DEPARTMENT OF THE NAVY
NAVAL SEA SYSTEMS COMMAND
WASHINGTON, DC 20362-5101

IN REPLY REFER TO
NAVSEAINST 5041.3
OPR CHENG-Q
27 OCT 1988

NAVSEA INSTRUCTION 5041.3

From: Commander, Naval Sea Systems Command

Subj: PRODUCT SUBSTITUTION FRAUD

Ref: (a) SECNAVINST 5430.92A

1. Purpose. To issue procedures for the control, monitoring, investigation, and reporting of suspected or verified product substitution fraud by contractors supplying systems, equipment, components, material, or services to the Naval Sea Systems Command.

2. Background. The frequency of reported Command cases of unauthorized product substitution for purchased material is increasing. Most unauthorized product substitution results from poor material, production control or both, or intentional substitution. Each instance of suspected fraud must be quickly evaluated and aggressively pursued until resolved and the potential impact on end-users must be reported. Appropriate corrective actions to purge unauthorized substitute material must be taken. Unauthorized product substitution affects the safety of personnel, the mission of ships and field activities, increases costs and reduces available resources. This instruction is separate and distinct from the Unsatisfactory Material Reporting Program (NAVSEAINST 4855.7A) which is used to report unsatisfactory material, effect corrective actions and prevent recurrence.

3. Exception. The Deputy Commander for Nuclear Propulsion (SEA 08) is responsible for all technical matters pertaining to nuclear propulsion of U.S. Naval ships and craft including all aspects of integration of the nuclear plant into the ship system. Nothing in this instruction detracts in any way from those responsibilities. Accordingly, SEA 08 will be consulted in all matters relating to or affecting the nuclear propulsion plant, associated nuclear support facilities and vendors of the nuclear propulsion program.

4. Definitions

a. Product Substitution Fraud. Any willful substitution of products or materials, including adulteration or substitution of certification documents, that results in the acquisition of unauthorized materials.

b. Coordinating Authority. Coordinates information and action associated with product substitution fraud.

c. Action Point. Informs cognizant authorities, investigates and analyzes preliminary information for subject product substitution, makes recommendations for actions or non-actions to be taken, provides assistance as required.

5. Policy. The Command will aggressively investigate all suspected or verified instances of product substitution fraud and ensure that criminal, civil, administrative and contractual actions (or both) are initiated when justified.

6. Responsibilities and Actions. The Deputy Chief Engineer for Design and Manufacturing Quality (CHENG-Q) is designated as the action point for matters involving product substitution fraud. The Naval Material Quality Assessment Office (NMQAO) is the point of contact within CHENG-Q. Actions to protect the Government from the acquisition of fraudulently substituted products are the responsibility of the procuring activities. The Deputy Commander for Nuclear Propulsion (SEA 08) shall be consulted for all matters involving nuclear propulsion plant material.

a. Inspector General (SEA 00N). Act as the Command coordinating authority for all matters of suspected or verified product substitution fraud:

(1) Inform CHENG-Q and provide pertinent information when a product substitution allegation has been made that requires CHENG-Q support.

(2) Conduct preliminary investigation to determine whether to proceed or terminate the case.

(3) Coordinate with technical and legal personnel to assess the probability of criminal or civil prosecution. Define those cases which should be handled administratively.

(4) Coordinate with the Naval Investigative Service (NIS), as appropriate.

(5) Ensure that the procuring activities consider appropriate administrative action.

(6) Task cognizant authorities to prepare a remedies plan in accordance with reference (a).

b. Deputy Chief Engineer for Design and Manufacturing Quality (CHENG-Q). Act as Command action point for suspected or verified product substitution fraud:

(1) Assist in preliminary investigations.

(2) When appropriate, notify and coordinate with cognizant Command procurement, technical and acquisition directorates of suspected or verified cases of product substitution fraud.

(3) During formal investigations, act as or coordinate for the Command technical representative and work with Government organizations involved (e.g. NIS, FBI, Assistant U. S. Attorney). All parties shall ensure that proper confidentiality is maintained.

(4) Provide periodic status reports to the SEA 00N, as appropriate.

(5) At the conclusion of an investigation, issue a letter report to SEA 00N, with a copy to the cognizant Deputy Commander, summarizing the findings and recommendations of the investigation. When administrative action will protect Government interests better than civil or criminal prosecution, the letter will recommend appropriate action.

(6) Assist cognizant authorities in the preparation of remedies plans as defined in reference (a).

(7) Coordinate with headquarters, fleet and field activities to assess technical and shipboard impact.

(8) Develop monetary values of loss or damage to the Government. This information will be used to recoup charges.

(9) Provide rationale for administrative action to appropriate contracting authorities.

(10) Provide assistance to investigative and legal agencies as required.

(11) Issue debarment recommendations to SEA 02 when NMQAO data is more comprehensive than data available to other activities that normally issue debarment letters, i.e. Defense Logistics Agency, Naval Supply Systems Command.

(12) As part of the normal work process, be alert for and segregate all instances in which product substitution fraud is suspected. Suspected or verified instances of fraud may be identified under one or more of the following circumstances: inspection or examination of material; telcons with activities or vendors; reviewing nonconformances; vendor histories; survey results; informants.

c. Deputy Commanders for Ship Design and Engineering (SEA 05) and Weapons and Combat Systems (SEA 06)

(1) Provide technical guidance as required with regard to matters involving known or suspected nonconforming products.

(2) Determine viability of use of systems, equipment, components, material, or services that involve a suspected or known substitution.

(3) Provide liaison with field activities.

(4) Ensure that field activity material control procedures are adequate to prevent the use of nonconforming systems, equipment, components, material, or services.

(5) Assist cognizant authorities in preparing remedies plans, in accordance with reference (a).

d. Deputy Commander for Industrial and Facility Management (SEA 07)

(1) Provide liaison with shipyards and Supervisors of Shipbuilding points of contact.

(2) Ensure that Navy shipyards and Supervisors of Shipbuilding material control procedures are adequate to prevent the use of nonconforming systems, equipment, components, material, or services.

(3) Assist cognizant authorities in preparing remedies plans, in accordance with reference (a).

e. Deputy Commander for Contracts (SEA 02)

(1) Provide guidance to Command field contracting offices on dealing with suspected or verified fraudulent vendors and assure that appropriate actions are taken to protect the interests of the Government, including the forwarding of reports required by DFARS 3.409.

(2) Assist cognizant authorities in preparing remedies plans, in accordance with reference (a).

f. Office of Counsel (SEA 00L)

(1) Provide legal guidance on product substitution cases.

(2) Provide liaison with Assistant U.S. Attorney and other legal agencies and points of contact on legal matters.

(3) Assist in preparing remedies plan.

g. Deputy Commanders for Surface Ships, Submarines, Amphibious, Auxiliary, Mine and Sealift (SEA 91, 92, 93)

(1) Implement corrective action to preclude the use of suspected nonconforming systems, equipment, components, material, or services in ships.

(2) Provide for inspection of installed nonconforming systems, equipment, components, material, or services in ships and determine impact.

(3) Provide assistance to SEA 00N and CHENG-Q as required.

h. Shore Activities

(1) Immediately advise NMQAO, through the proper chain of command, of all suspected instances of product substitution fraud.

(2) Advise SEA 00N of all suspected instances of product substitution fraud as specified in paragraph 7.a.

7. Reporting Procedures

a. Suspected product substitution fraud by a contractor shall be reported by cognizant field activities or headquarter codes through the cognizant Deputy Commander to SEA 00N. Distribution shall be limited by the originator to the Deputy Commander and SEA 00N. If the suspected product substitution or fraud involves critical material and time is a major concern, a telephone report to SEA 00N is preferred for the initial report.

b. When investigations exceed three months, NMQAO will submit status reports to SEA 00N.

8. Handling of Information. Unauthorized, premature or indiscriminate disclosure of information may compromise an ongoing investigation and damage the reputation of persons or companies that may be innocent of wrongdoing. All unclassified information shall be held close and shall be marked "FOR OFFICIAL USE ONLY". Classified information shall be processed in accordance with applicable security regulations.

9. Reports. The reporting requirements contained herein are exempt from reports control by OPNAVINST 5214.7.

M. MACKINNON III
Vice Commander

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