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Review Of The Army's Plan To Close The Army Pictorial Center, Long Island City, New York

B-146711

Department of the Army

BY THE COMPTROLLER GENERAL OF THE UNITED STATES

JUNE 7, 1971

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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

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Dear Mr. Chairman:

This is in reply to your letter of April 14, 1970, in which you requested that the General Accounting Office (GAO) review the Army's plan to phase out motion-picture production at the Army Pictorial Center, Long Island City, New York. As agreed with Mr. Daniel F. Ruge, Executive Secretary to the Steering Committee of the New York Congressional Delegation, we examined the case study that the Army Materiel Command had made to support, from a financial standpoint, the Army's decision to close the Center.

We reviewed the Army's methods for developing the study's statistical and accounting data, to determine whether the application of this data appeared to be logical and consistent. We did not audit accounting records to verify the accuracy of the data analyzed.

As a result of a previous study of all its audio-visual activities, the Army decided to reduce the Center's mission by authorizing the Continental Army Command to be responsible for production of its own training films. Therefore, to determine potential savings from closing the Center, the case study compared the estimated costs of retention of the Center (assuming this reduced mission) with the estimated costs of full closure of the Center (assuming that its reduced mission would be accomplished in total by commercial contractors and by other Army activities).

The factors considered were operating costs over the 5-year period ending June 30, 1975, the one-time costs of closure and relocation of the Center's activities, and the one-time income from disposal of the Center's real property.

Estimates for the amounts involved were discounted to their present value, in accordance with the policy set forth in Department of Defense instructions, to give effect to the fact that all transactions would not occur immediately but would take place over the 5-year period considered by the Army's study. The present value technique is based on the principle that a dollar received today is worth more than a dollar to be received a year from now. It requires use of discount rates, which in this case were those stipulated in Circular A-94 published by the Bureau of the Budget, now the Office of Management and Budget.

The case study concluded that, if the Center were closed and its mission accomplished elsewhere, the Army would save about $17.3 million over the 5-year period. We believe that this estimate is excessive by at least $9.4 million, as shown below.

	Army study	GAO review	Difference
	(millions)		
Savings in operating costs--5 years--gross	$20.0	$9.6	$10.4
Savings in operating costs--5 years--(present value)	$15.8	$7.6	$ 8.2
Deduct one-time costs of closure (present value)	2.2	3.4	(1.2)
Subtotal	13.6	4.2	9.4
Plus proceeds from disposal of real property (present value)	3.7	3.7	-
Net savings	$17.3	$7.9	$ 9.4

In addition to these dollar adjustments, we point out below several other significant factors in the study which, we believe, were not given sufficient attention by the study group. More extensive development of these factors by the study group might have resulted in estimated savings less than those shown in the study.

Operating costs

The case study concluded that, over a 5-year period ending June 30, 1975, the Army would save approximately $20 million in operating costs if the Center were closed and its work load accomplished elsewhere. We have identified a variety of deficiencies in the study and have made adjustments totaling about $17 million--$13.7 million in decreases and $3.3 million in increases--to the operating cost savings shown in the study. As adjusted, the estimated savings in operating costs amount to about $9.6 million over a 5-year period. On the basis of present value, the adjusted estimated operating savings amount to about $7.6 million.

We noted other estimated operating costs which, we believe, had been based on inappropriate assumptions on the part of the study group. We did not develop alternative estimates for these items, which included the number of personnel required to operate the Center with its reduced mission and the amount of travel necessary under the alternatives considered, because we found that the other deficiencies, which we estimated in the amount of $17 million, were of such significance as to indicate that the data used in the case study were not consistently or thoroughly developed.

The estimated cost of producing motion pictures commercially, if the Center were to be closed, comprised 60 percent of the Army's projected 5-year operating costs. This estimate is of doubtful validity because of the method used to develop projected costs.

Our findings relating to the estimated operating costs are considered in more detail in pages 7 to 11.

One-time costs and income

With respect to one-time costs involved in closing the Center, the Army estimate, in our opinion, was understated by about $1.2 million. This represents estimated costs of personnel who will remain at the Center through June 30, 1972, presumably for the caretaker functions of property maintenance and protection. Although the Army has included the estimate in the 5-year operating costs, we believe that it should more properly be included as a one-time cost.

The cost study included as one-time income an amount of $3.7 million, representing the appraised fair market value of the Center's real estate discounted to its present value.

This procedure is in accordance with Department of Defense policy, and we have not adjusted the Army's estimate for this item. It should be noted, however, that in disposal of such properties, other requirements, such as use by another Federal agency or by state or local governments, would take precedence over sale on the open market. In the event that the facility is disposed of in this manner, the Government may not realize any proceeds.

Another one-time cost not considered by the Army is that of early retirement of employees to be released through closure of the Center. Although we did not determine the amount involved, we think that the Army should have considered this factor since the study group estimated that 153 people, or 40 percent of the Center's civilian staff, would retire.

We discussed our findings with officials of the Army Materiel Command. They agreed with certain substantial adjustments and indicated that they would consider the others. They have not provided us, however, with an overall assessment of our findings. We have not requested formal comments from the Secretary of Defense on this report. We plan to make no further distribution of this report unless copies are specifically requested and then we shall make distribution only after your agreement has been obtained or public announcement has been made by you concerning the contents of the report.

We trust that this information meets your needs.

Sincerely yours,

Elmer B. Staats

Comptroller General
of the United States

The Honorable Emanuel Celler
Chairman, Steering Committee
New York Congressional Delegation

BACKGROUND

On August 6, 1969, the Adjutant General, Department of the Army, requested that the Army Materiel Command conduct a case study to determine the economic desirability of continuing operation of the Army Pictorial Center. The request noted that a March 1969 report on an Army-wide study of audio-visual activities had recommended that the Continental Army Command use its television facilities to produce the majority of films required by its various training organizations. The Center had been accomplishing this work load, but it had relied exclusively on motion picture filming in preference to producing selected subjects by television.

Recognizing that the Army-wide study had been approved, the Adjutant General noted that the Center's loss of the responsibility to produce the majority of films required by the Continental Army Command would reduce its work load by about 45 percent by the end of 1973.

The case study assumed that the Continental Army Command would begin producing its own television films without the need for further approval. Therefore, in considering the overall savings or costs to the Army to retain or to close the Center, the study group did not include an estimate for the cost of television production by the Continental Army Command.

Three alternatives were considered in the case study.

1. Retention of the existing facilities of the Center, acknowledging the 45-percent reduction in the motion-picture work load expected to occur with the loss of the responsibility to produce films required by the training activities of the Continental Army Command.

2. Partial closure of the Center which would retain only film distribution and depository functions.

3. Full closure of the Center and transfer of its functions to other facilities of the Materiel Command.

The study group computed estimates of costs pertinent to each of the three alternatives for the 5-year period ending

June 30, 1975. The results showed that the continued operation of the Center would cost the Government approximately $49 million over the period, that partial closure of the Center would cost some $37 million, and that full closure of the Center and transfer of its work load elsewhere would cost only $29 million. The case study concluded that alternative 3, with expected savings of $20 million, was the most economical course of action. Our comments concern the study's comparison of alternatives 1 and 3.

DEFICIENCIES IN THE STUDY

There are several major deficiencies in the Army Materiel Command's case study. These pertain to the method used to develop cost estimates for obtaining motion pictures from commercial sources and improper omission of certain cost estimates and inclusion of others.

DEVELOPMENT OF COST ESTIMATES FOR OBTAINING MOTION PICTURES FROM COMMERCIAL SOURCES

The most prominent weakness in the case study is in the cost estimates for having motion pictures produced commercially.

Under alternative 3--complete closure of the Center--officials of the Army Materiel Command anticipated that about 85 percent of the Army's motion-picture requirements would be obtained from commercial sources. The case study cost estimate of $17.6 million for this service represents about 60 percent of the total estimated costs of $29 million for alternative 3. The estimate was based on an analysis in an Army Audit Agency report of December 18, 1969, which compared estimates for producing certain motion pictures at the Center with quotations obtained from selected firms for producing the same pictures.

There were several deficiencies in the analysis, particularly concerning the solicitation of quotations from contractors. Officials of the Center, with the approval of the Army Audit Agency, selected five scripts, considered to be representative of the Center's work load for 1969, for use in soliciting pricing proposals from 25 contractors. Each of the 25 contractors was asked to submit proposals on 2 scripts. In this manner 10 proposals were solicited for each of the five scripts selected for a total of 50 proposals.

At the time of the study, Army Audit Agency personnel noted that the number of scripts upon which the proposals were based was small in relation to the production work load and that the scripts were of a type representative of only about 70 percent of the Center's work load.

Officials of the Army Audit Agency and the Materiel Command noted that the requests for prices had specified two conditions that would affect the credibility of the responses. They specified that (1) no current award could be expected and (2) no reimbursement would be made for preparing the proposals.

Only 17 pricing proposals, out of the 50 solicited for purposes of the comparison, were received. Auditors of the Materiel Command expressed the belief that the number of responses did not constitute a large enough sample upon which to develop valid cost data for a comparative analysis. Despite the reservations of the auditors of the Army Audit Agency and the Materiel Command, however, the contractors' pricing proposals were used in the cost comparison included in the Army Audit Agency report.

Officials of the Center noted that most of the contractors' proposals had omitted costs for certain required skills, crafts, and services. Because of time limitations, these officials did not attempt to obtain more complete quotations, but rather, they developed an adjustment to compensate for the omission. Documents that we reviewed indicated that the Army Audit Agency had planned to include this adjustment in the cost comparison to be included in its report. The adjustment was not included, however, in the final report of the Army Audit Agency. The effect was to lower the estimate of costs attributable to obtaining motion pictures from commercial sources.

We believe that the Army Audit Agency should have investigated this matter further to determine whether the omissions from contractors' proposals were significant. We noted that auditors of the Materiel Command were of the opinion that the cost adjustment formulated by Center officials, but not included in the study, was reasonable considering the circumstances surrounding the solicitation.

As a result we believe that the analysis contained in the Army Audit Agency report is not acceptable and that the estimates of contractor costs included therein should not have been used in the case study.

IMPROPER OMISSION AND INCLUSION OF COST ESTIMATES

A number of costs were excluded from the study or, in some instances, were included improperly. We identified several items that had been duplicated in the study.

The following schedule shows the case study estimates for alternatives 1 and 3 and the $17 million in adjustments--both increases and decreases--that we feel are appropriate. The net adjustments decrease the estimated cost savings by $10.4 million.

GAO Adjustments to the Case Study and Economic Analysis

	Alternatives 1	Alternatives 3	Gross estimated cost savings
Total operating costs	$48,973,555	$28,956,823	$20,016,732
Cost items eliminated by GAO which reduce operating costs:			
Personnel	-	3,008,185	3,008,185
Communications	240,000	25,000	-215,000
Rent and utilities	4,760,000	-	-4,760,000
Supplies and materials	1,024,000	240,000	-784,000
Total decreases in operating costs	6,024,000[a]	3,273,185[b]	-2,750,815
Adjusted operating costs	42,949,555	25,683,638	17,265,917
Cost items added by GAO which increase operating costs:			
Personnel	-	337,111[a]	-337,111
Laboratory services	-	7,354,250[a]	-7,354,250
Total operating costs after adjustments	$42,949,555	$33,374,999	$ 9,574,556
Gross net decrease in the savings in operating costs			$10,442,176

[a]Decreases to cost savings	$13,715,361
[b]Increases to cost savings	3,273,185
Total deficiencies	$16,988,546

Note: These figures have not been discounted.

Cost items eliminated by GAO which reduce operating costs

Personnel costs

Under alternative 3 we eliminated two of the estimates for personnel requirements totaling about $3 million. The first estimate of $1.6 million pertains to the personnel costs at the U.S. Army Missile Command for administering commercial motion-picture production contracts over the 5-year period. This cost had already been included in alternative 3 under the category of contractor costs.

The second estimate of $1.4 million that we eliminated as an operating expense of alternative 3 involved the costs of personnel remaining at the Center after its closure on June 30, 1970. These personnel will remain at the Center from July 1, 1970, through June 30, 1972, presumably for the caretaker functions of property maintenance and protection. We believe that such costs should not be considered as normal operating costs under alternative 3, but as one-time expenses associated with the closure of the Center. Accordingly, we added this estimate, discounted to its present value of $1.2 million, to the study estimate of one-time costs.

Cost of communications

The estimates of $240,000 for communications for alternative 1 and $25,000 for alternative 3 duplicated other cost estimates in the study. We eliminated these amounts in our computation.

Cost of rent and utilities

The case study included an amount of almost $4.8 million for rent and utilities for alternative 1. This element of cost, more properly entitled repair and utilities, was composed of such items as salaries and wages, materials and supplies, contractual services, and other costs which were also included in the case study under separate cost categories. Thus the estimated costs of continuing the operation of the Center were overstated by $4.8 million.

· Cost of supplies and materials

Supplies and materials were estimated at $4.9 million under alternative 1 and $1.2 million under alternative 3. These estimates come from the historical budget costs of the Center.

We found that the estimates had not been based on the Center's most recent experience. Using more recent data available at the time of the study, we estimated that supplies and materials for alternative 1 would be approximately $3.9 million or about $1 million less than shown in the study. Similarly, the study figure for supplies and materials for alternative 3 should be reduced by about $240,000.

Cost items added by GAO which increase operating costs

Personnel costs

In considering alternative 3, the study group failed to include an estimate for the cost of personnel required to provide certain script-writing services, a function formerly done at the Center. On the basis of historical data at the Center, we estimate that this service will cost about $337,000 for the period covered, and we have added this amount to alternative 3.

Costs of laboratory services

The case study guidance stated that release printing, a major part of laboratory processing costs for the distribution of motion pictures, would be accomplished by commercial contract. In its calculations for alternative 3, however, the study group made no estimate for this service, for performance either by the Government or by contract. The study group further failed to provide an estimate for certain types of laboratory services connected with the film depository function. Using historical costs of the Center as a basis for our calculation, we estimate that the cost of these laboratory services will be approximately $7.4 million over the 5-year period.