

DOCUMENT RESUME

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[Commercial versus Government Storage]. B-146779; LCD-76-241.
October 18, 1976. 6 pp.

Report to Frank A. Schronz, Assistant Secretary, Department of Defense; by Fred J. Shafer, Director, Logistics and Communications Division.

Issue Area: Facilities and Material Management: Federal Transportation of Things (704).

Contact: Logistics and Communications Division

Budget Function: National Defense: Department of Defense - Military (except procurement & contracts) (051).

Organization Concerned: Department of the Air Force: Kelly AFB, TX; Department of the Army: Oakland Terminal, CA; Department of Defense.

Congressional Relevance: House Committee on Armed Services; Senate Committee on Armed Services.

Protests by the Department of Defense (DOD) of the use of Government warehouses rather than commercial storage for the storage of household goods are discussed. A potential saving of \$576,956 by using unused Government-owned facilities at Kelly Air Force Base, Texas, was proposed. Findings/Conclusions: A one-time saving of over \$14 million and an annual saving of \$700,000 is now indicated by DOD; however, if the space could be used in a way that would result in greater savings, GAO would support the alternative use. At Oakland (California) Army Terminal, DOD took exception to four cost elements: storage in transit, packing and draying, opportunity costs, and self-insured liability. DOD alleged that storage in transit costs would be incurred under both Government and commercial storage and should be included in computations; these costs were included in computations under both alternatives. DOD believes that packing and draying costs would be incurred by conversion to a Government storage operation; it is felt that such costs would be the same regardless of the facilities used. Recommendations: Because the Oakland facility was vacant for a long period of time, the costs accounting principle of opportunity cost should be foregone. The subject of self-insured liability has little impact on comparative cost allowances. (RS)

01100



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

LOGISTICS AND COMMUNICATIONS
DIVISION

OCT 18 1976

B-146779

The Honorable Frank A. Schrontz
Assistant Secretary of Defense
(Installations and Logistics)

Dear Mr. Schrontz:

In your May 18, 1976, response to our report on the use of Government versus commercial facilities for storing household goods (OSD Case #4280), you said that the Department of Defense (DOD) concurred with our premise which was to use space in Government warehouses for the storage of household goods when it is more cost effective than commercial storage. You disputed some of the cost factors used in our report; however, you indicated that DOD would initiate a study to identify other areas where the use of available warehousing capacity would result in a saving.

In our opinion, further DOD studies may yield negative results unless some of the points raised by your response are considered. We therefore offer the following comments to the specific points of difference.

KELLY AIR FORCE BASE

In our report we cited a potential saving of \$576,956 annually by using Government-owned facilities at Kelly Air Force Base, Texas, instead of using commercial storage facilities. At the time of our review, the space was not being used, there was no alternative-use plan, and we had identified an area that offered a potential for saving--the storage of household goods. DOD now indicates that a one-time saving of over \$14 million and an annual saving of over \$700,000 can be achieved by using the space for a new logistical storage facility.

If DOD can better use the space and if such use will result in saving more than that which would be realized by storing household goods, GAO supports the alternative use.

At an appropriate future time, we will review the operation and effectiveness of the proposed logistical facility.

LCD-76-241

OAKLAND ARMY TERMINAL

DOD took exception to our handling of four elements of cost: (1) storage in transit, (2) packing and draying, (3) opportunity cost, and (4) self-insured liability.

Storage in transit

DOD said that storage-in-transit (SIT) costs would be incurred under a Government or commercial storage operation and should be included as a cost under each alternative or excluded entirely. DOD thought we included SIT cost only for the commercial storage alternatives.

On the contrary, our estimate of the cost of using Government storage included provision for SIT in Government-operated space, based on the weight of household goods in commercial SIT. So SIT costs were included under both alternatives.

Because of the high cost of commercial SIT and because it is levied on the basis of 30-day increments, it is an expensive form of storage. We estimated that the annual SIT cost is \$4.19 a hundredweight under the Government operation compared to \$33.20 a hundredweight under the the commercial alternative. Our estimate included a factor to cover the cost of additional personnel and space required to handle SIT shipments at Oakland Army Terminal, California. Indirect expense estimates were also increased proportionately.

In summary, SIT costs were included in our computation under both alternatives. Therefore, exclusion of the SIT costs from commercial contract costs in the Military Traffic Management Command (MTMC) comparison was not appropriate.

Packing and draying

DOD believes that additional packing and draying cost would be incurred by converting to a Government storage operation. However, in our opinion packing and draying costs would be the same regardless of whether storage is in Government or commercial facilities. The same services are required under either storage alternative.

Our report considered using services for nontemporary storage in Government warehouses identical to that now furnished in contractor warehouses. The major difference would be the physical location and ownership of the warehouses.

The \$12.94 pack and crate rate cited by DOD is for a different type of service than required for preparing shipments for nontemporary storage. For example, the rate considers packing, crating, and preparing military shipments for overseas transportation and stuffing the goods in heavy, type II transportation containers. In contrast, the only packing required for storage would be for protection as required for local drayages.

The type of container used by contractors for nontemporary storage is entirely different from the type II container used for overseas shipment. Use of type II containers for nontemporary storage would be inefficient and uneconomical.

Our report included the costs of storage containers of the type used by contractors as a separate item. (See note j, enc. I of our report.) Therefore, the inclusion of container costs as discussed by MTMC is not appropriate.

In addition, DOD was concerned that commercial contractors might raise packing and drayage rates to compensate for the loss of revenue from long-term storage. At the same time, however, it recognized the potential for lower rates which could result from larger volume contracts.

Opportunity costs

DOD believes that \$367,000 in opportunity costs should be considered in the cost comparison because it represents the fair market rental value of the warehouses under consideration.

The Army criterion (AR 235.5) for including an opportunity cost in comparing the costs of Government or contractor facilities is based on the premise that

"if reliance upon a commercial source will cause Government-owned equipment or facilities to become available for other Federal use or for disposal as surplus, the cost comparison analysis should include as a cost in the first year of operation of the Government activity an appropriate amount based upon the estimated current market value of such equipment or facilities. This amount represents an opportunity cost, which is the money the Government would lose by continuing this activity with its existing equipment and facilities."

This criterion is consistent with the provisions of OMB Circular No. A-76 which prescribes policies for acquiring commercial products and services. In other words, the criterion considers that there is or will be an imminent alternative use. This now appears to be the case at Kelly where the opportunity cost of the alternative use as a logistics facility makes the warehouses less attractive for storage of household goods.

At the time of our review, the continued use of contractor warehouses had not made the warehouses at Oakland Army Terminal usable for other Government purposes. The warehouses at the terminal continue to be unused and have been unused for 3 consecutive years.

We concluded that the use of contractor warehousing had not enabled the Government to use space at Oakland Army Terminal and therefore opportunity costs were appropriately excluded from our computations.

Such a conclusion is consistent with the generally accepted cost accounting principle that opportunity cost is the measurable advantage forgone as a result of the alternative uses of resources. In the case of the Oakland Army Terminal, since the space remained unused for such a continuous and lengthy period, there was no measurable advantage forgone. Our analysis does include a small factor for opportunity cost, because at the time of our review there appeared to be a reasonably firm arrangement for use of part of the space. That arrangement was never consummated.

In your letter, you said that the proposed buildings at Oakland are considered prime real estate, for which a modest fair market rental value would be \$367,000--the opportunity cost. Such a conclusion considers (1) that the property is being offered to the public or other Government agencies for rental and (2) in view of its asserted prime nature and the modest rental, the property will shortly be leased to a lessor.

At the time of our study, no such possibilities existed, and Oakland Port Authority officials, a potential user of the port at that time, advised us they were primarily interested in the pier capacity and not use of the buildings exclusive of the pier facilities.

As of September 1976, MTMC authorities advised us that the buildings had not been advertised for lease.

Unless the buildings are made available for leasing and are later leased within a reasonable period of time or there is some other imminent use of the buildings, we recommend you recompute the cost comparison for Oakland, excluding opportunity costs. We also recommend that the "imminent alternative use" principle of opportunity costs be applied to similar installations you study.

Self-insured liability

Although the subject of self-insured liability is one of the four major issues raised by DOD, it has little impact on comparative cost analysis. The difference between DOD and our estimates for this element is only \$9,400 and accordingly would not influence any decision on whether or not to use Government or commercial facilities.

However, the following points respond to the questions raised by DOD.

1. We are not suggesting that all the household goods in the bay area could be placed in one warehouse but rather that the two warehouses would be required.
2. The fire systems installed in the Government warehouses in question were built to meet higher standards than similar systems installed in commercial warehouses.
3. The warehouses at Oakland Army Terminal have a supervised fire alarm system (commercial warehouse systems generally do not). Also, the area where facilities are located is monitored 24 hours a day by TV cameras and roving guards.
4. The warehouses at Oakland Army Terminal, although they are large, are divided into six separate bays separated by concrete firewalls. It is unlikely that a single fire would destroy all household goods in the bay area.

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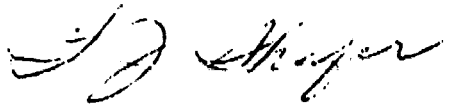
We recommend that you reevaluate your conclusions concerning nonuse of the Oakland Army Terminal for storage of household goods in light of the matters discussed in this letter.

We would appreciate being informed of the results of the study you are initiating to identify the potential saving

from the use of other available warehousing capacity for the storage of household goods.

We are sending copies of this report to the Director, Office of Management and Budget, and to the congressional committees designated under the Legislative Reorganization Act of 1970 to receive copies of DOD's response to our recommendation:

Sincerely yours,

A handwritten signature in cursive script, appearing to read "F. J. Shafer".

F. J. Shafer
Director