Schnozzles experienced a cost underrun of about $681,250 in relation to the cost estimates for direct labor and the related manufacturing overhead included in the purchase order price, or a profit equivalent to 60% of cost. This underrun resulted primarily because of reduced labor costs obtained by using mass production methods, and more than $400,000 of special equipment financed by the Air Force under Hi-Missile's prime contract. In October 1962, at the time of negotiation for the 1300 nozzles it was not precisely known when this special equipment would become available and operative. However, it was generally understood by Hi-Missiles, Schnozzles, and the Government, that the special equipment would be used in producing the nozzles.

PROBLEM

In a review of the prime contract awarded to Hi-Missile Corporation, should this case be considered as an apparent defective pricing situation?