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In March 1970, the Department of Defense (DOD) announced a 5-year program to generally phase out the use of in-place Government-owned facilities in the possession of contractors. Although progress has been made, more could be done to phase out this equipment through determined and sustained efforts by LUD and the military services. Findings/Conclusions: Uncertainties about the authority to dispose of Government equipment by negotiated sale to contractors and past lack of incentives for contractors to invest in capital equipment have detracted from the phaseout program's success. As of June 30, 1976, contractors at Government-owned and contractor-operated plants had 12% less Government-owned industrial and other plant equipment than the \$4.5 billion in their possession 5 years earlier. Recommendations: The Secretary of Defense should: obtain visibility of other plant equipment furnished to contractors by maintaining central records on such equipment; put more emphasis on identifying both industrial and other plant equipment essential to supporting either current procurements or wartime production and emphasize removing unneeded equipment; revise DOD procedures to guarantee that all plant equipment needed during wartime is identified and included in plant equipment packages set up to meet wartime requirements; and reassess DOD's position on authorizing the use of Government-owned equipment for commercial work and require that the contractor maintain records for use of Government-owned equipment on commercial work. The Congress should clarify the authority of the General Services Administration to negotiate sales of Government-owned equipment to the holding contractors. (Author/SC)

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REPORT OF THE COMPTROLLER GENERAL OF THE UNITED STATES

Challenges To Reducing Government Equipment In Contractors' Plants

Department of Defense

In March 1970, the Department of Defense announced a 5-year program to generally phase out the use of in-place Government-owned facilities in the possession of contractors.

This report describes the Department's effort to reduce the amount of equipment at contractor-owned plants and the problems involved in removing the equipment.

While some progress has been made, total phaseout cannot be achieved under current policies and procedures.

SEPTEMBER 15, 1977



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

B-140389

The Honorable Jack Brooks
Chairman, Legislation and National
Security Subcommittee
Committee on Government Operations
House of Representatives

Dear Mr. Chairman:

Your letter of December 31, 1975, asked us to review the Defense Department's progress in reducing the amount of Government-owned plant equipment in the possession of contractors. As requested, we (1) determined the extent that the Defense Department was pursuing a phaseout policy, (2) updated our previous findings on the Defense Department's requirements for contractors' utilization records, (3) determined whether plant equipment packages contain only the property needed for an approved preparedness plan, and (4) determined whether plant equipment package property is moth-balled or remains in use by contractors.

You also asked about the operations of the Defense Industrial Plant Equipment Center in Memphis, Tennessee. Our October 5, 1976, report to the Congress on improving the management of industrial plant equipment at Government-owned and operated facilities, a copy of which we sent to you, contains this information.

As directed by your office, we have not presented this report to the Department of Defense or the contractors for official comment. However, we discussed the results with agency officials and considered their comments in preparing this report.

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of the report. At that time we will send copies to interested parties and make copies available to others upon request.

Sincerely yours,

A handwritten signature in black ink, appearing to read "James A. Stute".

Comptroller General
of the United States

D I G E S T

What gains has the Defense Department made toward its goal of generally requiring contractors to furnish all equipment needed to carry out Government contracts?

Progress has been made but more could be done to phase out this equipment through determined and sustained efforts by Defense and the military services.

Uncertainties about authority to dispose of Government equipment by negotiated sale to contractors and past lack of incentives for contractors to invest in capital equipment have detracted from the phaseout program's success.

To prepare for possible wartime production expansion, Defense must keep some Government-owned equipment at contractor plants. Under current procedures only the industrial plant equipment required for mobilization production is put in plant equipment packages. Improvements are needed to guarantee that all plant equipment required during wartime is specifically identified, justified, and included in plant equipment packages.

Defense's policy of authorizing rent-free use of Government equipment in supply contracts has delayed phaseout. Clarification is needed on the relationship between phaseout planning and rent-free use of equipment. Unless clarification is provided, equipment could be indefinitely kept at contractors' plants even though it is not needed for mobilization production.

Control over contractor use of Government-owned plant equipment needs to be strengthened.

Defense must be more aggressive in obtaining contractor compliance with regulations and must improve its administration of contracts to protect the Government's interests. An alternative would be to restrict the use of Government equipment to Government work. This would motivate some contractors who wanted to remain competitive to increase their investment in contractor-owned equipment and would help phase out Government-owned equipment. Some advantages of such a policy would be offset by contractor reluctance to keep idle or little-used Government equipment solely for mobilization.

REDUCTIONS IN EQUIPMENT

On June 30, 1976, contractors at Government-owned and contractor-owned plants had Government-owned industrial and other plant equipment that originally cost \$3.95 billion. This was 12 percent less than the \$4.5 billion in their possession 5 years earlier.

Industrial plant equipment

Industrial plant equipment is that plant equipment costing \$1,000 or more which is used for purposes such as cutting, grinding, and shaping. It includes items such as lathes, milling machines, and drills.

On June 30, 1976, contractors held Government-owned industrial plant equipment that originally cost \$1.6 billion. This was 20 percent less than the \$2 billion held 5 years earlier.

The Defense Industrial Plant Equipment Center (Memphis, Tennessee) maintains central records on all Defense industrial plant equipment. Center records showed that, of the \$1.6 billion held by contractors on June 30, 1976, about half (\$852 million) was at contractor plants. This was 31 percent less than the \$1.24 billion worth at their plants 5 years earlier.

Other plant equipment

Other plant equipment is that plant equipment, regardless of cost, which is not industrial plant equipment. It includes items such as machine tools costing less than \$1,000, furniture, and vehicles.

On June 30, 1976, contractors held Government-owned other equipment that originally cost \$2.32 billion. This was 5 percent less than the \$2.45 billion held 5 years earlier.

Defense does not maintain central records on other plant equipment items unlike industrial plant equipment. Contractors submit an annual report to Defense on Government-owned facilities held by them. However, the report does not separately identify the amounts at Government plants operated by contractors and at contractor plants. Consequently, GAO could not determine the overall progress in reducing other plant equipment at contractors' plants.

At the 10 contractor plants included in GAO's review, the acquisition cost of other plant equipment was reduced by 47 percent, from \$17.8 million on June 30, 1971, to \$9.4 million on June 30, 1976.

RECOMMENDATIONS

The Secretary of Defense should:

- Obtain visibility of other plant equipment furnished to contractors by maintaining central records on such equipment.
- Put more emphasis on identifying both industrial and other plant equipment essential to supporting either current procurements or wartime production and emphasize removing unneeded equipment.
- Revise Defense procedures to guarantee that all plant equipment (industrial and other) needed during wartime is identified and included in plant equipment packages set up to meet wartime requirements.

--Reassess Defense's position on authorizing the use of Government-owned equipment for commercial work and require that the contractor maintain use records to improve the contractor's accounting for use of Government-owned equipment on commercial work.

As the Committee directed, GAO did not request formal comments from the Department of Defense or the contractors but did discuss the observations, conclusions, and recommendations in this report with officials of that Department and the military services.

MATTERS FOR CONSIDERATION
BY THE COMMITTEE

GAO further recommends to the Congress that the authority of the General Services Administration to negotiate sales of Government-owned equipment to the holding contractors be clarified.

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ABBREVIATIONS

ASPR **Armed Services Procurement Regulation**

GAO **General Accounting Office**

GSA **General Services Administration**

CHAPTER 1

INTRODUCTION

Since 1967, we have issued several reports to the Congress and to the Secretary of Defense on improvements needed for controlling Government equipment held by contractors. In August 1972, 1/ we reported that, although the Department of Defense had made some progress toward its goal of having contractors furnish all equipment required for Government work, more emphasis was needed. We also identified ways to improve management of the Government-owned plant equipment remaining with contractors.

Government-owned plant equipment held by contractors is either furnished by the Government or purchased by contractors for Government account, in accordance with the Armed Services Procurement Regulation (ASPR), under facilities' contracts. Plant equipment includes such items as machine tools, test equipment, furniture, vehicles, and accessory and auxiliary items.

In September 1968 the Defense Department revised its criteria for furnishing Government-owned equipment to contractors. The revised policy states that, with certain exceptions, it is the Defense Department's policy to place maximum reliance on the use of privately owned facilities in the performance of Government contracts. Facilities may be provided

- for use in a Government-owned, contractor-operated plant;
- for mobilization production in accordance with a mobilization plan approved by the Assistant Secretary of Defense (Installations and Logistics);
- when Defense determines that it is necessary or in the public interest because the contractor is unwilling or unable to acquire the necessary facilities with its own resources, or cannot acquire the facilities soon enough to meet required delivery schedules; or

1/Further Improvements Needed in Controls Over Government-Owned Plant Equipment in Custody of Contractors (B-140389, Aug. 29, 1972).

--as components of special tooling or special test equipment acquired or fabricated at Government expense.

THE PHASEOUT PROGRAM

In March 1970, the Assistant Secretary of Defense (Installations and Logistics) issued a memorandum to the Assistant Secretaries (Installations and Logistics) of the Army, the Navy, and the Air Force and to the Director of the Defense Supply Agency ^{1/} concerning phaseout plans for Government-owned facilities in the possession of contractors.

This memorandum restated the revised Defense policy of relying on the use of privately owned facilities in performing Government contracts, and required contractors to submit plans to phase out the use of in-place Government-owned facilities over a period generally not to exceed 5 years. Nonprofit contractors and wholly Government-owned, contractor-operated plants which do not compete with commercial firms were exempted.

Subsequently, in February 1971 the Deputy Secretary of Defense issued a memorandum stating that Defense was evaluating the impact of the phaseout policy on the mobilization base and providing for deferring phaseout plans where mobilization base requirements were being developed and where phaseout would be contrary to the interests of the Government or work an economic hardship on a company. His memorandum delegated to the Secretaries of the military services the authority to approve the exemptions and deferrals which formerly had to be approved by the Secretary of Defense. The phaseout program further emphasized the basic policy of placing maximum reliance on the use of privately owned facilities in the performance of Government contracts.

Our review was performed at the request of the Chairman, Legislation and National Security Subcommittee, House Government Operations Committee. (See app. VI.) As requested, we put emphasis on determining the extent that the Defense Department is pursuing a phaseout policy and whether controls over contractor use of Government-owned equipment have improved since our 1972 report.

^{1/}Now called the Defense Logistics Agency.

CHAPTER 2

GOVERNMENT-OWNED PLANT EQUIPMENT

AT CONTRACTOR PLANTS--CAN IT BE PHASED OUT?

On June 30, 1976, contractors had \$852 million worth of Government-owned industrial plant equipment at their plants. This was 31 percent less than the \$1,243 million worth in their plants 5 years earlier.

Similar data was not readily available for other plant equipment because such equipment is not centrally recorded, and it was not possible, in terms of the time and effort required, for us to develop comparable information.

While some progress has been made to reduce the amount of Government-owned plant equipment at contractor plants, under current policies and procedures total phaseout cannot be achieved.

Government-owned plant equipment is at contractors' plants to meet both peacetime and mobilization production requirements. Supply contracts were negotiated on the basis that the contractors could use this equipment under Government contracts. As a result, the equipment cannot be withdrawn from the contractors' plants without renegotiating the contracts. In some cases, new contracts were awarded before completion of the original contract. This extended the time that equipment was available to contractors.

About 27 percent (\$228 million worth) of the industrial plant equipment at contractors' plants on June 30, 1976, was there to meet mobilization production requirements and has been exempted from the phaseout program.

The Army has a program for modernizing and expanding the ammunition production facilities required to meet mobilization requirements. The program includes modernizing the facilities at those contractor plants which would be required to produce ammunition during a war to meet U.S. requirements. Obviously, it is not feasible to phase out the in-place Government-owned facilities at these contractor plants, and it will become even more unlikely after the facilities have been modernized.

**IMPLEMENTATION OF THE
PHASEOUT PROGRAM**

Although the Defense Department first announced the phaseout policy in March 1970, as of July 1977 the policy had not been incorporated into formal Defense instructions or directives on managing industrial facilities. The instructions on phaseout from the Defense Department to the military services were promulgated through various memoranda. In July 1977, a Defense official said that a revision to a Defense Department directive was being written to include Defense policies on the phaseout program, incentives for private investment, plant equipment packages, and the general reserve. He estimated that the directive would be available for the military services' comments during September 1977.

**EQUIPMENT REDUCTIONS AT
CONTRACTOR-OWNED PLANTS**

The Defense Industrial Plant Equipment Center, Memphis, Tennessee, maintains central records of the Defense Department's industrial plant equipment, including equipment at contractor plants. Industrial plant equipment is that part of plant equipment with an acquisition cost of \$1,000 or more which is used for purposes such as cutting, grinding, and shaping, and includes items such as lathes, milling machines, and drills. According to the Defense Industrial Plant Equipment Center records, reductions of industrial plant equipment at contractor-owned plants were as follows:

<u>Military services</u>	<u>Acquisition cost of industrial plant equipment at contractors' plants</u>			
	<u>6/30/71</u>	<u>6/30/76</u>	<u>Decrease</u>	
			<u>Amount</u>	<u>Percent</u>
	----- (millions) -----			
Army	\$ 324	\$214	\$110	34
Navy	197	136	61	31
Air Force	708	490	218	31
Others	<u>14</u>	<u>12</u>	<u>2</u>	14
Total	<u>\$1,243</u>	<u>\$852</u>	<u>\$391</u>	31

Similar data was not available for other plant equipment at contractor-owned plants because, unlike industrial plant equipment, it is not centrally recorded. Other plant equipment is that which is not industrial plant equipment, regardless of cost. It includes items such as machine tools costing less than \$1,000, furniture, and vehicles.

In accordance with section B-311 of the Armed Services Procurement Regulation, contractors submit an annual report to Defense on Government-owned facilities in their possession. The annual report includes the acquisition cost of Government-owned other plant equipment held by contractors, but does not separately identify the amounts at Government plants and at contractor plants, and it was not feasible to determine the amounts. As a result, we could not determine overall progress in reducing other plant equipment at contractor plants.

A May 1976 Defense audit report cited the following problem with controlling other plant equipment:

"Financial reports submitted by DOD [Department of Defense] property administration at June 30, 1975, showed OPE [other plant equipment] assets in the possession of Government contractors totaled about \$1.828 billion. [1] DOD policy did not require asset reporting by the contractors for this OPE."

* * * * *

"We believe consideration should be given to obtaining some form of asset visibility over OPE assets in the hands of contractors. While we do not advocate the intensified management applied to IPE [industrial plant equipment] items or their inclusion in the DOD general reserve inventory, we believe improved reutilization of excess OPE assets and the prevention of unnecessary procurements makes some form of control worthwhile."

1/The financial report cited was the Defense Department's summary of the reports submitted by the various contractors. The reported amount includes other plant equipment in the possession of contractors at both Government and contractor plants. It excludes \$542 million in other plant equipment at early warning defense system sites.

Defense is studying various ways to improve the management of plant equipment, including the feasibility of increased visibility of other plant equipment held by contractors. Defense officials said that they expect to complete the visibility study by September 1977.

RETENTION OF EQUIPMENT FOR INDUSTRIAL
MOBILIZATION PRODUCTION PLANNING

The Defense Department is responsible for mobilization planning to see that sufficient industrial capacity exists to meet potential wartime needs for Defense equipment. The Defense Department relies heavily on contractors' production capacity to meet wartime equipment needs. In some cases the Government supplements the contractor's plant equipment to assure that sufficient industrial capacity exists.

Retention of equipment for planned mobilization requirements limits the reductions possible under the phaseout program. Of the \$852 million of Government-owned industrial plant equipment at contractors' plants on June 30, 1976, about \$228 million worth (27 percent) was in plant equipment packages exempted from phaseout. In addition, phaseout plans were deferred for industrial plant equipment costing \$6.2 million (about 7 percent of the total) because of possible mobilization requirements.

The following table shows the amount of industrial plant equipment at contractor-owned plants and the equipment status at June 30, 1976:

	Cost of industrial plant equipment at contractor-owned plants	Cost of equipment on line and available for use	Cost of equipment in plant equipment packages
(millions)			
Army	\$214	\$117	a/\$ 97 (\$44)
Navy	136	97	39 (7)
Air Force	490	398	92 (82)
Others	<u>12</u>	<u>12</u>	<u> </u> <u> </u>
Total	<u>\$852</u>	<u>\$624</u>	<u>\$228</u> (<u>\$133</u>)

a/The amount in parenthesis is the total equipment in plant equipment packages in use at the contractors' plants.

The above data shows that \$97 million (45 percent) of the industrial plant equipment furnished to Army contractors is in plant equipment packages and therefore exempted from phase-out. About 29 and 19 percent, respectively, of such equipment provided under Navy and Air Force contracts are in plant equipment packages. About \$133 million (58 percent) of the total industrial plant equipment retained in packages for mobilization is used for current production. This is consistent with the Defense Industrial Reserve Act of 1973 definition of a plant equipment package being a complement of active and idle equipment held to produce defense items in an emergency.

Since June 30, 1971:

- The total cost of industrial plant equipment in contractors' plants decreased by about \$391 million.
- The cost of equipment not in packages decreased \$429 million, or about 41 percent.
- The cost of inactive equipment in packages decreased \$58 million, or about 38 percent.
- The cost of active equipment in packages increased \$96 million, or about 259 percent.

Most of the increase in active industrial plant equipment in plant equipment packages was caused by the Air Force (\$82 million). This increase resulted from (1) a change in Defense Department policy allowing active equipment to be included in plant equipment packages, and (2) a change in Air Force philosophy on its need to retain an industrial preparedness production capacity. Before these changes the equipment was only identified as active items supporting current procurements.

Appendixes III, IV, and V contain detailed comparisons of the net changes in the amounts of Government-owned industrial plant equipment held by contractors between June 30, 1971, and June 30, 1976. Separate comparisons--which identify the amounts in plant equipment packages and the equipment's status--are provided for (1) all industrial plant equipment held by contractors (app. III), (2) industrial plant equipment at Government-owned plants operated by contractors (app. IV), and (3) industrial plant equipment at contractor plants (app. V). Defense's records do not readily provide information about annual acquisitions and disposals. Acquisitions shown on page 11 were reconstructed from records at the Defense Industrial Plant Equipment Center at Memphis.

MODERNIZATION OF THE AMMUNITION PRODUCTION BASE

Early in 1970 the Army developed plans to modernize its portion of the ammunition production base, through 1981 at an estimated cost of \$3.9 billion. The March 1977 long-range plan for modernizing the ammunition production base through 1997 is \$9.4 billion. About \$1.5 billion of this is for equipment to be furnished to contractors at contractor and Government-owned plants.

Within the last 5 years, we have reviewed the Army's annual appropriation requests for ammunition plant modernization and expansion. Although we have recommended reductions for some projects and deferral of others, generally we found that the modernization of ammunition-producing facilities is warranted and necessary.

PHASEOUT THROUGH NEGOTIATED SALES TO CONTRACTORS

The Defense policy is to minimize its ownership of industrial facilities to the extent practicable and still provide assurances that facilities are available to produce essential

defense items. The Air Force has had the General Services Administration (GSA) negotiate the sale of plant equipment to contractors holding the equipment at their plants. The equipment is not considered excess to the needs of the Air Force because the equipment is required by the contractors to produce defense items. However, as long as the operating contractor agrees to purchase the equipment and maintain the capability to produce the defense item, the Air Force considers the equipment "excess to Government ownership." If the holding contractor decides not to buy the equipment or the sale is not approved for some other reason, the Air Force would withdraw the sale offer.

The Army and Navy have not done this as often because the Defense General Counsel expressed an opinion in November 1970, and reiterated it in July 1975, that there is no existing disposal authority adequate to support a Defense program which seeks to dispose of nonexcess Government-owned industrial equipment on a negotiated basis to contractors in possession of such property at their plants.

GSA, however, believes it has authority to sell such equipment under the Federal Property and Administrative Services Act of 1949, as amended (40 U.S.C. 484(e)(3)(G)), and believes it is not necessary to publicly advertise for bids. Subsection (e)(3) contains exceptions to the provision of the act which states that all disposals shall be made after publicly advertising for bids. Subsection (e)(3)(G) provides the following exception:

"With respect to real property only, the character or condition of the property or unusual circumstances make it impractical to advertise publicly for competitive bids and the fair market value of the property and other satisfactory terms of disposal can be obtained by negotiation."

Removal of Government-owned equipment would diminish the production capabilities of the facility. GSA claims that such equipment is considered as an integral part of the real property within the meaning of the subsection of the act. Because the contractor has contractual authority to use the equipment for defense contracts, it would be impractical to interrupt production schedules by disposing of such equipment through normal disposition procedures.

GSA considers each proposed sale individually and negotiates sales only when the agency believes the sale is within its authority. Independent appraisals to determine the fair

market value of the equipment are made, and a selling price approximating that value is negotiated with the contractors. When GSA determines that it does not have sales authority for an individual case, the equipment is returned to the Defense Department.

Since the Defense General Counsel reiterated his opinion in July 1975, the Department has been trying to resolve the matter. During the interim Defense allowed the services to submit requests for negotiated sales directly to GSA, which is responsible for administering the Federal Property and Administrative Services Act of 1949 and its disposal authority. However, the Army and Navy are waiting for the matter to be resolved and have not recently asked GSA to negotiate sales for them. As a result, Army and Navy contractors who wish to purchase Government-owned equipment in their possession are not permitted to do so.

Legislation to permit direct selling of nonexcess personal property to holding contractors through negotiation has been introduced in the Congress on several occasions. We have supported such legislation on the basis that it would facilitate Defense's efforts to phase out ownership at contractors' plants.

The Commission on Government Procurement has recognized that Defense's efforts to divest itself of equipment have been hampered by the lack of clear authority to negotiate sale with the using contractor of equipment which is excess to "Government ownership" but not to "Government requirements" and has recommended that legislation be enacted to authorize such sales. The sales agreement should provide adequate protection to the Government for its future needs of the equipment when competition is not considered feasible.

ACQUISITION OF ADDITIONAL EQUIPMENT

Sometimes the Defense Department must furnish Government-owned equipment to contractors. Defense policy provides for furnishing equipment to contractors in limited circumstances, such as for use in Government-owned plants operated by contractors or for production of items in accordance with approved mobilization plans.

Defense Department records show that new industrial plant equipment acquired for both Government-owned and contractor-owned plants for calendar years 1971 through 1975 was as follows:

<u>Calendar year</u>	<u>New acquisitions of industrial plant equipment</u> (millions)
1971	\$11.0
1972	11.6
1973	16.7
1974	20.9
1975	<u>34.6</u>
Total	<u>\$94.8</u>

Contractors may also receive equipment from Defense inventories when contracts are negotiated on that basis. Idle equipment may be relocated from other contractors' plants, from Government-owned plants, or from Defense storage sites. Defense Industrial Plant Equipment Center records show that the following amounts of industrial plant equipment were redistributed to contractor plants for fiscal years 1971 through 1976:

<u>Fiscal year</u>	<u>Acquisition cost of industrial plant equipment redistributed</u> (millions)
1971	\$ 27.7
1972	23.6
1973	18.0
1974	12.9
1975	26.9
1976	<u>18.8</u>
Total	<u>\$127.9</u>

A Center official said that the increase in 1975 was in equipment required for plant equipment packages established for some contractors with preparedness production planning commitments.

SPECIAL MANAGEMENT ACTIONS
WHICH WILL AFFECT PHASEOUT

In December 1975 the Assistant Secretary of Defense (Installations and Logistics) directed the military services and the Defense Logistics Agency to:

- Identify essential industry sectors and determine which sectors are most dependent upon Government-owned facilities.
- Identify sectors of industry that may require Government instead of private ownership.
- Identify those items to be removed from Government inventory, the methods of disposal, and disposal schedules.
- Modernize and make more productive the essential core of plant equipment for continued Government ownership.
- Review equipment in plant equipment packages and the general reserve 1/ to remove nonessential items, discontinue nonessential packages, and develop a plan to improve the productivity of essential items.

These projects, intended to strengthen the defense industrial base, will affect the announced phaseout policy. The projects will decrease the amount of plant equipment at some contractor locations and increase the amount at others.

There has been a lack of incentives for contractors to invest in privately owned facilities for use on Government contracts. During 1976, Defense offered new incentives to contractors to encourage private investment: (1) considering some interest expense on capital investments as an allowable cost for negotiated contracts, (2) recognizing the level of the contractor facility investment in establishing a prenegotiation profit objective for contracts, and (3) providing, in certain cases, for Government purchase of the contractor's equipment if the program for which the contractor's investment was made is partially or wholly terminated.

The first two incentives resulted from a Defense study called "Profit '76." The Army, the Navy, the Air Force, the Defense Logistics Agency, and private industry participated in the study. Defense Procurement Circular Number 76-3, issued September 1, 1976, was a result of the study. The circular states that one reason why contractors have not

1/The general reserve consists of idle industrial plant equipment that is being maintained by the Defense Industrial Plant Equipment Center for peacetime and mobilization requirements.

invested in modern machinery and equipment for use on Defense contracts was that the procurement policy did not adequately recognize the facility investment either in profit or as an allowable cost.

The third incentive, called "special termination-Government buy-back of capital equipment," was announced in May 1976 by the Deputy Secretary of Defense as a technique to encourage contractors to invest in cost-reducing capital assets.

This technique was to reduce the contractor's economic risk from program instability by allowing the contractor to sell capital investments to the Government when a risky program is partially or wholly terminated. Requirements for use of this technique include

- a determination by the Contracting Officer that the Government would save money if the contractor made specific investments in cost-reducing equipment and that the contractor would not make the investments without use of the technique,
- the risk of termination was recognized before the contractor reached its break-even point on the investment, and
- the contractor would not make the investment for other than the weapon system involved.

CONCLUSIONS

A phaseout of all Government equipment in contractors' possession was never intended and would be impractical. The term "phaseout" is misleading and may have caused some confusion and resistance to the program.

Although progress has been made in reducing the amount of Government-owned plant equipment at contractor plants, we believe that more could have been accomplished with more determined and sustained efforts by the Defense Department and the military services to implement the phaseout program.

Uncertainties about the authority to dispose of Government equipment by negotiated sale to contractors, and past lack of incentives for contractors to invest in capital equipment have also detracted from the program's success.

**RECOMMENDATIONS TO THE
SECRETARY OF DEFENSE**

We recommend that the Secretary of Defense put more emphasis on identifying equipment essential to support either current procurements or wartime production and emphasize removing unneeded equipment.

We also recommend that Defense obtain visibility of other plant equipment furnished to contractors by maintaining central records on such equipment.

**MATTERS FOR CONSIDERATION
BY THE COMMITTEE**

We further recommend to the Congress that the authority of GSA to negotiate sales of Government-owned equipment to holding contractors be clarified.

CHAPTER 3

IMPLEMENTATION OF THE PHASEOUT

PROGRAM AT 10 CONTRACTOR PLANTS

To assess the military services' efforts to reduce the amount of Government-owned plant equipment at contractors' plants and the problems involved in removing the equipment, we obtained information from 10 contractors, each holding over \$1 million worth of Government-owned plant equipment.

As shown below, these 10 contractors had \$72.4 million in Government-owned industrial and other plant equipment on June 30, 1976, compared to \$92.8 million 5 years ago--a 22-percent decrease.

<u>Military service</u>	<u>Cost of industrial and other plant equipment</u>		<u>Differ- ence</u>	<u>Percentage change</u>
	<u>June 30, 1971</u>	<u>June 30, 1976</u>		
	----- (millions) -----			
Army (note a)	\$23.7	\$26.6	\$ 2.9	12
Navy	16.8	12.5	-4.3	-26
Air Force	<u>52.3</u>	<u>33.3</u>	<u>-19.0</u>	-36
Total	<u>\$92.8</u>	<u>\$72.4</u>	<u>-\$20.4</u>	-22

a/The amount shown for June 30, 1971, includes \$3.9 million for one company which was formed in December 1973. The amount for this company was for June 30, 1974, rather than June 30, 1971.

At the 10 contractor plants, the amount of industrial plant equipment decreased by 16 percent (from \$75 million to \$63 million) and the amount of other plant equipment decreased by 47 percent (from \$17.8 million to \$9.4 million).

As discussed in chapter 2, the Army has an ongoing program for modernizing the ammunition production base and this is creating increases in plant equipment at some contractor plants. This is the primary reason why there was an increase in Army equipment.

During this 5-year period

--the amount of Government-owned plant equipment decreased for 7 of the 10 contractors,

--\$7.3 million worth of additional plant equipment was furnished to the 10 contractors, and

--\$5.3 million was spent to rehabilitate plant equipment at seven contractor plants.

The following table shows the status of plant equipment at 10 contractor plants on June 30, 1976.

<u>Category</u>	<u>Cost of plant equipment</u> (millions)
Industrial plant equipment retained in packages for mobilization production	\$27.6
Industrial plant equipment not in a package but certified as required for mobilization production	4.7
Other plant equipment at plants having packages	7.7
Industrial plant equipment not required for mobilization production	13.9
Industrial and other plant equipment retained for anticipated production contract	<u>a/9.6</u> (8.1)
Industrial and other plant equipment in negotiations to sell	<u>a/8.9</u> (8.8)
Total	<u>\$72.4</u>

a/The part which is industrial plant equipment is shown in parenthesis.

Appendixes I and II show changes in plant equipment over the 5-year period and the amount of equipment in plant equipment packages.

MOBILIZATION PRODUCTION

As discussed in chapter 2, equipment required for mobilization production is exempted from the phaseout program. Of \$72.4 million in plant equipment at the 10 contractor plants, \$40 million (55 percent) may be required for mobilization production requirements (the first three categories in the table on p. 16). This equipment was being retained by seven contractors.

There is \$27.6 million of industrial plant equipment in packages specifically identified as required for mobilization production and therefore exempted from the phaseout program. These planned producers have other plant equipment with an original acquisition cost of \$7.7 million, some or all of which may also be required for mobilization production. We could not determine what portion of the \$7.7 million was required, because neither the contractor nor Defense records identify the other plant equipment required for mobilization production. Other equipment required for mobilization production is also exempted from phaseout.

Douglas Aircraft Company had 17 industrial plant equipment items costing \$4.7 million, which the Navy exempted from phaseout in 1971 for mobilization requirements. This equipment is being used to produce a military aircraft. Although the equipment is not in a plant equipment package, Navy representatives stated in February 1977 that the equipment was required for mobilization production and was exempted from phaseout. The Navy representatives said that a plant equipment package will probably be established for this equipment at the end of the current production program.

Determining the need for plant equipment packages

The Assistant Secretary of Defense (Installations and Logistics) initially approves and annually recertifies the requirement for each plant equipment package. A Defense official said that packages are approved essentially as recommended by the military services because their office does not have the staff and resources to review them extensively.

To establish or continue a package, the military services must determine that the following criteria are met:

- The package provides production capacity for critical mobilization needs of the sponsoring service.
- Available sources will not be able to produce the specific military items in question.
- The need for such capacity has been established in accordance with the policies set forth in the Department of Defense Industrial Preparedness Planning directive (Department of Defense Directive 4005.1).

These criteria emphasize the justification for the package as a whole, and the production end item for which it is required. Although a package may be required, little emphasis is put on making a critical review of the equipment in the packages to verify that the specific types and quantities included are essential and justified.

A May 1976 Defense audit report stated that the recertification process did not require the submission of information on the assigned planned producers, the status of equipment included in the packages, or the status and availability of the necessary special tooling and test equipment required for production of the end item. The report recommended that Defense policies and procedures be reviewed and strengthened to provide better management control over the recertification of plant equipment packages.

Military service representatives said that plant equipment packages do not always contain all the industrial plant equipment required for mobilization production. They said that equipment being used for current supply contracts which is not included in a package may also be required for mobilization production.

Although industrial plant equipment has been identified as required for mobilization production and plant equipment packages have been established to assure that the equipment will be available during a mobilization, the condition of the equipment may prevent or delay its use during a mobilization.

For example, in 1975 the Army reviewed the actual condition of some industrial plant equipment assigned to plant equipment packages. The Army study concluded that the condition was not reliable and most equipment shown as acceptable for use was actually unacceptable. The Army's sample showed that about 76 percent of the Army equipment in packages was coded "useable, without repair"

but, in fact, only 29 percent was useable for mobilization planning without repair.

The Army currently has a program for modernizing the manufacturing facilities for Army tank cartridge cases at one contractor plant included in our review. The facilities are being modernized to assure that the capacity exists to meet mobilization requirements. The Department of Defense Appropriation Act of 1976 (Public Law 94-212, Feb. 9, 1976) included funds for the first of a three-phase effort to modernize the facilities. The Army's March 1977 long-range plan for the modernization program shows a total estimated cost at this plant of \$43.7 million, of which \$12.2 million was planned for the first phase and most of this amount (\$10.9 million) is intended for the purchase and installation of new industrial plant equipment.

In May 1977 we issued a report to the Congress on shortfalls in planning with private industry for national emergency mobilization production requirements (PSAD-77-108, May 13, 1977). The report points out that present Defense mobilization planning with private industry does little to strengthen our industrial capacity to meet emergencies. Planning data often lacks adequate analysis and little is done by the military services to correct problems when such analysis is performed. We also reported that planned producers frequently assume that Government-owned plant equipment packages not used in current production are complete and in good working condition. However, some planned producers stated that they had not inspected such equipment packages and others had inspected the equipment but found it badly outdated, and in some instances, incomplete.

In commenting on the report, Defense generally agreed with our findings and said it was devoting increased management attention to improving the effectiveness of the industrial preparedness planning program. Defense established a steering group to review all aspects of the program, including policy and planning.

EFFORTS TO PHASE OUT
EQUIPMENT NOT IDENTIFIED FOR
MOBILIZATION PRODUCTION

Contractors with plant equipment packages for mobilization production have \$13.9 million of industrial plant equipment which is not part of the packages. This represents 19 percent of the total industrial and other plant equipment

held by the 10 contractors on June 30, 1976. Little progress is being made by the military services to phase out this equipment.

Army

Three of the 10 contractors reviewed have Army plant equipment packages for producing munitions during a mobilization. As shown below, 450 of 1,089 Army industrial plant equipment items, or 41 percent, are not part of the plant equipment packages.

<u>Contractor</u>	<u>Number of industrial plant equipment items</u>		
	<u>In packages</u>	<u>Not in packages</u>	<u>Total</u>
Norris Industries	201	109	310
Northrop Corporation	243	292	535
Silent Industries, Inc.	<u>195</u>	<u>49</u>	<u>244</u>
Total	<u>639</u>	<u>450</u>	<u>1,089</u>

The acquisition cost of this Army industrial plant equipment was \$8.9 million. Although not specifically exempted or deferred, the Army has not required the contractors to submit phaseout plans for this equipment and continues to authorize rent-free use of this equipment on Government contracts. For example, an Army command which controls the Army plant equipment at Northrop Corporation (Electro-Mechanical Division) awarded a \$2.4 million contract in May 1976 authorizing rent-free use of \$4.1 million in plant equipment not in a plant equipment package. The contract has an expected completion date beyond July 1979. Therefore, the equipment cannot be phased out before completion of this and other contracts authorizing its use without an equitable adjustment to the contractor.

Army officials said that the plant equipment packages may not contain all plant equipment required for mobilization production. They said that equipment used for current production, which is not in packages, may also be required for mobilization production. The Army does not determine whether the equipment should be put in a mobilization package until current production decreases, causing the potential removal of equipment from the contractor's plant. Therefore, the Army has not required contractors with plant equipment packages to submit phaseout plans for equipment not in a package.

In addition, in May 1975 the Army awarded a \$3.5 million contract to an engineering company to assist in developing a package modernization plan. The three Army contractors reviewed were among the contractors studied by the engineering company. The contract requires an evaluation of the mobilization production base to determine the technical capability and the economic justification for each plant equipment package and to prepare a plan for modernizing the package as necessary.

Navy

Two contractors have Navy plant equipment packages. As shown below, most of their Government-owned industrial plant equipment was in plant equipment packages and therefore exempted from the phaseout program.

<u>Contractor</u>	<u>Number of Navy industrial plant equipment items</u>		
	<u>In packages</u>	<u>Not in packages</u>	<u>Total</u>
Singer Company	62	7	69
Norris Industries	<u>117</u>	<u>0</u>	<u>117</u>
Total	<u>179</u>	<u>7</u>	<u>186</u>

The acquisition cost of the seven Navy industrial plant equipment items not in a package was \$84,000. Although this equipment is not in an exempted or deferred category, the Navy has not required the contractor to submit a phaseout plan for this equipment.

Navy officials said that at contractor plants, the industrial plant equipment not in a package is not being phased out because the equipment is being used on current contracts. When production declines, the equipment could be set aside for mobilization production.

Air Force

Two contractors reviewed have Air Force plant equipment packages. As shown below, over 70 percent of the industrial plant equipment items at these two plants are not part of the Air Force plant equipment packages required for mobilization production.

<u>Contractor</u>	<u>Number of industrial plant equipment items</u>		<u>Total</u>
	<u>In packages</u>	<u>Not in packages</u>	
Hughes Aircraft Company	198	714	912
Menasco Manufacturing Company	<u>84</u>	<u>11</u>	<u>95</u>
Total	<u>282</u>	<u>725</u>	<u>1,007</u>

As of July 1976, neither contractor had a phaseout plan for the 725 pieces not in plant equipment packages.

Hughes Aircraft Company

In December 1975 Hughes Aircraft Company stated that it could not meet mobilization production requirements for two of four programs the plant equipment package was intended to support without additional Government facilities. The contractor indicated that the Government should fund a study to determine the additional facilities needed for mobilization production requirements. In September 1976 the plant equipment package was recertified. Eight items were added and 13 items were deleted.

At the time of our review the contractor planned to replace \$3.2 million of Air Force plant equipment not in the mobilization package by March 1978, and to retain \$3.5 million of Air Force plant equipment until at least 1981. The contractor planned to retain equipment until 1981 because he has been granted rent-free use of the equipment for Air Force contracts.

During May 1976, 8 of 17 contracts at this location authorized rent-free use of Government-owned equipment. One \$12.1 million Air Force contract in 1976 authorized use until February 1981. The contractor also expects to use this equipment on Army and Navy programs beyond 1983. The contractor therefore would not execute a new Air Force facilities contract which included a provision that all equipment not in a plant equipment package should be phased out by 1981.

In deciding not to execute the contract, the contractor said that the plant equipment is required to produce items with ever-changing requirements and, therefore, he could not agree to phasing out this equipment. The contractor pointed out that the present contracts authorizing use of the equipment through 1981 would have to be renegotiated if he could not retain the equipment until they were completed.

Menasco Manufacturing Company

On June 30, 1976, Menasco Manufacturing Company (California Division) had 84 Air Force industrial plant equipment items, costing about \$5 million, in a temporary Air Force plant equipment package, and 11 items costing \$563,000 not in the package. The contractor also had other plant equipment costing over \$125,000, of which some or all may be part of the temporary plant equipment package.

As of August 1976 the contractor had not submitted a formal phaseout plan because he was waiting for a decision on the plant equipment package. The contractor requested as early as August 1971 that the equipment be retained for industrial readiness, and he submitted a request to the Air Force for a plant equipment package in April 1972. The request was updated in 1973 and again in 1974, but as of December 1976, it had not yet been approved. This equipment has been deferred from phaseout pending a final decision on the package.

An Air Force Headquarters representative said in December 1976 that the Air Force was considering consolidating the plant equipment package with packages at the contractor's other locations and that the amount of equipment in the temporary package is expected to decrease. The Air Force was also considering replacing the facilities contract with a lease, whereby the Government-owned plant equipment would be phased out over a 10-year period.

INDUSTRIAL AND OTHER PLANT EQUIPMENT RETAINED FOR ANTICIPATED CONTRACT

One Air Force contractor, Rockwell International Corporation (B-1 Division), does not have a plant equipment package but was retaining \$9.6 million of plant equipment pending approval for production of the B-1 bomber. The amount consisted of \$8.1 million in industrial plant equipment and \$1.5 million in other plant equipment. At the time of our review of the contractor's plant, the contractor planned to acquire from the general reserve additional Government-owned plant equipment that cost \$8 million if production was approved. 1/

1/In June 1977, the President announced that the aircraft would not be produced at this time. We did not determine the impact of this announcement.

The contractor estimated that replacing the \$17.6 million of older Government-owned plant equipment with new contractor-owned equipment would cost up to \$50 million, half of which would be written off during the life of the aircraft program. Air Force representatives at the contractor's plant said that the \$50 million investment was a maximum amount and they believed that the replacement cost would be somewhat less.

In July 1976 the contractor submitted a plan to phase out the \$9.6 million in plant equipment by the end of 1986 unless the aircraft production schedule extends beyond that date. As of October 1976 the proposed plan had not been incorporated in the facilities contract.

PHASEOUT THROUGH NEGOTIATED SALES TO CONTRACTORS

Air Force Regulation 78-22 dated July 26, 1976, describes the categories of plant equipment exempted or deferred from the phaseout program. This regulation provides for deferring from phaseout plans equipment to be considered for sale until a decision is made on the sale.

Phaseout of \$8.9 million of Air Force plant equipment in the possession of two contractors has been delayed, pending sales negotiations between the contractors and GSA. Aerojet Manufacturing Company expressed interest in buying the equipment in September 1972 and Magna Mill Products expressed interest in February 1973. As of November 1976 negotiations for the sales were still pending.

IMPROPER ACQUISITION OF SPECIAL TEST EQUIPMENT

Our April 1971 1/ and August 1972 2/ reports to the Congress reported that large amounts of general-purpose test equipment had been acquired by contractors as special test equipment at Government expense. We stated that, had this equipment been classified properly as general-purpose test equipment, it probably would have been provided by the contractors because it would not have met the Armed Services Procurement Regulation criteria for furnishing Government-owned equipment to contractors.

1/"Improvements Being Made In The Controls Over Government Test Equipment Acquired By Contractors" (B-140389, Apr. 9, 1971).

2/See note, p. 1.

In both reports we recommended that Defense revise the definition of special test equipment and its regulations to exclude items that are really plant equipment. This has not been done, and general-purpose equipment is still being acquired as special test equipment. Hughes Aircraft Company estimated that 2,300 out of 3,400 special test equipment items are general-purpose items.

CONCLUSIONS

Defense must retain some Government-owned plant equipment at contractor plants for mobilization production. Improvements are needed in implementing the mobilization production policy to assure that all equipment required for mobilization production is specifically identified and justified. We believe that all equipment needed for mobilization production-- industrial plant equipment, other plant equipment, special test equipment, and tooling--should be included in the plant equipment packages.

Defense's policy of authorizing rent-free use of Government equipment in supply contracts has delayed the phaseout of plant equipment at contractor plants. Clarification is needed on the relationship between phaseout planning and rent-free use of equipment for supply contracts. Unless clarification is provided, equipment could be retained at contractor plants for supply contracts for an indefinite period.

RECOMMENDATIONS TO THE SECRETARY OF DEFENSE

As recommended on page 14, detailed instructions should be provided to the military services for determining the essential core of equipment needed to support either current procurements or mobilization production and for removing the nonessential items.

We also recommend that the military services be directed to specifically identify at each contractor plant the essential core of Government-owned equipment needed to support either current procurements or defense preparedness, and expedite their activities to remove nonessential items.

Finally, we recommend that Defense procedures for establishing plant equipment packages be revised to include both industrial and other plant equipment needed for mobilization production in the plant equipment packages.

CHAPTER 4
UTILIZATION AND CONTROL
OF PLANT EQUIPMENT

We reported to the Congress in August 1972 on the need for further improvements in controlling Government-owned industrial and other plant equipment furnished to Defense contractors. The report cited many examples of plant equipment, no longer needed for Government contracts, retained in contractor plants and used for commercial work without appropriate authorization. We recommended certain revisions to Defense regulations to require contractors to maintain better utilization records which in turn would provide better bases for (1) identifying equipment no longer needed and (2) evaluating rental computations.

Our current review involving 10 contractor locations and two recent Defense audits at 23 contractor locations showed that Defense continues to have the same problems.

PROCUREMENT REGULATIONS ON
UTILIZATION AND CONTROL

Appendix B of the Armed Services Procurement Regulation sets forth the basic requirements for contractors to control Government property furnished to them. ASPR B-603, Utilization of Government Property, states

"The contractor's procedures shall be in writing and adequate (i) to assure that Government property will be utilized only for those purposes authorized in the contract, and that any required approvals are obtained, and (ii) to provide a basis for determining and allocating charges."

ASPR B-603.1 describes the following minimum procedures applicable for using industrial plant equipment:

- Establishing a minimum level of utilization.
Anything below this level would require an analysis of need and a justification for retaining the equipment, except for approved inactive items held for mobilization.
- Providing for recording authorized and actual use consistent with the established utilization levels.

--Requiring periodic analyses of production needs for industrial plant equipment and for future utilization based on known requirements.

--Having firm provisions for immediately reporting to the contracting officer all industrial plant equipment items for which retention is not justified.

Defense's criteria for rent payments by contractors on Government-owned industrial and other plant equipment is contained in ASPR 7-702.12 (the "use and charges" clause) which is required in all facilities contracts. The clause permits contractors to use Government-owned plant equipment for commercial work, provided they pay rent. For industrial plant equipment, the clause provides for monthly rental rates between three-fourths and 3 percent of the acquisition cost, which includes installation and transportation costs, depending on the age of the equipment as shown below.

<u>Age of equipment</u> (years)	<u>Monthly rental rates</u> (in percent)
0 to 2	3.00
2 to 3	2.00
3 to 6	1.50
6 to 10	1.00
over 10	0.75

The rental for other plant equipment is to be no less than the prevailing commercial rate or, in the absence of a commercial rate, (1) not less than 2 percent a month for electronic test equipment and automotive equipment, and (2) not less than 1 percent a month for all other equipment.

ASPR 13-405, "Non-Government Use of Industrial Plant Equipment (IPE)" states that prior written approval from the contracting officer is required for non-Government use of equipment. It also states that the Secretary of the military branch concerned or a designee must approve non-Government use over 25 percent of the total available time.

RESULTS OF OUR REVIEW

We reviewed the use of plant equipment at three contractor plants and examined contract files and reports of utilization surveys for all 10 contractors at Defense offices administering those contracts. Following are some examples which show the need for better controls over the utilization of Government-owned plant equipment.

Example 1

The Air Force has not surveyed property utilization at Rockwell International (B-1 Division) since June 1973, primarily because the Air Force considered any idle or low-use equipment as needed for production of the B-1 bomber. The contractor maintains utilization records which identify those industrial plant equipment items used less than the minimum acceptable time specified in ASPR 603.1, and thus requiring justification for continued retention. Its records for industrial plant equipment items costing \$25,000 or more showed that during the year ended March 31, 1976, an average of 47 items costing \$2.6 million were used 14 percent of the available time. During this same period an average of 171 industrial plant equipment items costing \$1.5 million (but with a unit cost less than \$25,000) were used an average of 24 percent of the available time.

The contractor used some Government-owned plant equipment at times for commercial work over 25 percent of its available use without authorization. For example, two milling machines costing \$225,000 were used solely for commercial work since April 1975 without approval. The contractor was paying full rent for commercial use. The contractor said that the two machines had been adapted to produce items for the Government, but they are now used on commercial work. The contractor preferred to pay full rent rather than the cost to adapt similar contractor-owned machines.

As a result of our review (1) the Air Force has directed the contractor to stop using industrial plant equipment for commercial work over 25 percent of available time, (2) the contractor submitted a written request for commercial use of equipment in accordance with the rental agreement which has been approved by the Air Force, and (3) action was initiated immediately to remove from the contractor's plant the two items used solely for commercial work, making it available for use within the Defense Department.

Example 2

Because of the generally unsatisfactory condition of Hughes Aircraft Company's property control system in 1973, the rental agreement was terminated in January 1974 and the use of Government equipment for commercial work was suspended. Corrective action was taken by the contractor in 1974 and a new rental agreement was executed on January 1, 1975. The contractor's system is now approved.

In accordance with the approved system, the contractor does not maintain daily-use records for individual machines, but determines use from 20 observations per quarter for industrial plant equipment items costing \$25,000 or more, and 5 observations per quarter for items costing between \$1,000 and \$25,000. Use data is not obtained or recorded for other plant equipment (such as computer equipment) even though some equipment costs much more than \$1,000.

The contractor's use records for the year ending March 31, 1975, showed that 124 items did not meet the minimum acceptable utilization level. Our analysis of the 124 items showed that

- 73 items were being retained to meet planned mobilization production requirements,
- 28 items had been or were being excessed,
- 20 items met the following year's minimum acceptable percent utilization level, and
- 3 items were being retained for other reasons.

The contractor's records supporting rental payments for commercial use of plant equipment show that individual items have been used for commercial work more than 25 percent of actual time. For example, during one month 133 items costing \$222,000 were used for commercial work about 28 percent of actual time and 47 other items costing \$266,000 were used 61 percent of the time for commercial work.

ASPR 13-405 allows the contractor to determine the average utilization of all items costing less than \$25,000 per unit on a base time period of 3 months minimum to not more than a 1-year period. Averaging, therefore, may permit utilization of some items in excess of 25 percent without special authorization.

Example 3

Northrop Corporation's use system was considered unsatisfactory in 1972, 1974, 1975, and 1976 because the contractor did not maintain records on all Government-owned equipment. This contractor did not dispose of idle equipment on a timely basis in 1972, 1975, and 1976, and the contractor used equipment on Government work in 1975 and 1976 without proper authorization.

DEFENSE DEPARTMENT AUDITS

The Auditor General of the Defense Logistics Agency evaluates the adequacy of the Defense Contract Administration Services' regional equipment utilization surveys and regional contract administration procedures and controls for assessing and collecting rent for contractors' use of Government equipment.

The results of two recent Defense Logistics Agency audits are summarized below. Similar results were found in earlier audits.

St. Louis region--report number 76-126

The audit covered operations from October 1973 through June 1975 for nine contractors holding Government-owned plant equipment that cost about \$96.6 million. These contractors paid rent of \$310,150 for using equipment during fiscal years 1974 and 1975. The report (issued Mar. 5, 1976) stated that the administration of rental payments and the annual utilization surveys needed improvement. The following problems were reported.

- Three contractors had inadequate utilization records.
- Rents paid by six contractors were not calculated in accordance with the ASPR "use and charges" clause. Five contractors did not compute rent in accordance with their negotiated rental agreements. The auditors estimated that the six contractors had underpaid rent by \$115,563 during a 12-month period preceding the audit.
- An after-the-fact approval for unauthorized use caused a waiver of rent amounting to \$23,700.
- Rent was underpaid by about \$206,694 by two contractors because the Defense component furnishing the equipment had executed rental agreements which were not equitable to the Government.

Los Angeles region--report number 76-29

The audit covered operations from July 1972 through March 1975 for 14 contractors holding Government-owned

plant equipment costing \$138.9 million. These contractors paid rent of \$2.3 million for using equipment during fiscal years 1973 and 1974. The report (issued Aug. 22, 1975) stated that there was a need for improvement in the performance of annual utilization surveys, in assessing and collecting rent, and in negotiating rents. The report findings are summarized as follows:

- Equipment was used on Government or commercial contracts by six contractors without authorization. The uncollected rent was at least \$109,000. In addition, utilization records were so poor at two contractors' plants that neither use nor authorization could be determined.
- Rent was underpaid by about \$41,000 annually because it was not calculated in accordance with the rental agreements with three contractors.
- Negotiated rental agreements were not adequate for two contractors, rental agreements for two other contractors had not been negotiated, and the basis of the rent computations was not specific in another facilities contract.

CONCLUSION

Defense continues to have problems with managing and controlling the use of Government-owned plant equipment. Defense needs to be more aggressive in obtaining contractor compliance with existing regulations and must improve its contract administration to protect Government interests. An alternative would be to restrict the use of Government equipment to Government work. This policy would motivate some contractors to increase their investment in contractor-owned equipment to remain competitive and would also tend to expedite phasing out of Government-owned equipment. We realize that some advantages of such a policy would be offset by the reluctance of contractors to retain idle or low-use Government equipment solely to maintain capability to meet mobilization requirements.

RECOMMENDATION TO THE SECRETARY OF DEFENSE

In view of the continuing difficulties in controlling the use of Government-owned equipment, the Defense Department should reassess its position on authorizing the use of

Government equipment for commercial work and require the contractor to maintain use records to improve the contractors' accounting for use of Government equipment on commercial work.

CHAPTER 5

SCOPE OF REVIEW

We obtained statistics, reports, and overall data on Government-owned equipment in the custody of contractors, and implementation of the phaseout program, from the Defense Department, military service headquarters, and the Defense Industrial Plant Equipment Center (Memphis, Tennessee). We did not verify the accuracy of the statistics provided. We also reviewed reports issued by Defense Department audit agencies on management and use of Government equipment in contractors' possession.

Our review included 10 contractors in the Southern California area. We made a detailed review at three contractor plants and obtained information for the remaining seven contractors primarily by questionnaires to the contractors and from records and files of the cognizant Department of Defense contract administration office. The number of contractors selected was limited to 10 because this was a followup to our August 1972 report; we essentially wanted to know if problems previously identified in that report still exist. Three of the 10 contractors were also included on our earlier review.

- Aerojet Manufacturing Company, Fullerton, California 1/
- Hughes Aircraft Company, Culver City, California 1/ 2/
- Magna Mill Products, South Gate, California
- McDonnell Douglas Corporation, Douglas Aircraft Co., Long Beach, California
- Menasco Manufacturing Company, California Division, Burbank, California 1/
- Norris Industries, Vernon Division, Los Angeles, California 2/
- Northrop Corporation, Electric-Mechanical Division, Anaheim, California

1/Also included in earlier review.

2/Detailed review.

--Rockwell International Corporation, B-1 Division,
Los Angeles, California 1/

--Silent Industries, Inc., North Long Beach,
California

--The Singer Company, Librascope Division, Glendale,
California

We did not review Government equipment (1) at Government-owned plants operated by contractors or (2) in the custody of nonprofit contractors because the Defense Department has exempted this equipment from the phaseout program.

1/Detailed review.

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CHANGES IN GOVERNMENT-OWNED PLANT EQUIPMENT
IN THE CUSTODY OF 10 SELECTED CONTRACTORS
DURING THE 5-YEAR PERIOD ENDED JUNE 30, 1976

<u>Contractor</u>	<u>Service</u>	<u>Total plant equipment</u>		
		<u>6/30/71</u>	<u>6/30/76</u>	<u>Increase/ (decrease)</u>
(\$000 omitted)				
Norris Industries Vernon Division	Army	8,882	11,698	2,816
	Navy	<u>5,639</u>	<u>5,651</u>	<u>13</u>
		14,521	17,349	2,829
Hughes Aircraft Company	Army	1,319	899	(420)
	Navy	2,167	397	(1,770)
	Air Force	<u>17,031</u>	<u>9,205</u>	<u>(7,826)</u>
		20,517	10,501	(10,016)
Northrop Corporation Electro-Mechanical Division	Army	8,959	9,781	822
	Navy	408	305	(103)
	Air Force	<u>1,066</u>	<u>-</u>	<u>(1,066)</u>
		10,433	10,086	(347)
Rockwell International B-1 Division	Air Force	19,159	9,595	(9,564)
	Air Force	19,159	9,595	(9,564)
Aerojet Manufacturing Company	Army	643	-	(643)
	Navy	3,226	39	(3,187)
	Air Force	<u>5,216</u>	<u>6,250</u>	<u>1,034</u>
		9,085	6,289	(2,796)
Menasco Manufacturing Company California Division	Air Force	6,731	5,665	(1,066)
McDonnell Douglas Company Douglas Aircraft Company	Navy	3,837	4,689	852
Silent Industries, Inc.	Army	<u>a/3,918</u>	4,215	297
Magna Mill Products	Air Force	3,130	2,662	(468)
Singer Company Librascope Division	Navy	1,535	1,399	(136)
Subtotals	Army	23,721	26,593	2,873
	Navy	16,812	12,480	(4,332)
	Air Force	<u>52,333</u>	<u>33,377</u>	<u>(18,956)</u>
Total		<u>92,866</u>	<u>72,450</u>	<u>(20,415)</u>

a/As of June 30, 1974. The company was formed in December 1973.

AMOUNT OF INDUSTRIAL PLANT EQUIPMENT
INCLUDED IN PLANT EQUIPMENT PACKAGES

<u>Contractor</u>	<u>Service</u>	<u>Industrial plant equipment</u>		
		<u>6/30/76</u>	<u>Amount in packages</u>	<u>Percentage in packages</u>
(000 omitted)				
Norris Industries Vernon Division	Army	\$10,489	\$ 5,748	54.8
	Navy	<u>4,989</u>	<u>4,989</u>	100.0
		15,478	10,737	69.4
Hughes Aircraft Company	Army	366	0	0
	Navy	166	91	54.8
	Air Force	<u>5,833</u>	<u>2,016</u>	34.6
		6,365	2,107	33.1
Northrop Corporation Electro-Mechanical Division	Army	8,646	4,523	52.3
	Navy	96	0	0
	Air Force	<u>0</u>	<u>0</u>	0
		8,742	4,523	51.7
Rockwell International B-1 Division	Air Force	8,052	0	0
Aerojet Manufacturing Company	Army	0	0	0
	Navy	39	0	0
	Air Force	<u>6,139</u>	<u>0</u>	0
		6,178	0	0
Menasco Manufacturing Com- pany, California Division (note a)	Air Force	5,539	4,976	89.8
McDonnell Douglas Corpora- tion, Douglas Aircraft Company	Navy	4,689	0	0
Silent Industries, Inc.	Army	4,029	4,029	100.0
Magna Mill Products	Air Force	2,662	0	0
Singer Company Librascope Division	Navy	1,338	1,254	93.8
Subtotals	Army	23,530	14,300	60.8
	Navy	11,316	6,334	56.0
	Air Force	<u>28,225</u>	<u>6,992</u>	24.8
Total		<u>\$63,071</u>	<u>\$27,626</u>	43.8

a/The amount shown as in a plant equipment package is in a temporary package.

CHANGES IN GOVERNMENT-OWNED
INDUSTRIAL PLANT EQUIPMENT IN CONTRACTORS' POSSESSION
DURING THE 5 YEARS ENDED JUNE 30, 1976

	<u>6/30/71</u>	<u>6/30/76</u>	<u>Increase or (decrease)</u>	
			<u>Amount</u>	<u>Percent</u>
	—————(000,000 omitted)—————			
<u>Army</u>				
In packages:				
Active	\$ 88	\$ 82	\$ (6)	(7)
Inactive	290	245	(45)	(16)
Subtotal	<u>378</u>	<u>327</u>	<u>(51)</u>	(13)
Not in packages	<u>396</u>	<u>293</u>	<u>(103)</u>	(26)
Total	<u>774</u>	<u>620</u>	<u>(154)</u>	(20)
<u>Navy</u>				
In packages:				
Active	0	11	11	-
Inactive	73	104	31	42
Subtotal	<u>73</u>	<u>115</u>	<u>42</u>	58
Not in packages	<u>294</u>	<u>186</u>	<u>(108)</u>	(37)
Total	<u>367</u>	<u>301</u>	<u>(66)</u>	(18)
<u>Air Force</u>				
In packages:				
Active	0	152	152	-
Inactive	16	15	(1)	(6)
Subtotal	<u>16</u>	<u>167</u>	<u>151</u>	944
Not in packages	<u>880</u>	<u>523</u>	<u>(357)</u>	(41)
Total	<u>896</u>	<u>690</u>	<u>(206)</u>	(23)
<u>Other components</u>				
In packages:				
Active	0	0	0	0
Inactive	0	0	0	0
Subtotal	<u>0</u>	<u>0</u>	<u>0</u>	0
Not in packages	<u>16</u>	<u>14</u>	<u>(2)</u>	(13)
Total	<u>16</u>	<u>14</u>	<u>(2)</u>	(13)
<u>Grand totals</u>				
In packages:				
Active	88	245	157	178
Inactive	379	364	(15)	(4)
Subtotal	<u>467</u>	<u>609</u>	<u>142</u>	30
Not in packages	<u>1,586</u>	<u>1,016</u>	<u>(570)</u>	(36)
Total	<u>\$2,053</u>	<u>\$1,625</u>	<u>\$(428)</u>	(21)

CHANGES IN GOVERNMENT-OWNED
INDUSTRIAL PLANT EQUIPMENT IN GOVERNMENT PLANTS
OPERATED BY CONTRACTORS DURING
THE 5 YEARS ENDED JUNE 30, 1976

	<u>6/30/71</u>	<u>6/30/76</u>	<u>Increase or (decrease)</u>	
			<u>Amount</u>	<u>Percent</u>
————(000,000 omitted)————				
<u>Army</u>				
In packages:				
Active	\$ 51	\$ 38	\$(13)	(25)
Inactive	179	192	13	7
Subtotal	<u>230</u>	<u>230</u>	<u>0</u>	0
Not in packages	<u>220</u>	<u>176</u>	<u>(44)</u>	(20)
Total	<u>450</u>	<u>406</u>	<u>(44)</u>	(10)
<u>Navy</u>				
In packages:				
Active	0	4	4	-
Inactive	47	72	25	53
Subtotal	<u>47</u>	<u>76</u>	<u>29</u>	62
Not in packages	<u>123</u>	<u>89</u>	<u>(34)</u>	(28)
Total	<u>170</u>	<u>165</u>	<u>(5)</u>	(3)
<u>Air Force</u>				
In packages:				
Active	0	70	70	-
Inactive	0	5	5	-
Subtotal	<u>0</u>	<u>75</u>	<u>75</u>	-
Not in packages	<u>188</u>	<u>125</u>	<u>(63)</u>	(34)
Total	<u>188</u>	<u>200</u>	<u>12</u>	6
<u>Other components</u>				
In packages:				
Active	0	0	0	0
Inactive	0	0	0	0
Subtotal	<u>0</u>	<u>0</u>	<u>0</u>	0
Not in packages	<u>2</u>	<u>2</u>	<u>0</u>	0
Total	<u>2</u>	<u>2</u>	<u>0</u>	0
<u>Grand totals</u>				
In packages:				
Active	51	112	61	120
Inactive	226	269	43	19
Subtotal	<u>277</u>	<u>381</u>	<u>104</u>	38
Not in packages	<u>533</u>	<u>392</u>	<u>(141)</u>	(26)
Total	<u>\$810</u>	<u>\$773</u>	<u>\$(37)</u>	(5)

CHANGES IN GOVERNMENT-OWNED
INDUSTRIAL PLANT EQUIPMENT IN CONTRACTORS' PLANTS
DURING THE 5 YEARS ENDED JUNE 30, 1976

	<u>6/30, '71</u>	<u>6/30/76</u>	<u>Increase or (decrease)</u> <u>Amount</u>	<u>Percent</u>
	—(000,000 omitted)—			
Army				
In packages:				
Active	\$ 37	\$ 44	\$ 7	
Inactive	111	53	(58)	19
Subtotal	<u>148</u>	<u>97</u>	<u>(51)</u>	(34)
Not in packages	176	117	(59)	(34)
Total	<u>324</u>	<u>214</u>	<u>(110)</u>	(34)
Navy				
In packages:				
Active	0	7	7	0
Inactive	26	32	6	23
Subtotal	<u>26</u>	<u>39</u>	<u>13</u>	50
Not in packages	171	97	(74)	(43)
Total	<u>197</u>	<u>136</u>	<u>(61)</u>	(31)
Air Force				
In packages:				
Active	0	82	82	0
Inactive	16	10	(6)	(38)
Subtotal	<u>16</u>	<u>92</u>	<u>76</u>	475
Not in packages	692	398	(294)	(42)
Total	<u>708</u>	<u>490</u>	<u>(218)</u>	(31)
Other components				
In packages:				
Active	0	0	0	0
Inactive	0	0	0	0
Subtotal	<u>0</u>	<u>0</u>	<u>0</u>	0
Not in packages	14	12	(2)	(14)
Total	<u>14</u>	<u>12</u>	<u>(2)</u>	(14)
Grand totals				
In packages:				
Active	37	133	96	259
Inactive	153	95	(58)	(38)
Subtotal	<u>190</u>	<u>228</u>	<u>38</u>	20
Not in packages	1,053	624	(429)	(41)
Total	<u>\$1,243</u>	<u>\$852</u>	<u>\$(391)</u>	(31)

MEMORIAL TEL. CHAIRMAN
 JOHN H. MOSS, CALIF.
 BENJAMIN C. ROSENTHAL, N.Y.
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FRANK ROSTON, N.Y.
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 220-2147

SEVENTY-FOURTH CONGRESS
Congress of the United States
House of Representatives
 LEGISLATION AND NATIONAL SECURITY SUBCOMMITTEE
 OF THE
 COMMITTEE ON GOVERNMENT OPERATIONS
 RAYBURN HOUSE OFFICE BUILDING, ROOM B-373
 WASHINGTON, D.C. 20515

B-140389

December 31, 1975

The Honorable Elmer B. Staats
 The Comptroller General
 U. S. General Accounting Office
 Washington, D. C. 20548

Dear Elmer:

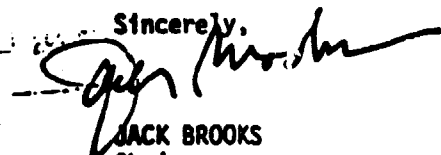
The Legislation and National Security Subcommittee is becoming increasingly concerned about DOD's practice of furnishing large amounts of Government-owned equipment to Government contractors. This practice is costly to the Government and may give certain contractors a substantial competitive advantage. The Subcommittee plans to initiate an investigation to determine the desirability of continuing this program.

Through preliminary contacts with Mr. Carmen Smarrelli and Mr. Ray Dunham of the Logistics and Communications Division, the Subcommittee staff is aware of GAO's past work concerning DOD's plans to phase out the use of Government-owned equipment by Government contractors. It appears that DOD has not pursued these plans very aggressively. To assist the Subcommittee in its investigation, it is requested that GAO (1) ascertain the extent to which DOD is pursuing a phase-out policy, (2) update its previous findings on DOD's requirements concerning contractors' utilization records, (3) investigate the extent to which plant equipment packages (PEPs) contain only the property needed for an approved preparedness plan, (4) determine whether PEP property is being mothballed or remains in use by contractors, and (5) develop a more precise understanding of the property in DIPEC's possession and its use or intended use by DOD.

I have asked the Secretary of Defense for information on the above matters, and will make this information available to you when it is received.

Your cooperation in this matter is appreciated.

Sincerely,



JACK BROOKS
 Chairman

LIST OF GAO REPORTS TO THE CONGRESSAND THE SECRETARY OF DEFENSEON THE DEFENSE DEPARTMENT'SMANAGEMENT OF PLANT EQUIPMENT

Need For Improvements In Controls Over Government-Owned Property In Contractor's Plants (B-140389, Nov. 24, 1967)

Action Taken To Put Inactive Industrial Plant Equipment In Army Arsenal's To Use (B-163691, May 23, 1968)

Construction Of Industrial Facilities At Government-Owned Plants Without Disclosure To The Congress (B-140389, Apr. 7, 1970)

Improvements Being Made In The Controls Over Government Test Equipment Acquired By Contractors (B-140389, Apr. 9, 1971)

Further Improvements Needed In Controls Over Government-Owned Plant Equipment In Custody Of Contractors (B-140389, Aug. 29, 1972)

Management Of Ship Overhaul And Repair Programs, Fiscal Years 1972 And 1973 (B-133170, June 7, 1973)

An Industrial Management Review Of The Maintenance Directorate, San Antonio Air Materiel Area, San Antonio, Texas (B-159896, Apr. 11, 1974)

Industrial Management Review Of Puget Sound Naval Shipyard (B-118733, Aug. 5, 1974)

Numerically Controlled Industrial Equipment: Progress And Problems (B-140389, Sept. 24, 1974)

Government Support Of The Shipbuilding Industrial Base (PSAD-75-44, Feb. 12, 1975)

Use Of Numerically Controlled Equipment Can Increase Productivity In Defense Plants (LCD-75-415, June 26, 1975)

Navy Aircraft Overhaul Depots Could Be More Productive (LCD-75-432, Dec. 23, 1975)

Management Of Department Of Defense Industrial Plant Equipment Can Be Improved (LCD-76-407, Oct. 5, 1976)

**Restructuring Needed Of Department Of Defense Program For
Planning With Private Industry For Mobilization Production
Requirements (PSAD-77-108, May 13, 1977)**

PRINCIPAL OFFICIALS RESPONSIBLE FOR
ACTIVITIES DISCUSSED IN THIS REPORT

	<u>Tenure of office</u>	
	<u>From</u>	<u>To</u>
SECRETARY OF DEFENSE:		
Dr. Harold Brown	Feb. 1977	Present
Donald H. Rumsfeld	Nov. 1975	Jan. 1977
James R. Schlesinger	July 1973	Nov. 1975
William P. Clements, Jr. (acting)	Apr. 1973	July 1973
Elliot L. Richardson	Jan. 1973	Apr. 1973
ASSISTANT SECRETARY OF DEFENSE (MANPOWER, RESERVE AFFAIRS, AND LOGISTICS):		
Dr. John P. White	May 1977	Present
Dale R. Babione (acting)	Jan. 1977	Apr. 1977
Frank A. Shrontz	Feb. 1976	Jan. 1977
John J. Bennett (acting)	Mar. 1975	Feb. 1976
Arthur I. Mendolia	June 1973	Mar. 1975
Hugh McCullough (acting)	Jan. 1973	June 1973
DIRECTOR, DEFENSE LOGISTICS AGENCY:		
Lt. Gen. Woodrow E. Vaughn (USA)	Dec. 1975	Present
Lt. Gen. Wallace H. Robinson, Jr. (USMC)	July 1971	Dec. 1975
SECRETARY OF THE AIR FORCE:		
John C. Stetson	Apr. 1977	Present
Thomas C. Reed	Jan. 1976	Apr. 1977
James W. Plummer (acting)	Nov. 1975	Jan. 1976
Dr. John L. McLucas	June 1973	Nov. 1975
Dr. Robert C. Seamans, Jr.	Jan. 1969	May 1973
SECRETARY OF THE ARMY:		
Clifford L. Alexander, Jr.	Feb. 1977	Present
Martin R. Hoffmann	Aug. 1975	Jan. 1977
Howard H. Callaway	July 1973	Aug. 1975
Robert F. Froehke	Jan. 1971	Apr. 1973
SECRETARY OF THE NAVY:		
W. Graham Claytor, Jr.	Feb. 1977	Present
J. William Middendorf	Apr. 1974	Jan. 1977
John W. Warner	May 1972	Apr. 1974

(947218)