

GAO

Report to the Assistant Secretary of the
Navy for Financial Management

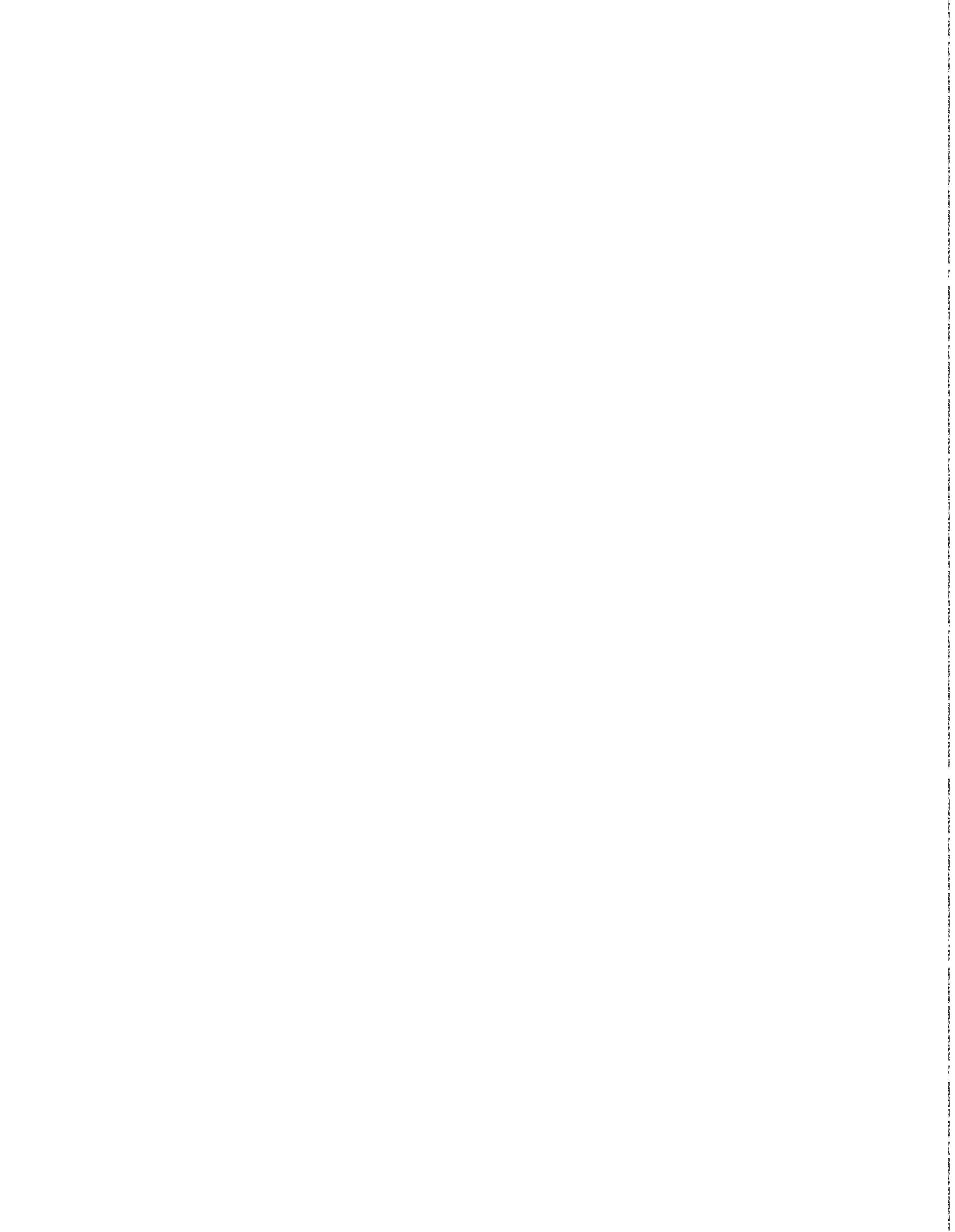
December 1986

NAVY CONTRACTING

Improving Management of Procurements for Computer-Aided Equipment



131845-





United States
General Accounting Office
Washington, D.C. 20548

National Security and
International Affairs Division

B-224148

December 30, 1986

The Honorable Robert H. Conn
The Assistant Secretary of the Navy
for Financial Management

Dear Mr. Conn:

This report presents the results of our review of the Navy's procurement of computer-aided design and computer-aided manufacturing (CAD/CAM) equipment and related services under seven contracts. (See app. IV for a listing of these contracts.) The largest is an estimated \$99.9 million contract for the Computer Aided Engineering Documentation System (CAEDOS) with the Computervision Corporation.

Our review was initiated as the result of a GAO Fraud Hotline referral involving possible procurement violations on a CAD/CAM contract the Long Beach Naval Shipyard had awarded. The Navy, based on our inquiry, investigated the matter and found that two contracts contained irregularities and procurement violations. We subsequently visited additional naval activities to determine if (1) the CAD/CAM procurement problems were widespread, (2) the problems could negatively affect future CAD/CAM procurements, and (3) the Navy's management of CAD/CAM acquisitions needs to be improved. Our objectives, scope, and methodology are discussed in appendix II.

We found that required approvals by your office were not obtained for some contract actions. Consequently, the dollar amounts of the initial contract award, as well as subsequent modifications, exceeded approval limits. Neither we nor the Navy could determine the total actual value of the CAEDOS contract because procurement regulations were not followed and adequate records were not maintained. We also found that controls were not adequate to ensure that payments made under the contract were proper. In addition, appropriate accounting classification data were not consistently charged. (See app. I for a further discussion of our observations.)

Navy activities have taken some actions to improve these situations. However, we believe these problems, unless corrected, could recur in future CAD/CAM acquisitions.

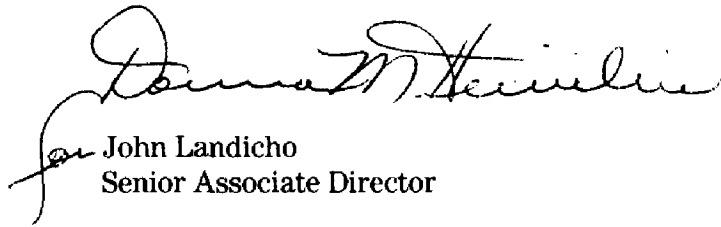
We briefed you on our findings in December 1985. In a February 26, 1986, letter (see app. III), you concurred with our findings, agreed that

corrective actions were needed, outlined several immediate actions, and stated that additional corrective actions would be taken on specific problems identified in this report. This report illustrates the necessity for (1) determining the amount of the contract, its obligations, expenditures, and credits and (2) implementing procedures so that lessons learned from this contract are applied to future CAD/CAM procurements.

In view of the improvements already made and your willingness to take corrective action upon receipt of our report identifying specific problems, we are not making recommendations at this time. However, we would appreciate being informed of any further corrective actions planned or taken on these issues.

Copies of this report are being sent to the Secretary of the Navy and to the Director, Defense Logistics Agency. Copies will be made available to other interested parties.

Sincerely yours,



for John Landicho
Senior Associate Director

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Abbreviations

ADP	Automatic Data Processing
ASN/FM	Assistant Secretary of the Navy for Financial Management
CAD/CAM	Computer-Aided Design and Computer-Aided Manufacturing
CAEDOS	Computer Aided Engineering Documentation System
COTR	Contracting Officer's Technical Representative
DCASMA	Defense Contract Administration Services Management Area
DCASR	Defense Contract Administration Services Region
GAO	General Accounting Office
NAVDAC	Naval Data Automation Command
NRCC	Naval Regional Contracting Center

Observations on the Navy's Procurement and Management of CAD/CAM Equipment and Services

Our review concentrated on the Navy's CAEDOS contract. This contract was awarded to the Computervision Corporation of Bedford, Massachusetts, on September 23, 1981, for approximately \$63 million, and provided for the initial acquisition of CAD/CAM equipment, software, and related support services for a 1-year period, with renewable options for 7 additional years. The contract establishes maximum equipment ordering limitations. Funds are obligated when delivery orders are placed under the contract.

As of September 30, 1985, the basic contract had been modified 35 times. Its current value is estimated at \$99.9 million, although there is no contractual documentation supporting this amount.

Approximately 50 naval activities, including shipyards, air rework facilities, and laboratories, purchase CAD/CAM equipment and related services under the contract. Contract management and administration are performed by the following Navy and Defense Logistics Agency organizations located across the country:

- The contracting officer at the Naval Regional Contracting Center (NRCC), Long Beach, California, is responsible for final review and approval of all contract actions.
- The contracting officer's technical representative (COTR), located at the Naval Weapons Center, China Lake, California, is responsible for coordination and control of the acquisition, maintenance, and training associated with the contract, including preparing delivery orders and authorizing the payment of invoices.
- The Defense Contract Administration Services Region (DCASR) and the Defense Contract Administration Services Management Area (DCASMA), Boston, Massachusetts, are responsible for payment and contract administration, respectively.
- The Commander, Naval Data Automation Command (NAVDAC), Washington, D.C., is responsible for reviewing proposed automatic data processing (ADP) procurement requests for technical adequacy and for forwarding agency procurement requests and related ADP actions to the appropriate approval authority.

ASN/FM Approvals Not Obtained for Some Contract Actions

Navy ADP procurement regulations require Assistant Secretary of the Navy for Financial Management (ASN/FM) approval for the initial acquisition of ADP equipment, service, or software and for the extension or expansion of an existing contract when specific dollar thresholds are exceeded. Navy Instructions 5230.6 and 5230.6B require ASN/FM

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approval for the initial, competitive acquisition of equipment and support services exceeding \$3 million and for sole-source expansion of \$1 million or more to existing contracts.

Required approvals were not obtained on \$66.7 million of the estimated \$99.9 million—current value of the CAEDOS contract. The initial amount approved for contract award was exceeded by \$32.4 million, and subsequent contract modifications exceeded the amount approved by \$34.3 million, as shown in table I.1.

**Table I.1: CAEDOS Contract Amounts
Exceeding ASN/FM Approvals**

Dollars in millions

Description	Amount		
	Contract award	Approved	Not approved
Basic contract award:			
Procurement approval		\$27.8	\$0
Authorized increase		2.8	32.4
Total	63.0	30.6	32.4
Modifications ^a :			
Number 6	6.6	0	6.6
Number 14	30.3	2.6	27.7
Total	36.9	2.6	34.3
Total	\$99.9	\$33.2	\$66.7

^aThe contract, as amended, has no stated value. These values reflect the contracting officer's, the COTR's, and Computervision's best estimate based on assumptions or documentation that is not referenced by the contract or the respective modifications.

Initial Contract Award

The initial CAEDOS contract award of \$63 million exceeded the amount the ASN/FM approved by \$32.4 million. On October 31, 1979, the ASN/FM approved awarding a contract at an estimated cost of \$27.8 million. He directed that the total contract cost could not be exceeded by 10 percent, for a total contract value of \$30.6 million, without approval from his office. However, on September 23, 1981, the contract was awarded by the NRCC, Long Beach, California, for approximately \$63 million.

NRCC officials, including the contracting officer, mistakenly believed that additional approval from the ASN/FM for the increase in contract value was not required. In addition, although NAVDAC reviewed the CAEDOS contracts, NAVDAC officials could not explain why the contract award exceeding the amount approved by the ASN/FM was not detected.

Contract Modifications

The dollar amount of modifications to the CAEDOS contract exceeded the amount approved by \$34.3 million. Of the total estimated \$36.9 million in modifications to the contract, only \$2.6 million was approved by the ASN/FM.

According to COTR correspondence, modification number 6, issued August 10, 1982, added an estimated \$6.6 million to the original contract award. However, ASN/FM approval, which was required prior to award of this modification, was not obtained. The responsible NAVDAC official stated that the modification was improperly approved at the NAVDAC level, which did not have the authority to grant such approval.

Modification number 14, issued on September 16, 1983, was approved by the ASN/FM for a total contract cost increase of \$2.6 million. However, the actual value of this modification has been estimated at \$30.3 million by the COTR. Similar to what occurred with the initial contract award, the contracting officer mistakenly believed that an additional approval from the ASN/FM for the increase in the modification's value was not required.

The Contract, As Modified, Has No Stated Value

The total value of the CAEDOS contract, as modified, is not known. The contracting officer, the COTR, and the responsible NAVDAC officials could not explain why the modifications did not specify a contract value. Defense Acquisition Regulations 16-104.4 and 26-104 require that each modification shall clearly state the impact on the overall total contract price.

Although the CAEDOS contract has been modified 35 times, as of the end of fiscal year 1985, there was no contractual documentation stating its actual value. NRCC, COTR, and contractor officials believe the estimated value of the contract is \$99.9 million. The COTR prepared a schedule showing the estimated value of selected modifications, which when added to the value of the initial contract, totaled \$99.9 million. We attempted to summarize the total value of the contract and its modifications but were unable to do so because of missing or incomplete documentation.

The contracting officer stated that, although the value of the modified contract has not been documented, the delivery orders, which obligate funds, do have stated values. However, we found that the delivery orders were not effectively matched against the contract to determine if the terms and conditions of the contract were met.

Controls Not Adequate to Ensure Proper Contract Obligations and Expenditures

The Navy does not have an effective system to properly control obligations and expenditures under the CAEDOS contract, although such a system is required by federal regulations. Specifically, we found:

- Expenditures were not consistently charged to the appropriate accounting classification.
- Required contractual documentation was often missing, incomplete, or late.
- Payments were not effectively tracked or matched against obligations.
- Credit for maintenance and equipment downtime was inconsistently reported and used.

As a result, the total amount paid was not known, and there was no assurance that (1) payments for equipment and services were proper and (2) performance was in accordance with contractual terms and conditions. In fact, as of October 1985, the COTR and Computervision had identified gross discrepancies totaling over \$2 million.

Federal Regulations Require Adequate Contract Controls

Federal law and regulations applicable to the CAEDOS contract require a system to control contract obligations and expenditures. Each accounting system should provide information and controls to insure that (1) funds are used only for authorized purposes and (2) obligations and expenditures do not exceed authorized amounts. In addition, Defense Acquisition Regulation 20-308 and Department of Defense Supplement to the Federal Acquisition Regulation 4.7108 require that accounting classification data be related to specific contract line item numbers. The accounting classification reference number is used to associate contract line items with particular lines of accounting against which to make payment. These latter two regulations require that the reference number be used in all contracts administered by the Defense Contract Administration Service. These same regulations also require that the purchasing office (NRCC, Long Beach, in this case) assign the reference numbers and state that this responsibility shall not be delegated to another office.

Appropriate Accounting Classification Data Not Consistently Charged

Expenditures for equipment and services were not consistently charged to the appropriate accounting classification because the COTR did not always provide reference numbers on the delivery orders. According to DCASR and DCASMA officials, most delivery orders were subsequently modified in ways that changed reference numbers and funding, which further complicated tracking expenses against obligations. As a result,

DCASR and DCASMA officials reported to the COTR that funding balances remaining on delivery orders and billed to the separately funded user activities were not representative of services rendered. In December 1984, DCASMA informed the COTR that due to the inadequate system, the service could not accept responsibility for reconciling contract charges to individual lines of accounting or to user activities.

DCASMA also informed the contracting officer that due to these problems, DCASR had stopped trying to apply payments to the appropriate accounting classification reference numbers. DCASR and DCASMA officials stated that, as a result of this situation, almost every delivery order needed a total audit before being closed out. Further, a DCASR official said some delivery orders were closed out that should not have been and the total amount of incorrect charges was not known.

DCASR and DCASMA officials told us that while COTR personnel spent much time attempting to correct the problems, little had been accomplished to improve the situation prior to our visit.

**Required Contract
Documentation Was
Missing, Incomplete, or Late**

Documentation essential to properly account and determine the propriety of payments under the CAEDOS contract was often missing, incomplete, or late. The documents include procurement approvals, requests for contractual procurement, the contract, delivery orders, modifications to the contract, receipt and acceptance forms, and invoices and related advice of payments.

The activities we visited lacked the necessary documentation to determine the appropriateness of charges under the CAEDOS contract. One reason given by many was poor document distribution. In March 1985, DCASMA determined that it had not received over 100 delivery orders and modifications from the COTR. Also, DCASR questioned the COTR about modifications not received because of their impact on closed delivery orders. Furthermore, several officials at user activities stated that their activities needed to go back to "day one" to reconstruct past contract actions and to request related documents to ensure that amounts paid were proper and that appropriate procedures were followed.

One of the user activities we visited and the COTR had difficulty reconciling their CAD/CAM equipment inventories with what had been billed because of incomplete records. The COTR stated that there were discrepancies in the CAD/CAM inventory for the different users. As a result, the COTR stated that he was going through every delivery order for every

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activity from "day one" to determine what equipment should be at each site.

When contract documentation did exist, several user activities we visited had difficulty tracking contract actions because of unclear and incomplete information. For example, an analyst stated that he could not make "heads or tails" of the documentation, especially the delivery orders, because the information was incomplete and not descriptive enough to clearly track contract actions. He blamed this condition on incomplete accounting data, mathematical errors, commingling of funds from multiple funding documents, and numerous modifications to delivery orders.

The COTR and the contracting officer did not process delivery orders in a timely manner—some were issued 6 to 20 months late. For example, the contracting officer signed two delivery orders that were dated February 6, 1984, and October 1, 1984, on September 9, 1985. In addition, DCASMA reported that 10 expired delivery orders, for which modifications had been written in January 1985 and signed in March 1985, had not been distributed as of April 12, 1985.

According to Computervision representatives, more timely processing of delivery orders was often requested as the Corporation postponed submitting invoices because DCASR would reject bills in the absence of authorized delivery orders. According to Computervision representatives, approximately \$600,000 in accruals for past services have yet to be billed. The contracting officer advised all parties that delinquent delivery orders would no longer be approved and that the vendor would be instructed to file a claim for any monies it believes the Navy owes.

**Payments Not Effectively
Tracked or Matched
Against Obligations**

Because the appropriate accounting classifications were not always provided and required contract documentation was missing, incomplete, or late, DCASR could not match expenditures against appropriate obligations when making contract payments. Also, the contracting officer was not tracking payments against obligations, nor did he ensure that the COTR was effectively performing this function. Neither the contracting officer nor the COTR could track or monitor payments because advice of payments, which shows actual charges by obligation, had not been received. The user activities, although receiving advice of payment, did not consistently track or match payments against their funding obligations.

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The COTR was uncertain as to what contractual controls existed and who should be determining the propriety of payments. He had been relying on DCASR and the user activities to track expenditures and ensure propriety of payment since he had not received adequate information to properly track payments.

According to several user activity officials, funding documents were prepared without considering the terms and conditions of the contract and were based on information the COTR provided. These officials stated that they relied on the COTR and DCASR to manage their funds and expenditures. However, because they believe they also are responsible for tracking obligations and expenditures, they plan to take corrective action.

Through attempts to reconcile expenditures against obligations, DCASR and the COTR identified instances of duplicate payments under the CAEDOS contract and other cases in which payments had not been made. While the amounts are preliminary, the COTR has identified approximately \$197,000 due the government and over \$949,000 owed to Computervision.

**Credits for Maintenance
and Equipment Downtime
Were Inconsistently
Reported and Used**

Although the CAEDOS contract provides credit for CAD/CAM maintenance and equipment downtime, the user activities we visited and the COTR were not consistently reporting downtime and utilizing the credit. The users stated they either failed to understand the credit accounting and reporting system or believed tracking and reporting downtime was not cost effective. COTR officials stated that an effective system for collecting and tracking users' downtime credit was not maintained and that many of the original records the users had submitted to the COTR had been discarded in error.

During our review, the COTR, in an attempt to correct the problem by reconstructing past maintenance and equipment downtime credits, identified over \$303,000 in credits for fiscal year 1984. Although the COTR plans to apply these credits against fiscal year 1986 equipment maintenance costs, Computervision, citing a lack of supporting documentation and numerous data entry and mathematical errors, has taken exception to the amount and is seeking relief from the claims.

Problems May Recur in Future Procurements

According to NAVDAC, shipyard, DCASMA, and DCASR officials, as well as Computervision representatives, the problems associated with the CAEDOS contract, if not corrected, may recur in future procurements. We agree, and since larger CAD/CAM acquisitions are being planned, the Navy needs to quickly resolve its contract control weaknesses.

Officials in NAVDAC, the COTR's office, and the Naval Sea Systems Command's Information Systems Improvement Program Office advised us that major CAD/CAM acquisitions are being planned, with estimated costs ranging from \$500 million for an interim buy to over \$1 billion for long-term acquisitions. However, according to the ASN/FM, as of December 3, 1985, funds for these procurements had not been budgeted.

Although the majority of our efforts involved the CAEDOS contract, we found indications that similar problems existed on other CAD/CAM procurements. In August 1985, the Navy awarded a \$13.4 million contract for CAD/CAM equipment at the Long Beach Naval Shipyard. This contract was, in part, a replacement for two earlier CAD/CAM contracts that the ASN/FM had discontinued because of contractual irregularities and procurement violations. Personnel at several of the activities visited believe that this contract was experiencing problems similar to the ones associated with the CAEDOS contract. For example, as of June 17, 1986, this shipyard was continuing to procure services under the contract even though the contract had expired on September 30, 1985, and had not been modified to extend the period of performance. The shipyard's CAD/CAM program manager agreed with these facts and said NRCC's legal counsel was reviewing this issue.

Selected Activities Report Corrective Efforts

In response to our preliminary observations and questions, several Navy activities reported that they were taking corrective action to better control CAD/CAM procurements. As discussed in the letter, while the reported efforts are positive, additional actions are needed to ensure adequate control over contract obligations and expenditures.

The following corrective actions were initiated by the naval activities we visited.

- The naval shipyards and air rework facilities were reconstructing past contract actions to determine propriety of charges and were developing procedures to monitor contract actions.
- The contracting officer was implementing a plan to assure timely disposition of delivery orders.

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- The COTR was reconstructing past contract actions, with emphasis on maintenance charges and downtime credits.

After our visit, DCASR also began reconstructing a partial reconciliation of payments that, according to DCASR officials, was completed in May 1986. Although DCASR officials agreed that a total reconciliation of the contract was needed, this has not been attempted.

Based on our briefing to you on December 3, 1985, the Navy has taken corrective actions that include (1) requesting the Commander, NAVDAC, to issue an advisory bulletin to remind Navy activities of the requirement to seek additional approvals when contract or project costs exceed the approved cost by 15 percent, (2) sending more contracting people to ADP contracting training, and (3) applying lessons learned from the CAEDOS acquisition to the next CAD/CAM procurement.

Objectives, Scope, and Methodology

GAO's Fraud Hotline received an allegation concerning possible procurement violations on a CAD/CAM contract awarded by the Long Beach Naval Shipyard. On the basis of a limited review, we found merit to the allegation and forwarded it to the Navy for further investigation. The Navy's investigation disclosed contractual irregularities and procurement violations on two contracts. Based on the results of the Navy's investigation, we expanded our review to other naval activities on the west coast. Our objectives were to determine if (1) the CAD/CAM procurement problems extended to other naval activities, (2) the problems could negatively affect future CAD/CAM procurements, and (3) the Navy's management of CAD/CAM acquisition needs to be improved.

We visited shipyards at Long Beach and Mare Island, California, and Puget Sound, Washington; aircraft rework facilities at San Diego and Alameda, California; the Naval Regional Contracting Center, Long Beach, California; and the CAEDOS Program Office, China Lake, California. We also visited the Defense Contract Administration Services' Regional and Management Area offices in Boston, Massachusetts, and the CAEDOS contractor, Computervision Corporation, in Bedford, Massachusetts, to determine what the value of the contract was, how it was administered, and what credits were due the government. In conducting our review, we interviewed key Navy, DCASR, and DCASMA personnel, including commanding officers, comptrollers, contracting officers, CAD/CAM managers, department heads, budget analysts, financial officers, and financial and accounting personnel. We obtained information from the Naval Data Automation Command Headquarters and the Naval Sea Systems Command's Information Systems Improvement Program Office in Washington, D.C.

We did not statistically sample or analyze CAD/CAM contracts. Although we identified CAD/CAM acquisitions under seven contracts with an estimated value of \$122 million, our review primarily focused on the CAEDOS contract because of its significant dollar value and the large number of participating activities. We reviewed Department of Defense and Navy instructions and regulations, applicable legislation, and administrative documentation, contract files, funding documents, delivery orders, payment vouchers, and other related documentation. Our attempt to track and reconstruct contract activity was hampered because procurement regulations had not always been followed and adequate records had not been maintained.

Our review was made in accordance with generally accepted government auditing standards.

Comments From the Assistant Secretary of the Navy for Financial Management



THE ASSISTANT SECRETARY OF THE NAVY
(FINANCIAL MANAGEMENT)
WASHINGTON, D.C. 20350-1000

26 FEB 1986

Mr. Larry Bridges
U.S. General Accounting Office
World Trade Center, Suite 1010
350 South Figueroa Street
Los Angeles, California 90071

Dear Mr. Bridges:

We appreciate the opportunity to respond to the briefing of the Computer Aided Engineering Documentation System (CAEDOS) contract which you provided to me on 3 December 1985. The following comments are provided on the issues you raised:

1. Contract Approvals. The original contract increase from \$27.8 million to \$63 million was not forwarded for approval as requested in my predecessor's original approval letter. The CAEDOS contract was characterized by close competition among several bidders, and it offered extremely high payback to Navy in terms of productivity increases as well as in progress toward standardization and interoperability of Navy Computer Aided Design and Manufacturing (CAD/CAM).

The cost increase from the \$2.6 million which I approved for additional work stations to approximately \$30 million should also have been forwarded for additional approval. In this case, the Naval Data Automation Command granted authority for auxiliary costs associated with the work-station acquisition. That may have been erroneously construed as covering the cost increase.

Subsequent to these two approval actions, we published a new life-cycle management instruction, SECNAVINST 5231.1B of 8 March 1985, which reiterates the need for additional approval when projects exceed costs by 15%, and emphasizes the responsibility of the project manager to report cost growth and of the contracting officer to withhold action on projects which lacks the proper approvals. Enclosure (1) contains a copy of the instruction with the relevant pages highlighted.

In addition, the Chief of Naval Operations has asked the Commander, Naval Data Automation Command to issue an advisory bulletin reminding Navy activities of these requirements. A copy of that letter is at enclosure (2).

2. Administration.

a. Responsible Activity. COMNAVSEASYSKOM is not responsible for the CAEDOS effort. CAEDOS is and always has been a laboratory project managed by the Naval Weapons Center, China Lake. COMNAVSEASYSKOM is only one of several users.

Appendix III
Comments From the Assistant Secretary of
the Navy for Financial Management

PMS 309's only role was acting as a collection point for COMNAVSEASYSKOM requirements being forwarded to China Lake.

b. Administration Problems. Errors in contract administration did occur, as stated in the audit briefing. The China Lake office responsible for administering the contract is aware of some problems and is taking steps to assure they do not continue. When the audit report with specific problems identified is made available to the contracting officer and his technical representative, additional steps will be taken to ensure that the procedures are corrected.

Administration errors are among the most common of all contracting problems. The Department of Defense has been working with contracting organizations in the services to improve training. The Navy has already sent a number of contracting people to automated data processing contracting training. More will be sent to the course the Army has established for multiservice use. As this training becomes more widespread, contract management across Navy should improve.

3. Future Awards. COMNAVSEASYSKOM is responsible for the next major procurement for CAD/CAM. They have reviewed the problems in administering the CAEDOS contract, as described in your briefing, and will apply lessons learned from the CAEDOS acquisition to the impending CAD/CAM procurement.



R H CONN

Encl:

- (1) SECNAVINST 5231.1B
- (2) CNO ltr Ser 945E/6U345218 of 26 Feb 86

Copy to: (w/o encls)
Mr. John Landicchio

Listing of Seven Contracts Under Which Naval Activities Acquired CAD/CAM Equipment and Related Services

Contract number	Award date	Amount	Expiration date	Navy activity serviced
NO0123-81-D-0456	9/23/81	\$99,900,000 ^a	9/30/86 ^b	Labs, ship and aircraft repair facilities, etc.
NO0123-85-D-0292	8/05/85	13,413,874	9/30/85 ^b	Long Beach Shipyard
NO0163-81-C-0059	1/26/81	3,269,833	9/30/84	Aircraft repair facilities
NO0123-80-C-0267	10/01/79	3,553,206	6/30/85 ^c	Long Beach Shipyard
NO0123-82-C-0094	10/05/81	744,455	10/05/86	Long Beach Shipyard
NO0123-82-C-0095	10/05/81	741,055	5/06/86	Mare Island Shipyard
NO0123-84-C-0207	3/01/84	310,308	8/31/84 ^c	Long Beach Shipyard

^aEstimated.

^bDoes not include renewals of all contractual options.

^cThe ASN/FM disapproved extending these contracts further because of contractual and procurement problems.

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