources of repair that cost less than the exchange price but perhaps more than the actual cost of depot-level repair. If this behavior emerges in response to an average cost exchange price, the second approach should be used.

Recommendation 2b: When customers can affect the condition of a returned carcass (e.g., through excess usage, cannibalization, or sorting), the DLR exchange price should reflect the condition of the carcass. When a carcass is returned alone rather than through an exchange, the carcass price should reflect the condition of the returned carcass.

When a customer can influence which of several possible repairs are necessary, the exchange price the customer pays should reflect the cost of each of the necessary repair activities. These repair activities include separable repairs as well as repairs with varying degrees of difficulty. For example, the exchange price of an avionics LRU should include only the cost of screening if the technician cannot duplicate the failure. However, in the case of a failure, there should be an additional charge for each SRU repaired. Similarly, if a customer requests a serviceable unit but keeps the carcass longer than the period allowed for exchanges (the customer is charged the standard price for the serviceable unit requested), then the carcass price should reflect its condition if that customer returns the carcass at a later date.

Charging customers in this way should cause them to adversely affect carcass conditions only when that is the most cost-effective strategy for the Air Force.[9] In addition, charging according to the

[9]There is the possibility that the depot repair shop could overstate the required repairs in order to artificially inflate the demand for its services. (We have not been told of any such cases.) This might occur when the shop is not busy; there is no incentive to do so otherwise. However, this behavior is no more likely under the recommended pricing strategy than under the current one. Under the current system, if the average repair cost reported during the year is higher than the one used to set the current DLR exchange price for an item, the estimated depot repair cost will rise, and the shop will suffer no long-term consequences unless there are alternative sources of repair. Under the recommended strategy, the wing could receive a report on what repairs were deemed necessary that could serve as an external check.

condition of the returned carcass would eliminate the necessity of adjusting the exchange price to account for changes in the average condition (and cost) of repair, an adjustment that takes two years to achieve.

Similarly, when the customer can affect the condemnation rate of a DLR, the customer should pay the standard price if the returned carcass must be condemned. We recognize that there is a possibility that customer commands may demand ownership of serial numbers in response to such a policy. In this case, the cost of customer-induced condemnations must be weighed against the increased administrative costs of a repair-and-return system.

Implementation. This recommendation requires tracking a carcass from the base to inspection at the repair facility. It does not require a repair-and-return policy (unless customers demand serial number ownership). We say "inspection" rather than "completion of repair" because the price could be established when the needed repair is determined. (However, for some complex items that are difficult to diagnose, perhaps because of multiple failures, the full cost of depot repair may not be known until the repair has been completed.) The charge for each distinct repair activity should represent a standard cost of that activity (e.g., a fixed charge for the repair of a given SRU) rather than the actual material and labor used to make the repair. Thus, assuming the customer cannot affect the time it takes to accomplish each identified type of repair, variability in individual repair times should be ignored. Similarly, if there are several levels of difficulty of repair for a mechanical item, the charge for each should be a standard cost. Because there is a limited number of distinct repairs for each NSN, there should be a limited number of prices for each NSN.

Clearly, this pricing recommendation should be adopted only for selected NSNs: those for which incentives cause significant adverse selection problems. The Air Force could determine the cost and effectiveness of this recommendation by first implementing it for a few "pilot" NSNs.

The source of DLRs arriving at ALCs can be identified. In addition, at least one ALC, the Ogden ALC, can track repairs of avionics LRUs by serial number. (Our understanding is that these data are for the F-16,

F-15E, and F-117.) However, currently there is no method for connecting this information with a charge to the customer.

To reduce the financial uncertainty facing the wing, pricing should take place in two stages. First, the wing should be charged the average marginal repair cost at the time it exchanges an unserviceable for a serviceable DLR. The wing's account then should be debited or credited to reflect the condition of the carcass as soon as practical. With a fully automated system this could be done as soon as the necessary repairs are determined. Without such a system, the goal should be to adjust the charge to the wing within the same fiscal year so that the wing's costs are tied to its actions. This may prove difficult for items with lengthy times between entry into the supply system and induction into repair. However, under the Air Force's lean logistics initiatives, unserviceable DLRs will be inducted into repair soon after they are returned to the supply system, so the lag between the original billing and identification of needed repairs should be minimal.

> *Recommendation 2c: The exchange price for a DLR in excess supply should be discounted based on the length of time before repair or replacement is necessary.*

As the number of aircraft in the force structure declines, the Air Force may find itself with enough spare serviceable DLRs of a given type to satisfy demands for a year or more without repairing or replacing carcasses. Because repair can be deferred until the excess serviceable inventory is drawn down, the DLR exchange prices should be less than the costs that would be incurred if those DLRs were repaired immediately.[10] With each purchase of a serviceable item from the inventory, the date that repairs become necessary to satisfy demand for the item moves closer. Thus, the true marginal cost of each purchase is the discounted present value of the additional future repair costs imposed upon the supply system. (See the end of Appendix B for a derivation of this cost.)

The Air Force may choose to repair a portion of the returned carcasses each year to maintain technicians' repair skills. If it does so,

[10]The Army has adopted a similar strategy with its "Reduced Price Initiative" that lowers the standard price of some items that are in long supply.

then the DLR exchange price should be a weighted average of the marginal repair cost and the discounted cost described above. The weights are the proportion of carcasses repaired immediately and the proportion deferred, respectively.

In extreme cases, the Air Force may find itself with enough spares of a given type to satisfy demands for the remaining lifetimes of selected aircraft mission/design/series (MDS). In these cases, it would be a waste of resources for anyone—wing or depot—to repair or replace unserviceable carcasses (except in the unlikely event that the cost of local repair is exceeded by the cost of transporting serviceable units from the depot to the wing). The price charged for a serviceable item in long-term excess supply should reflect only the cost of the actions taken in response to the purchase and not include any charge for repair or replacement.[11] Doing otherwise could provide incentives for wings to seek alternative sources of repair, thereby increasing total costs to the Air Force.

Excess supply of NSNs could result from poor procurement procedures. Prices should reflect these excess supplies not only to prevent customers from taking repair actions that cost the Air Force money, but also to highlight the cost of poor inventory management.

Implementation. An automated financial system would require a discount rate, an estimate of the demand rate, the number of serviceables in excess supply, and proportions of exchanged carcasses to be repaired to compute these prices. In the absence of an automated system, prices should be adjusted in those selected cases in which the cost consequences of distorted incentives are largest. The distortion is positively related to the discount rate, the size of the excess supply, and the availability of low-cost local repair alternatives.

[11]An exception would be if the Air Force could sell the DLR elsewhere or return it to the manufacturer for a refund. In this case, the sales or refund value of the item would be a current cost and should be included in the DLR price.

Wings and Depot Repair Shops Are Not Customers for Some Depot Services

Recommendation 3: Headquarters U.S. Air Force should be the customer for services that may be undervalued by customer commands.

There may be some costs unrelated to the rate of repair that should not be recovered from customer commands. For example, much of the engineering services focus on extending the life of basic airframes. With tight budgets, commands might let some of the long-term engineering services (e.g., configuration management and lead-the-fleet testing programs) atrophy rather than cut back on the current flying-hour program. If this is not the appropriate decision from the Air Force point of view, then Hq USAF should be considered the customer and pay for the services. More generally, services considered valuable to the Air Force but at risk of being undervalued by customer commands should be paid for by direct appropriation.[12]

Pipeline Inventory Fees Can Be Used for Rewards and Penalties

Recommendation 4: Pipeline inventory fees should be used to penalize delays and reward reductions in pipeline times at wings and depot repair shops.

Pipeline times are affected by how the unserviceable item is handled within the supply system and in repair as well as by the actions of customers. Pipeline inventory costs increase when repair processes are delayed. Wings increase pipeline inventory costs when they delay turning in carcasses after drawing serviceable units from supply.

Wings should be charged an additional fee, separate from the exchange price, for each day they delay turning in a carcass after receiving a serviceable unit.[13] These additional fees will encourage

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[12]We are indebted to our colleague Ray Pyles for this point.

[13]See case 4 in Appendix B for a definition of the daily pipeline inventory cost for an NSN.

wings to weigh the costs of turning in unserviceable items concurrent with drawing serviceable ones versus delaying to effect cannibalization. Similarly, by charging repair shops (or other responsible parties) for delays and rewarding reductions in repair times (relative to the average times included in the exchange price), pipeline inventory charges can promote efficient repair processes.

Implementation. Fees charged to wings for delays in returning unserviceable carcasses must not be collected through reduced carcass prices. Such a reduction in carcass prices would reduce incentives for turning in long-delayed carcasses. It may be necessary to accumulate these fees off-line and charge them on a monthly or quarterly basis. The key is that wings see the costs of their actions during the same budget year as much as possible. However, for a given delayed carcass, a wing should incur no additional pipeline fees once cumulative fees associated with that transaction equal the carcass price.[14]

In cases of significant improvements in depot repair times, prices should be adjusted soon after the improvement to reflect the new pipeline times. If prices are not updated off-line, depot shops will receive rewards for performing at what should be considered their normal level for up to two years after the change. Also, customers will not receive accurate cost information through prices.

In the absence of an automated billing system, it is likely that the benefits of pipeline inventory fees will not justify the implementation expense.

GENERAL IMPLEMENTATION ISSUES

These recommendations vary in the extent of changes to the financial management system they require. The most significant gains would come with the least costly change—excluding the fixed costs in the surcharge from DLR prices and tying the variable costs in the

[14]We recognize that this method of implementing pipeline fees will cause a customer who loses a carcass to incur charges for the transaction that are greater than the standard price of the item. However, we do not perceive this to be a likely scenario. This situation could be avoided by deducting the pipeline fees from the carcass price. We chose not to do this in order to provide customers with the full incentive to return a carcass at any point after a transaction has occurred.

surcharge (e.g., DLA issues and receipts, condemnations) to the NSNs that generate them.[15] Even recovering these fixed costs through arbitrary charges to commands—e.g., in proportion to total demand—would improve the alignment of Air Force costs and command incentives.

The United States Transportation Command (TRANSCOM) Working Capital Fund, formerly DBOF-T, provides an example of a financial management system that does not recover all costs through transaction prices to customers. As discussed above, airlift rates are set to be competitive with commercial carriers. Remaining costs are recovered through direct appropriations.[16]

Price system recommendations that require more significant expenses should be implemented on a small scale to determine if they have the desired effects on decisionmaking. For example, charging differential prices for a few DLRs whose states of repair are most influenced by customer behavior would provide a basis for evaluating the benefits of this aspect of DLR pricing. However, any introduction of differential prices must be viewed by customers as being permanent. Otherwise, only short-run behavior will be influenced.

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[15]Tying *all* variable costs to the NSNs that generate them is not easy, even without the refinements associated with tracking the states of repair of individual items, and can be costly.

[16]Undersecretary of Defense, DOD 7000.14-R, pp. 52–2 and 3.

Table 5

Summary of Recommendations

Major Costs	Location in Current Exchange Price Structure	Recommended Method of Recovery
Condemnations	Surcharge	Exchange price/standard price • Average cost associated with individual NSNs when customer cannot affect carcass condition • Cost associated with specific items otherwise
First destination transportation COD: DLA issues & receipts COD: item management	Surcharge	Exchange price/standard price • Average cost associated with individual NSNs
Price stabilization Depreciation Inventory maintenance Inflation COD: other inventory control point activities	Surcharge	Fee to customer commands • If attributable to specific NSNs or specific demands, charge according to usage • Otherwise, arbitrarily allocate
Direct materials Direct labor Utilities (repair facilities)	DRC DRC DRC: G&A	Exchange price • Average repair cost for a given NSN if customer cannot affect the state of the returned carcass • Average cost of the specific repair otherwise

Table 5—continued

Major Costs	Location in Current Exchange Price Structure	Recommended Method of Recovery
Indirect labor Schedulers Planners Indirect material	DRC: production overhead	Exchange price • Costs associated with individual NSNs to the extent feasible
Equipment depreciation	DRC: production overhead	Fee to customer commands • If attributable to specific NSNs or specific demands, charge according to usage • Otherwise, arbitrarily allocate
Base support HQ costs Utilities (nonrepair related)	DRC: G&A	Fee to customer commands • Arbitrary allocation