



UNITED STATES GENERAL ACCOUNTING OFFICE
 REGIONAL OFFICE
 26 FEDERAL PLAZA
 NEW YORK, NEW YORK 10007

Dir. OPSS

07-116

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FEB 8 1971

Major General Erwin M. Graham, Jr.
 Commanding Officer
 U.S. Army Munitions Command
 Dover, New Jersey 07801

DLG 05780

Dear General Graham:

We have reviewed the April 17, 1968, proposal submitted by System and Instruments Division, Bulova Watch Company, Inc., to the U.S. Army Ammunition Procurement and Supply Agency (APSA), Joliet, Illinois, for M524A5 fuses. On the basis of this proposal, contract DAA09-68-C0233 was awarded on April 26, 1968, for 1.6 million fuses at a total price of \$10,414,727.

DLG 05781

The contract included a defective pricing clause providing for a reduction in price if the price was increased by a significant amount because the contractor furnished incomplete, inaccurate, or noncurrent cost or pricing data. Negotiations were held on April 17, 1968, and Bulova submitted the required cost or pricing certificate on April 25, 1968.

LABOR COST ESTIMATES HIGHER
 THAN INDICATED BY AVAILABLE
 COST OR PRICING DATA

The firm fixed price negotiated was about \$707,400 higher than it should have been because Bulova used inaccurate cost information in preparing its proposal. This amount includes direct manufacturing labor plus applicable overhead, general and administrative expenses, and profit (see app. I, II).

[Review of Bulova Watch Co., Inc. Proposal]

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Bulova originally proposed \$1,2231 for unit manufacturing labor costs. This rate was computed by applying actual average hourly labor rates to the standard time required to make a fuse. During negotiations on April 17, 1963, Bulova increased this amount to \$1,4635. AFSA representatives questioned the unit cost because "standard hours should be applied to standard rates, and actual hours should be applied to actual rates." A unit manufacturing labor cost of \$1.31444 was negotiated subject to Bulova furnishing a justification for its revised proposal.

On April 19, 1963, prior to the contract award and submission of the pricing certificate, Bulova furnished the requested justification. Bulova justified its labor unit cost by citing its costs on a previous contract, DALL-173-AMC-834(A), which it adjusted for a subsequent wage increase. (See app. III.) This new information was not admitted by Government personnel prior to the award of the contract.

Inaccurate data

The Bulova computation was misleading since it contained inaccurate data. Correct information would have shown a labor unit cost of \$1.11213 for units to be manufactured before the wage increase and \$1.15713 for units manufactured thereafter. (See app. III)

The prior contract, 834(A), called for fuses, fuse less arming mechanisms, and arming mechanisms. The number of equivalent fuses produced had to be computed to determine unit costs. Bulova did this by using the selling prices of the arming mechanisms and the fuse as follows:

		<u>Selling price</u>	<u>Percent</u>
Fuse less arming mechanism		\$3.90	57.778
Arming mechanism		<u>2.85</u>	<u>42.222</u>
Fuse		<u><u>16.75</u></u>	<u><u>100.000</u></u>
	<u>Contract quantity</u>	<u>Percent</u>	<u>Total</u>
Fuses	466,000		466,000
Fuse less arming mechanism	333,000	57.778	221,290
Arming mechanism	1,312,130	<u>42.222</u>	<u>554,028</u>
Equivalent fuses		<u><u>100.000</u></u>	<u><u>1,241,318</u></u>

The use of selling prices was invalid since the labor expended on the fuse components was not in the same ratio as their selling prices. Bulova's labor standards showed that labor required for the arming mechanism was twice that needed for the fuse less arming mechanism as follows:

	Standards	Percent
Fuse less arming mechanism	\$ 418,86	33.152
Arming mechanism	843,98	66.848
Fuse	<u>1,262,84</u>	<u>100,000</u>

Using the above standards the equivalent units should have been computed as follows:

	Actual delimitation	Percent	Total
Fuses	466,000		466,000
Fuse less arming mechanism	383,338	33.152	127,083
Arming mechanism	1,330,180	66.848	859,199
Equivalent fuses		<u>100,000</u>	<u>1,452,282</u>

The increase in equivalent fuses to 1,452,282 significantly decreases the historical labor unit costs.

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We discussed this matter with officials of the New York Branch Office, Defense Contract Audit Agency, and AFSA officials including the Deputy Chief, Procurement Division, and the procurement controlling officers. They agreed, that based on the information we furnished, there was defective pricing on the subject contract on which Bulova had a cost overrun of about \$1,250,000.

We recommend that the contracting officer exercise the Government's right to a price adjustment under the defective pricing clause of the contract. We also suggest that procurement officials stop negotiating prices before adequate analyses of contractor furnished data are performed.

Please advise us within 60 days of any actions taken or planned.

A copy of this letter is being forwarded to the Director, Defense Contract Audit Agency.

Sincerely yours,

Alfonso J. Strassullo
Regional Manager

Enclosure:
as stated

cc: Director, OPSS ✓

APPENDIX I

COMPUTATION OF AMOUNT
OF DEFECTIVE PRICING

Excess direct manufacturing labor (see app. II)	\$303,632.00
Overhead (100%) allowed in negotiations Subtotal	<u>303,632.00</u> \$607,264.00
General and administrative expense (5.9%) allowed in negotiations Subtotal	<u>35,828.58</u> \$643,092.58
Profit (10%) allowed in negotiations Total	<u>64,309.26</u> <u>\$707,401.84</u>

APPENDIX II

COMPUTATION OF PROPOSED MANUFACTURING LABOR COSTS IN EXCESS OF EXPERIENCED COSTS

	<u>Deliveries</u>		<u>Total</u>
	<u>Prior to Feb. 1, 1969</u>	<u>After Feb. 1, 1969</u>	
Negotiated manufacturing labor costs	\$1.31444	\$1.31444	
Actual experienced costs, adjusted for wage increases (see app. III)	<u>1.11213</u>	<u>1.15773</u>	
Difference	<u>\$.20231</u>	<u>\$.15671</u>	
Number of units	<u>1,160,000</u>	<u>110,000</u>	<u>1,600,000</u>
Excess labor costs	<u>\$236,679.60</u>	<u>\$68,952.10</u>	<u>\$303,632.00</u>

APPENDIX III

COMPUTATION OF UNIT MANUFACTURING
LABOR COST

Employee's April 19, 1968, letter

Actual labor including tooling	\$1,681,146.73 ^a
Overtime premium	<u>53,142.76^b</u>
Total	<u>\$1,734,289.49</u>

Equivalent units	<u>1,241,318</u>
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Manufacturing costs per unit	\$ 1.39715
Add: 4.9% wage increase	<u>.06816</u>
Projected unit cost	<u>\$ 1.46531</u>

GAO Computation

Actual labor costs recorded in contractors records - without overtime premium

1967 Manufacturing labor	\$ 513,916.85	
Tooling	<u>57,477.49</u>	\$ 571,394.34

1968 Manufacturing labor	\$1,050,988.96	
Tooling	<u>50,627.88</u>	<u>1,101,616.84</u>

Total labor including tooling	\$1,672,811.18 ^c
Less tooling	<u>107,905.37^b</u>
Total	\$1,564,905.81

Add: Wage increases to 2/1/69	<u>83,588.84</u>
Total projected cost	<u>\$1,648,494.65</u>

Equivalent units	<u>1,482,282</u>
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Manufacturing labor cost per unit to 2/1/69	<u>\$ 1.11213</u>
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Manufacturing labor cost per unit after 2/1/69 (4.1% increase effective 2/3/69)	<u>\$ 1.15773</u>
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^aPart of factory overhead

^bProvided for separately in price

^cContractor could not explain why he reported \$8,335.55 in excess of booked costs.