

**GAO**

Report to the Honorable  
Charles E. Bennett, House of  
Representatives

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February 1989

# OMB CIRCULAR A-76

## Contracting Out Public Works Functions at Jacksonville Naval Air Station



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

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General Government Division

B-227365

February 10, 1989

The Honorable Charles E. Bennett  
House of Representatives

Dear Mr. Bennett:

This report responds to your request that we examine the U.S. Navy's decision to contract out the public works functions at the Naval Air Station, Jacksonville, Florida (NASJAX). You were concerned whether implementation of the cost study process (under the Office of Management and Budget [OMB] Circular A-76) leading up to that decision was complete and accurate. In particular, you asked that we review the treatment of costs associated with severance pay and permanent change of station, and whether the contract, if awarded, would cost the government more than it had anticipated.

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## Results in Brief

We found that the work statement prepared by NASJAX for specifying the work to be done under the contract was incomplete and ambiguous due to poor preparation, inadequate review, and overall ineffective management of the cost study process. The Naval Inspector General (IG) in his December 16, 1987, report, reached similar conclusions. For example, the performance work statement (PWS) prepared by NASJAX for this contract (1) omitted significant segments of required work (see pp. 7 to 8), (2) incorrectly classified work (see p. 8), (3) understated the cost of materials (see pp. 8 to 10), and (4) inadequately described tasks to be done (see pp. 10 to 11). As a result, we estimate that over the 3-year life of the contract the government could pay from \$5.21 million to \$8.14 million more than anticipated (see p. 7), and depending on the resolution of apparent ambiguities in the contract, costs could go higher.

The original cost comparison showed that contracting out would yield anticipated savings of \$8.2 million. As a result of the appeals process, this savings figure was reduced to \$6.10 million. Navy officials recognize that their original estimate of savings will not be achieved, but they believe the contract's cost will not increase as much as we estimate and therefore will still save money. Using the Navy's estimated savings of \$6.10 million, and our low estimate of contract cost increase of \$5.21 million, the Navy could still expect to save \$0.89 million over the 3-year life of the contract. However, should our highest estimate of contract cost increase prove more accurate, the Navy could lose \$2.04 million.

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## Background: Chronology of Key Events

OMB Circular A-76—"Performance of Commercial Activities"—provides that agencies (1) study the most efficient way to provide commercial activities using a federal workforce, (2) determine the cost of the most efficient in-house operation, and (3) compare that cost with private sector bids.

In August 1982, at the direction of the Chief of Naval Operations (CNO), NASJAX began an A-76 cost study of all functions being carried out by the Public Works Department to determine whether these functions might be done more economically under contract. These functions include maintenance support for hundreds of buildings, structures, aircraft runways, utilities, and equipment, such as air conditioning and heating systems, located on the 40-year-old, 1,650-acre installation. In 1982, 243 in-house employees provided this maintenance support.

In accordance with A-76, the first step for NASJAX was to develop a PWS that would define the government's requirements. Work on the NASJAX PWS, however, was interrupted in August 1983, when the CNO suspended for 18 months all public works studies involving buildings and structures to collect and analyze work load data. NASJAX decided in April 1984 that its first attempt at preparing a PWS was unsuccessful for the same reason that the CNO had suspended all studies of buildings and structures—incomplete work load data.

In January 1985, at the expiration of the 18-month moratorium on these studies, a newly assigned shops engineer who had been given responsibility for developing the PWS began drafting it using model work statements from other Naval installations and a computer program to extract fiscal year 1985 NASJAX labor hour data. In April 1985, a preliminary draft of the PWS was completed and circulated to six Public Works Department managers for comment. The revised preliminary draft was forwarded for initial review in June 1985 to the Facilities Contracting Authority at the Naval Facilities Engineering Command in Charleston, South Carolina.

In June 1986, Naval Facilities Engineering Command issued a letter approving the PWS as suitable for supporting a request for technical proposals (RFTP) as the first step of a two-step solicitation process. According to the RFTP, all routine work, such as scheduled periodic maintenance as well as recurring work, including minor repairs and service calls, would be bid, in the second step, at a fixed price, while other unscheduled work would be done as indefinite quantity work for which the contractor would be paid extra. However, the PWS established a

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threshold whereby minor repairs incident to periodic maintenance costing more than \$250 for labor and materials, or minor repairs and service call work involving more than \$250 in materials cost or 16 labor hours would be paid extra as unscheduled, indefinite quantity work.

In the meantime, from April 1985 to July 1986, the shops officer who prepared the PWS participated in the NASJAX management study to develop the most efficient organization (MEO)—an A-76 requirement to streamline the in-house operation in order to be more competitive with private sector bidders.

By July 22, 1986, the management study was completed, showing an MEO requiring 205 public works direct labor employees. This was the basis for the NASJAX in-house bid. The PWS and MEO were given to the Naval Audit Service on July 29, 1986, for independent review. The auditors completed the review on October 17, 1986, and recommended that the \$250 threshold for service calls in indefinite quantity work be raised, recognizing a low threshold could result in higher contract costs. NASJAX, however, did not raise the threshold figure because its analysis of a sample of fiscal year 1985 work load data showed that few, if any, tasks would exceed the \$250 threshold.

In November 1986, the Navy issued the RFTP, which contemplated a combination fixed price and indefinite quantity contract for the operation, maintenance, repair, and construction services for buildings, structures, utilities, systems, and equipment at NASJAX. The contract was to be for 1 year with options for 2 additional years. In April 1987, a public opening of bids by technically acceptable offerors was held and the results of the cost comparison were announced. The apparent low bidder was Apex International Management Services, Inc. (Apex), with a low total bid of \$20.4 million versus an in-house estimated cost of \$28.6 million for a projected savings of \$8.2 million over a 3-year contract period.

In June 1987, the International Association of Machinists and Aerospace Workers, the union representing the NASJAX public works employees, filed an appeal alleging the solicitation contained 13 specific flaws. For example, the union named specific buildings, systems, and equipment requiring periodic maintenance and routine service that were omitted from the PWS and alleged that the PWS contained incorrect classification of work that caused private sector bidders to underbid. Pending a decision on recommendations by NASJAX through its chain of command urging cancellation of the solicitation, the appeals officer took no immediate action on the appeal.

During this period, a joint review of the NASJAX PWS was made by the Commander in Chief, U.S. Atlantic Fleet, and the Commander of the Naval Air Force Atlantic Fleet, Norfolk, Virginia, and Naval Facilities Engineering Command, Charleston, South Carolina, to determine whether the solicitation was sufficiently flawed to warrant cancellation. On September 3, 1987, the team concluded that cancellation was appropriate, saying that deficiencies in the PWS resulted in incorrect classification of work, causing the lowest bid to be understated by 26.2 percent; changes required in periodic maintenance would require a 28-percent increase in the level of work; and facilities and systems totaling 42 percent of NASJAX plant value had been omitted. The team recommended cancellation of the solicitation and preparation of a new PWS and resolicitation.

In October 1987, the contracting officer, at the direction of the Assistant Secretary of the Navy for Shipbuilding and Logistics, told Apex that the solicitation was cancelled on the basis of inadequate specifications. The Navy also decided to develop a new PWS that would be adequate for later solicitation. Before the cancellation, however, it was determined that Apex's bid was responsive, Apex was responsible, the bid was fair and reasonable, and that Apex was in line for award of the contract. On October 30, 1987, Apex filed a motion in the U.S. Claims Court for a temporary restraining order to enjoin cancellation of the solicitation. A hearing was scheduled for January 5, 1988.

Meanwhile, on November 2, 1987, the Principal Deputy Assistant Secretary of the Navy for Shipbuilding and Logistics asked the Naval IG to investigate the circumstances surrounding the in-house development of the PWS, reasons for its flaws, and whether any military or civilian officials at NASJAX had intentionally produced a flawed PWS, causing the solicitation to be cancelled. On December 16, 1987, the IG concluded that preparation of the PWS had been poorly managed, but there was no evidence that NASJAX deliberately produced a flawed PWS. The IG also concluded that, while the work in the PWS was understated by an estimated \$3.56 million, it would have been sufficient to support the NASJAX mission.

On January 5, 1988, in an out-of-court settlement, Apex agreed to drop all claims against the United States, and the Navy agreed to withdraw the cancellation of the solicitation and proceed with resolution of the employee union's appeal.

On March 4, 1988, the appeals officer upheld the union appeal on the basis that among other adjustments, the in-house cost estimate inequitably included over \$7.14 million in costs that were not contained in the solicitation and should be deducted from the in-house bid, and that costs associated with a reduction-in-force (RIF) would be \$1.55 million above that allowed in the cost comparison and should be added to the cost of contracting out. The appeals officer concluded that the adjustments necessary to make the cost comparison comparable with Apex's bid would make in-house performance more economical by \$2.31 million.

On March 30, 1988, the CNO, after independently reviewing the appeal, asked the appeals officer to reexamine two elements on which the appeal decision was based: (1) the cost of materials and related personnel costs and (2) the cost of severance pay. On April 13, 1988, the appeals officer agreed with the CNO that \$3.09 million of reductions from in-house materials costs and \$1.93 million in related personnel costs could not be supported within existing A-76 guidelines. The appeals officer also agreed that, on the basis of A-76 procedures, severance costs used in the original cost comparison were valid. These changes, based on A-76 guidelines, would now favor contracting by \$6.1 million. The appeals officer opposed awarding a contract, however, until the PWS was corrected.

Navy officials recognized the PWS was flawed but believed that a contract would still save money. On the basis of (1) the Naval IG report, which concluded that the PWS, though flawed, was sufficient to support the NASJAX mission; (2) the U.S. Claims Court settlement, which had the effect of withdrawing the cancellation of the solicitation and proceeding with the A-76 appeals process; and (3) the final appeals decision, which, based on A-76 guidelines, favored contracting, the CNO authorized NASJAX to award the contract to Apex on April 19, 1988. On May 11, 1988, the International Association of Machinists and Aerospace Workers at NASJAX requested a preliminary injunction in U.S. District Court to prevent the Navy from awarding the contract, claiming that the Navy, by the CNO's action to review and overturn the appeals officer's decision, had violated its own appeals procedures. On May 23, 1988, the Navy moved to have the union's suit dismissed on grounds that the CNO had discretionary authority within existing regulations to review the appeal decision. On June 2, 1988, the suit was dismissed when the presiding judge ruled in favor of the defendants.

## Objectives, Scope, and Methodology

Our objectives were to determine whether the implementation of the cost study had provided a complete and accurate PWS, and whether treatment of severance pay and permanent change of station (PCS) costs in the cost comparison reasonably reflected conditions at NASJAX. To identify omissions and inaccuracies in the PWS, we analyzed the original and revised PWSS (prepared in anticipation of resolicitation) in terms of information on work loads, staffing, labor estimates and standards, and materials usage. To determine whether the contract, if awarded, would result in unanticipated costs, we reviewed the contractor's technical proposal in relation to the differences as specified in the two PWSS. (We did not determine whether the revised PWS was complete and accurate.)

In making our estimates, we recognized that some variables could not be known until completion of the contract. To allow for this uncertainty, we developed high and low estimates for each cost element and did sufficient testing to assure ourselves that they were reasonable. For details of our methodology and calculations, see appendix I. To assess the reasonableness of severance pay and PCS costs, we reviewed OMB, Department of Defense (DOD), Navy, and Office of Personnel Management (OPM) guidelines and rules.

To obtain information about this case, we held discussions with staff at NASJAX; the Naval Facilities Engineering Command in Charleston, South Carolina; the Office of Commander, Naval Air Force, Atlantic Fleet, Norfolk, Virginia; the Naval IG; CNO; and the Assistant Secretary of the Navy for Shipbuilding and Logistics. We also obtained and used the Naval IG report of its investigation of NASJAX.

We did our work between February 1988 and June 1988 and in accordance with generally accepted government auditing standards. We did some selected additional testing in November 1988 to respond to DOD comments on the report. A more detailed discussion of our scope and methodology, including specific calculations, appears in appendix I.

## Incomplete Consideration of Costs

Our analysis showed several major problems with the original PWS and cost study. These problems included work that was omitted, incorrectly classified, and inadequately described. In addition, costs associated with displaced federal workers may have been understated. The sections that follow describe the nature of these problems. Our estimate of costs associated with these problems is shown in table 1. To account for the imprecision in estimating potential costs, this table shows low and high range estimates of potential cost increases.



**Table 1: Summary of Potential Cost Increases**

Dollars in millions	GAO estimates <sup>a</sup>	
	Low	High
	Periodic maintenance omitted	\$1.44
Service call work omitted	.62	.65
Service call work incorrectly classified	2.34	4.35
Understated reimbursable material cost	.81	1.32
PCS cost	.00	.32
<b>Total potential cost increase</b>	<b>\$5.21</b>	<b>\$8.14</b>

<sup>a</sup>See appendix I for details on methodology and calculations.

## Omitted Periodic Maintenance and Recurring Service Work

A major omission in the PWS was work associated with periodic maintenance, such as equipment inspection, lubrication, and minor parts replacement. By comparing the PWS used in the original solicitation with the one developed after bid opening, we found that the original PWS omitted 2,471 line items that would require periodic maintenance, but included 687 line items that were later determined not to require periodic maintenance. This was a net addition of 1,784 line items, or about half of the equipment requiring periodic maintenance that was omitted. Systems and equipment including air conditioning, heating, and electrical systems of entire buildings, such as a Navy Exchange retail store, engine maintenance shop, gymnasium, operations building, electronics maintenance shop, and the housing office, were left out of the original PWS.

As a result, labor hours needed to do periodic maintenance were understated. For example, a Navy Exchange retail store was described as containing only a fire sprinkler system requiring 2 hours of periodic maintenance annually, with no details as to what was to be done. However, the new PWS describes this building as containing 10 radiators, 4 heating coils, 1 instantaneous heater, and 4 split air conditioning systems ranging from 2.5 tons to 30 tons. It also provides 20 pages of detailed information on the type and frequency of tasks to be done. The revised PWS, however, does not provide the estimated labor hours required to do these tasks.

Additionally, there were 143 facilities, equipment, and systems omitted from the original PWS that required recurring service work. Recurring work requires the presence of workers to monitor systems such as boiler and utility plants and to do minor repair and service call work at any facility as needed.

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On the basis of average labor required per item, we calculated it would take an additional 10.6 labor years to do periodic maintenance on the net 1,784 items left out of the PWS. In addition, on the basis of actual records of service calls, we calculated there were 4.57 labor years of recurring work omitted from the PWS.

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**Incorrect Classification of Work**

The contract solicitation contained both a fixed price portion and an indefinite quantity portion of work to be done. The fixed price portion included routine operation of utilities, periodic maintenance of utilities and other systems and equipment, and service call repair work requiring less than 16 hours labor or \$250 materials cost. The indefinite quantity portion included "minor" and "specific" work. Minor work is similar to service calls but over the 16-hour, \$250 materials cost threshold and less than \$2,000 per work item. Specific work refers to jobs between \$2,000 and \$25,000 per job. The RFTP contained 20,468 craft hours of minor work and 55,837 craft hours of specific work.

The preparer of the NASJAX PWS compiled these craft hours from a listing of labor used to do minor and specific jobs during fiscal year 1985. The listing appropriately classified service calls as minor work when they required over 16 labor hours. However, the preparer compiled or included no service call labor hours for which materials costs exceeded the \$250 threshold, and therefore the RFTP contained no craft hours for these service calls.

While the preparer of the PWS believed little, if any, service call work would exceed this threshold, we estimated that there were between 17 and 30 labor years of service call work per year that, by exceeding the \$250 threshold, would escalate into the indefinite quantity portion of the contract and add to its cost.

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**Understated Cost for Materials Reimbursement**

Under the indefinite quantity portion of the contract, the Navy is to reimburse the contractor for the cost of materials used. NASJAX included in the solicitation an estimated cost for indefinite quantity materials, which was to be included as part of the total price of each bidder. The in-house bid contained total estimated materials cost for both fixed price and indefinite quantity work. According to NASJAX officials, the estimate for indefinite quantity materials used was prepared by NASJAX with the guidance and assistance of the Naval Audit Service and the Naval Facilities Engineering Command. However, this estimate was not based on actual indefinite quantity materials usage at NASJAX. As a result, the

estimates were inaccurate and caused contractor bids to be understated by \$0.81 million to \$1.32 million.

The anticipated 3-year contract period was fiscal year 1988 with options through 1990. In determining the cost of materials for indefinite quantity work, the Naval auditors did not use available actual material cost records because they believed these records were incomplete. Instead, materials cost was estimated by applying a rule-of-thumb, 60 to 40 labor-to-materials ratio to the estimated cost of indefinite quantity labor. The resulting figure, projected to the 3-year contract period, was \$4.20 million. This sum appeared in the RFTP as part of prospective contractors' bids.

On the basis of information available at that time, we used two other methods to determine the cost of indefinite quantity materials. We believe either of these methods would have been more accurate than using the 60 to 40 ratio since they are based on actual NASJAX data.

Under one method, actual materials usage data recorded at NASJAX in 1985 (which we obtained but did not audit in detail) showed that 76.2 percent of all materials were for indefinite quantity-type work. Applying the 76.2 percent to the total contract period materials cost of \$7.25 million that the Naval auditors used, we estimated that \$5.52 million rather than \$4.20 million should have been included for the cost of indefinite quantity materials in the bid packages. This method produced bids understated by \$1.32 million.

The second method used NASJAX's actual total materials cost of \$1.93 million for fiscal year 1985. Projected to the contract period, total materials cost would have been \$6.58 million. Using year-end tabulations, NASJAX officials computed the fixed price materials to be \$459,030. We projected this to the contract period, subtracted the fixed price material from the total material cost, and arrived at \$5.01 million for the indefinite quantity cost of materials. Under this method, contractor bids were understated by \$0.81 million.

Table 2 summarizes both of our methods for estimating understated materials cost.

**Table 2: Understated Cost for Reimbursable Materials**

Dollars in millions			
Method	GAO estimate	As bid	Understated bid
Historical 76.2 percentage	\$5.52	\$4.20	\$1.32
Actual usage records	\$5.01	\$4.20	\$0.81

### Unquantifiable Costs Due to Incomplete and Ambiguous PWS

It was not possible to precisely estimate the additional cost for work required but not stated in detail. The original PWS listed 2,877 items of equipment requiring periodic maintenance. However, when NASJAX prepared a new PWS in anticipation of resolicitation, it determined that descriptions of work for 2,075 of these items failed to adequately specify the tasks to be done by the contractor.

The original PWS listed equipment and systems requiring maintenance but did not specify what was to be done. It described the equipment and systems in very general terms, such as "cooling tower, 20-Ton," or "A/C split system, 3-Ton," or "A/C package unit, 5-Ton" to describe air conditioning systems. In one section of the PWS, a large maintenance shop that covers over 800,000 square feet was described as having self-contained, chilled-water air conditioners, but another section shows this maintenance shop containing many different types of air conditioning and air handling systems. The original PWS does not show any details of what is to be done for maintenance on the equipment. However, the new PWS provides detailed descriptions of the equipment and the work steps to be done.

Because the original PWS does not specify exactly what work is to be done, it could leave the Navy vulnerable to interpretation and negotiation by the contractor about what work was intended, how much should be done, and how much of the work exceeds the \$250 threshold for indefinite quantity payment. This could result in higher than anticipated costs for completing the intended work, in addition to the elements shown in table 1.

The Contracting Officer said that if the Navy wants any periodic maintenance or recurring work done that is not contained in the contract specifications, it will have to negotiate with the contractor and pay for the work over and above the contract price. The Contracting Officer further said that the Navy may be liable for any periodic maintenance and recurring work the contractor claims is not specified in sufficient detail

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for it to do what the Navy intended. On the basis of the contract specifications, the Navy also will be liable, under the indefinite quantity portion of the contract, for any repairs and materials exceeding the \$250 threshold.

A contractor may cooperate with the Navy and do all the tasks that may be implied but not specifically defined in the original solicitation. However, a contractor also could file claims against the government due to the poorly defined work in the PWS. In addition, the contract could be difficult to manage and monitor for performance and quality due to its ambiguities and lack of specificity.

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## Cost of Displaced Workers

We were asked to review severance pay and permanent change of station costs used in the cost comparison and consider whether these reasonably reflected conditions at NASJAX. For severance pay used in the cost comparison, OMB and Navy guidelines allow 2 percent of federal personnel cost to be added to contractors' bids. NASJAX calculated an allowable cost of \$105,012, which was used in the cost comparison. The guidelines permit exceptions if they can be fully documented. The guidelines also say, however, that it would be inappropriate to expect that all eligible employees will receive severance pay because most workers find other federal employment. Moreover, OPM guidelines say workers who are offered comparable positions with the contractor are not eligible for severance pay, even if they decline employment or accept any employment with the contractor within 90 days from conversion to contractor operation.

During development of its in-house cost estimates in 1986, NASJAX twice requested a rate higher than 2 percent because three major local installations were making almost identical A-76 studies, and little opportunity for vacancies in these skills existed at these local installations. The CNO denied these requests. In support of the employee appeal, NASJAX simulated a RIF and estimated that of 169 employees expected to be separated by contracting, 124 would be eligible to receive severance pay. NASJAX then assumed that 95 eligible employees would actually receive severance pay at a total cost of \$1.34 million—\$1.24 million above the 2 percent allowed.

The appeals officer initially agreed that the appeal had merit. However, the CNO rejected the exception on the basis of historical experience in which only about 4 percent of the employees assigned are separated and

receive severance pay. The CNO said that employees, unions, and commands typically maximize this element and that simulated RIFs show almost no displaced employees finding new government work. Actual experience shows that costs incurred are significantly lower than original estimates. Our 1985 report entitled DOD Functions Contracted Out Under OMB Circular A-76: Contract Cost Increases and the Effects on Federal Employees (GAO/NSIAD-85-49, Apr. 15, 1985) also documented that of 2,535 employees affected by contracting out, 5 percent were involuntarily separated, not all of whom were eligible to receive severance pay. The appeals officer agreed that, on the basis of A-76 guidelines, the \$105,012 used in the cost comparison was valid. At NASJAX, moreover, the contractor's proposal said recruiting existing Public Works Department employees was its top priority.

The CNO's decision to disallow additional severance pay in the cost comparison appears to be consistent with existing guidelines, historical experience, and the contractor's proposal to recruit NASJAX employees as a top priority.

For PCS costs, Navy instructions allow a 10-percent cost factor to be added to the contractors' bids in the cost comparison and provide for exceptions if fully documented. Following these instructions, NASJAX calculated a PCS cost allowance of \$466,664 for use in the cost comparison.

As with severance pay, NASJAX's requests for an exception based on local conditions twice had been turned down. The calculation of PCS costs in the appeals officer's decision was based on experience at nearby Naval Air Station Cecil Field, which had undergone a RIF of its Public Works Department employees in December 1987. At that location, 14.3 percent of affected employees were given PCS assistance within the first 4 months—the time that NASJAX made its "mock-RIF" calculation—with another 9.5 percent expected in the succeeding 8 months. The total 23.8 percent factor, applied to the 169 affected employees, meant that 40 NASJAX employees might receive PCS assistance. The average cost per employee calculated by NASJAX was \$19,618.45, for a total PCS cost of \$784,738—\$318,094 above that allowed.

Again the appeals officer agreed with the NASJAX justification but the CNO did not. In rejecting the appeal decision, the CNO said that actual experience had been close to standards. The CNO provided examples in which actual PCS moves were less than projected. The CNO recognized, however, that this cost factor is a matter of speculation and cannot be verified or proven until the actual RIF is done.

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We could find no basis to disagree with either the CNO or NASJAX. Both positions have merit. In recognizing both, our low range estimate agrees with the CNO that no additional cost will be incurred. Our high range estimate is based on the NASJAX calculation that additional costs for PCS of \$318,094 potentially could be incurred.

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## Conclusions

As shown in table 1, the combination of omitted and incorrectly classified work, coupled with higher PCS costs, could result in contract cost increases that could range from \$5.21 million to \$8.14 million if the contract remains in effect for its full 3-year life. In addition, there are unquantifiable risks associated, for example, with ambiguous descriptions of work that could be subject to contractor claims and repeated negotiations. Using the Navy's adjusted savings estimate of \$6.10 million and our low estimate of contract cost increase of \$5.21 million, the Navy could still expect to save \$0.89 million over the 3-year life of the contract. However, should our highest estimate of contract cost increase prove more accurate, the Navy could lose \$2.04 million.

In our April 12, 1988, briefing to officials of the Office of the Assistant Secretary of the Navy for Shipbuilding and Logistics, the CNO, and Naval IG, these officials agreed that the contract will have to be negotiated upward, but they expressed confidence that they could negotiate terms that will save money.

While we recognize that the Navy may be able to negotiate favorable terms for some elements of the contract, we believe it may not achieve the savings it anticipated and could incur total costs higher than those that would be incurred by retaining the Public Works Department functions in-house.

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## Agency Comments

In commenting on a draft of this report, DOD agreed that the contract has some deficiencies that may result in some cost increases over the life of the contract, but it did not believe the deficiencies cited would result in cost increases equal to our highest estimate. In its comments DOD said that it believes the Navy's decision to contract out was justified.

The reasons DOD gave for believing that the deficiencies would not result in cost increases equal to our highest estimate were twofold. First, DOD believes that any discussion of the PWS that does not consider the contractor's technical proposal will lead to a disagreement over the nature of deficiencies and the resulting costs. For example, DOD believes that

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omitting some tasks from the RFTP does not mean that the work is necessarily omitted so long as it is addressed in the contractor's technical proposal. However, our review of the RFTP, which also included a review of the contractor's technical proposal, showed that entire systems and buildings had not been included in these documents.

Second, DOD disagreed as to how much of the indefinite quantity work load questioned by us is already provided for in the contract. As a result of DOD's disagreement, we revisited NASJAX in November 1988 to reexamine the records supporting our original estimates; discuss in greater detail how NASJAX had developed its estimates of craft hours for minor and specific work included in the contract; and to reconcile, if possible, our estimates of cost growth with NASJAX's estimates of contract craft hours.

We found that the data system used by NASJAX was incomplete, inaccurate, and unreliable and that the craft hours included in the contract could not be reconciled with the data used. Both the data system and the NASJAX estimate of craft hours understated contract requirements. We discussed the data system with NASJAX personnel who said that the system had been developed expressly for preparing the PWS. They acknowledged that the system was inaccurate and unreliable but said it was the best information available at the time.

After reexamining the Navy's estimates and the documents we used to develop our original estimates, and after holding discussions with NASJAX personnel, we continue to believe that the Navy's estimate of craft hours was understated and that our highest cost estimate for the contract is conservative and perhaps understated. The detailed DOD comments and our evaluation are contained in appendix II.

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As arranged with your office, we will send copies of this report 15 days after its issue date to the staff of former Senator Lawton Chiles and to Senator Bob Graham, who asked to receive the report when completed. We will also send copies to the Secretaries of Defense and the Navy, the Director of the Office of Management and Budget, and other interested parties upon request.



The major contributors to this report are listed in appendix III.

Sincerely yours,

A handwritten signature in black ink that reads "Gene L. Dodaro". The signature is written in a cursive style with a large initial "G" and "D".

Gene L. Dodaro  
Associate Director

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## Abbreviations

Apex	Apex International Management Services, Inc.
CNO	Chief of Naval Operations
DOD	Department of Defense
IG	Inspector General
MEO	Most efficient organization
NASJAX	Naval Air Station Jacksonville
OMB	Office of Management and Budget
OPM	Office of Personnel Management
OSD	Office of the Secretary of Defense
PCS	permanent change of station
PWS	Performance Work Statement
RFTP	Request for Technical Proposals
RIF	Reduction-in-Force



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# Objectives, Scope, and Methodology

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We were asked to examine whether the Navy's decision to contract out the public works functions at NASJAX was proper. More specifically, there was concern that the cost study under OMB Circular A-76 was not complete and accurate and that the contract, if awarded, would cost the government more than anticipated. We were also asked to review whether the costs associated with severance of displaced federal workers were given full consideration in the cost comparison.

We did our work at NASJAX, where we obtained and discussed the Management Study on which the in-house cost estimate was based; the original and revised performance work statements to identify work omissions and other flaws; the contractor's bid and technical proposal for doing the Public Works functions; and the employee union's appeal. We then reviewed, analyzed, and discussed information regarding the cost comparison, historical work loads, backlogs, staffing, labor estimates and standards, historical materials usage, and other service contracts. We also reviewed the results of a simulated reduction-in-force (RIF) done by the Consolidated Civilian Personnel Office at NASJAX that it used to estimate numbers of employees who might be eligible for and likely to receive severance pay and permanent change of station assistance. Our review also took into account the assumptions on which their estimates were based.

At the Office of the Naval IG, Washington, D.C., we obtained, reviewed, and discussed its Report of Investigation entitled Analysis of NAS Jacksonville Recommendation to Cancel Solicitation N-62467-87-R-0010, together with supporting documentation. We did not independently verify all of the information included in the report.

We obtained background information from, and discussed our findings and conclusions with, officials at NASJAX, Southern Division, Naval Facilities Engineering Command; Naval Air Force Atlantic Fleet; and with others in the offices of IG, CNO, and Assistant Secretary of the Navy for Shipbuilding and Logistics. We also discussed our findings with officials of the DOD IG and the DOD Commercial Activities Office.

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## Methodology for Estimating Contractor Wage Rates

In order to estimate the potential cost increase for omissions and incorrectly classified work, we developed, with the assistance of the Naval Facilities Engineering Command, a weighted average contractor wage rate of \$13.16 per hour. We used a weighted average to account for differences in crafts, their wage rates, and numbers of hours expected to be worked. We then increased this weighted base rate by applying FICA,

workers' compensation insurance, materials, overhead, and profit to estimate an average applied hourly rate, as shown below:

**Table I.1: Average Applied Hourly Rate**

	\$13.16 Average Base Rate
$13.16 \times 0.07125 =$	0.94 (FICA)
$13.16 \times 0.015 =$	0.20 (workers' compensation)
$13.16 \times 0.30^a =$	3.95 (materials)
$13.16 \times 0.10^a =$	1.32 (overhead)
$13.16 \times 0.10^a =$	1.32 (profit)
<b>Average applied hourly rate =</b>	<b>\$20.89</b>

<sup>a</sup>Rates provided by Naval Facilities Engineering Command.

The average applied hourly wage rate of \$20.89 was annualized to determine the annual rate of \$43,451 ( $\$20.89 \times 2,080$  workhours per year). As corroboration, we asked the Facilities Engineering Command to provide examples of actual applied rates for similar operations at other installations. The command provided four examples showing annual contractor rates ranging from \$37,500 to \$50,000 and one in-house example showing a rate of \$43,835, with an overall average of \$43,450.

To develop high and low range cost estimates, we assumed different wage rates on the basis of differences in vacation pay.<sup>1</sup> One rate was based on employees receiving 11 paid holidays but no paid vacation ( $2,080 - 88 = 1,992$  hours per year), and the other was based on employees receiving 88 hours of holiday pay plus 80 hours of vacation pay ( $2,080 - 168 = 1,912$  hours per year). This produced effective hourly wage rates as follows:

Average applied annual rate of \$43,451 divided by 1,992 = \$21.81 per hour.

Average applied annual rate of \$43,451 divided by 1,912 = \$22.73 per hour.

The effective annual rates were:

<sup>1</sup>Under a Department of Labor Wage Determination, contractors are required to pay their employees for 11 holidays, but they are not required to pay vacation leave during the first year of employment. The second through the 10th year, contractors are required to pay 2 weeks vacation, and 3 weeks after 10 years.

$\$21.81 \times 2,080 = \$45,365$  (11 paid holidays, no vacation)

$\$22.73 \times 2,080 = \$47,278$  (11 paid holidays, 2 weeks paid vacation)

These rates were used in all of our calculations to convert labor hours or years to high and low cost estimates.

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## Potential Cost of Omitted Work

To estimate the potential cost of omitted work, we (1) used the number of line items omitted as calculated by NASJAX officials, who compared the original PWS with a more detailed and revised version prepared in anticipation of resoliciting (we did not verify these calculations); (2) determined average labor per line item by dividing total standard hours in the original PWS by the number of line items (35,454 by 2,877 = 12.32); (3) converted the result to labor years; and (4) determined the potential cost increases by multiplying estimated labor years by estimated contractor labor rates that we calculated.

For periodic maintenance (commonly referred to as preventive maintenance) the original PWS omitted 2,471 line items, but it contained 687 line items later determined not to need periodic maintenance. The net effect was the omission of 1,784 line items requiring an average of 12.32 labor hours for periodic maintenance each per year, or 10.6 labor years. Applying the estimated effective contractor annual wage rates and extending to a 3-year contract period, the value of the omitted periodic maintenance work ranged from a low of \$1,442,607 to a high of \$1,503,440.

In the area of omitted service call work, the technical exhibit in the PWS did not include 143 structures and facilities. To estimate cost ranges for these omissions, we used actual service call information from fiscal year 1985, as compiled by NASJAX personnel. They identified 9,498 labor hours, or 4.57 labor years, omitted. Again using estimated effective contractor annual wage rates, we estimated the high and low ranges as follows:

High  $(4.57 \times \$47,278) \times 3 \text{ years} = \$648,181$ .

Low  $(4.57 \times \$45,365) \times 3 \text{ years} = \$621,954$ .

---

## Potential Labor Cost for Incorrectly Classified Work

Service work includes maintenance, repairs, replacements, minor construction, and alterations and was intended to be part of the fixed price portion of the contract. Service call work in excess of 16 labor hours or \$250 materials cost, however, would be paid under the indefinite quantity portion of the contract, over and above the fixed price.

Using NASJAX Public Works Department actual material cost records for fiscal year 1985, we determined that there were 928 service calls in which the total materials cost was over \$250. Because the job order cost accounting system at NASJAX did not record labor for service calls under 16 hours, we were not able to determine the labor cost associated with these service calls. To determine the cost of labor, we first determined the cost of materials associated with the 928 service calls identified for fiscal year 1985. This totaled \$780,148, or \$2,340,444 for 3 years. We then applied two labor-to-materials ratios to obtain the high and low cost ranges. One was a 65 to 35 ratio provided to us by the Naval Facilities Engineering Command, and the other was a 50 to 50 ratio, which we used on the premise that service calls with high materials content might be more materials cost-intensive than the 65 to 35 ratio. We believe this rationale is reasonable because information at NASJAX showed that indefinite quantity-type tasks in fiscal year 1985 had been about 48 percent materials cost-intensive.

High ( $\$2,340,444$  divided by 0.35)  $\times$  0.65 =  $\$4,346,539$ , and approximately 30 labor years per year.

Low ( $\$2,340,444$  divided by 0.50)  $\times$  0.50 =  $\$2,340,444$ , and approximately 17 labor years per year.

---

## Potential Cost for Reimbursable Materials

The Navy is to reimburse the contractor for the cost of materials used in doing indefinite quantity work. The contractor pays for all materials used under the fixed price portion of the contract. Due to assumptions and calculations by the Naval Audit Service and Naval Facilities Engineering Command, all contractor bids were understated in the category of reimbursable materials. We developed two estimates of understated materials.

Using the same financial data and inflation factors as the Navy auditors, showing total fiscal year 1985 materials usage by NASJAX of \$2,121,228, the total dollar value for materials during the 3-year contract period of 1988 through 1990 would be \$7,251,192. We did not verify the accuracy of the inflation factors the auditors used. We then applied the actual

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fiscal year 1985 NASJAX data in which 76.2 percent of all materials supported indefinite quantity-type work. This yielded a reimbursable materials cost estimate of \$5,525,408 for 3 years. This figure could have been included in the solicitation as reimbursable materials, rather than \$4,204,512 actually used in contract bids. This method produced a bid understated by an estimated \$1,320,896.

On the basis of actual material usage recorded at NASJAX during fiscal year 1985, the \$1,925,179 estimate was projected for the 1988 through 1990 contract period using the same inflation factors as the other method. This produced a 3-year total materials cost of \$6,581,019. We then used NASJAX tabulations of fiscal year 1985 fixed price-type materials of \$459,030 and projected this to the contract for a 3-year total of \$1,569,145. The difference of \$5,011,874 could have been included as the government's estimate for reimbursable materials cost instead of the \$4,204,512. This method produced an estimated understatement of \$807,646.

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### Potential Cost of Displaced Workers

To assess the reasonableness of severance pay and PCS cost used in the cost comparison, we reviewed OMB, DOD, Navy, and OPM guidelines and rules and compared the results with a simulated reduction-in-force done at NASJAX. We then reviewed the logic of assumptions made about the probable number of employees likely to receive severance pay and PCS assistance and compared this with historical experience. We also reviewed the contractor's proposal with regard to the likelihood that any displaced NASJAX employees would receive offers of comparable employment with the contractor. This has potential for adding \$318,094 to the cost of contracting, as discussed on pages 11-13.



# Comments From the Department of Defense

Note: GAO comments supplementing those in the report text appear at the end of this appendix.



ASSISTANT SECRETARY OF DEFENSE  
WASHINGTON, D.C. 20301-8000

PRODUCTION AND  
LOGISTICS

NOV 30 1988

Mr. Frank C. Conahan  
Assistant Comptroller General, National  
Security and International Affairs Division  
US General Accounting Office  
Washington, D.C. 20548-0000

Dear Mr. Conahan:

This is the Department of Defense (DoD) response to the General Accounting Office (GAO) second revision of its draft report, "OMB CIRCULAR A-76: Navy's Decision to Contract Out the Public Works Functions at Jacksonville Naval Air Station" dated October 25, 1988 (GAO Code 410538/OSD Case 7728). The Department of Defense partially concurs with the subject report. The Department recognizes the Jacksonville contract has some deficiencies that may result in some cost increases over the life of the contract. The DoD does not, however, agree that the deficiencies cited may result in the GAO worst case scenario. The difference in estimates between the GAO and the DoD derives to a large degree from disagreements in estimating procedures and from differing interpretations concerning the contractual requirements. In the final analysis, after the corrective action was taken, the decision to contract was justified.

The detailed DoD comments on the revised draft report findings are provided in the enclosure (suggested technical changes were separately provided). The Department appreciates the opportunity to comment on the draft report.

Sincerely,

A handwritten signature in cursive script, appearing to read "Merle Freitag".

Merle Freitag, MC, USA  
Military Deputy

Enclosure

See discussion on pp. 13-14.

Appendix II  
Comments From the Department of Defense

GAO DRAFT REPORT - DATED AUGUST 5, 1988  
(GAO CODE 410538) OSD CASE 7728

"OMB CIRCULAR A-76: Navy Decision to Contract Out  
the Public Works Functions at Jacksonville Naval Air Station"

DEPARTMENT OF DEFENSE COMMENTS

\* \* \* \* \*

FINDINGS

- o FINDING A: Background: Contracting Out Of Public Works Functions At Jacksonville, Florida Naval Air Station. The GAO pointed out that OMB Circular A-76, "Performance of Commercial Activities," provides that agencies (1) study the most efficient way to provide commercial activities using a Federal workforce, (2) determine the cost of the most efficient in-house operation, and (3) compare that cost with private sector bids. The GAO noted that, in August 1982, the Naval Air Station, Jacksonville, Florida (NAS JAX) initiated an A-76 cost study of all functions being carried on by the Public Works Department to determine whether these functions might be done more economically under contract. The GAO further noted that the Public Works functions included maintenance support for hundreds of buildings, structure, aircraft runways, utilities and equipment (such as air conditioning and heating systems) located on the 40 year old, 1,650 acre installation. The GAO reported that, in 1982, 243 in-house employees provided this maintenance support. The GAO explained that, in accordance with A-76, the NAS JAX began developing a Performance Work Statement (PWS) to define the Government requirements, but work was interrupted when the Chief of Naval Operations (CNO) suspended all public work studies involving buildings and structures for 18 months in order to collect and analyze workload data. The GAO reported that:
  - in early April 1984, the NAS JAX decided its first attempt at preparing a PWS was unsuccessful because of incomplete workload data;
  - in January 1985, at the expiration of the 18 month moratorium, another attempt to prepare a PWS was initiated; and
  - in June 1986, the Naval Facilities Engineering Command issued a letter approving the PWS as suitable for supporting a request for technical proposal (RFTP) for contracting. (pp. 2-10/GAO Revised Draft Report)

Now begins on p. 2.

Enclosure

Appendix II  
Comments From the Department of Defense

oo DoD RESPONSE: Concur.

o FINDING B: Inadequate Performance Work Statement. The GAO reported that, in November 1986, the Navy issued a combination fixed price and indefinite quantity solicitation (RFTP) for the operation, maintenance, repair and construction services for buildings, structures, utilities, systems and equipment at the NAS JAX. The GAO found that a joint review of the NAS JAX PWS, made by the Commander in Chief, U.S. Atlantic Fleet, the Commander, Naval Air Force Atlantic Fleet, and the Naval Facilities Engineering Command, Charleston, concluded that the PWS was sufficiently flawed to warrant cancellation of the solicitation. According to the GAO, a subsequent review by the Naval Inspector General concluded that the preparation of the PWS was poorly managed and, while work included in the PWS was understated by an estimated \$3.56 million, it was nonetheless sufficient to support the NAS JAX mission. In March 1988, an appeal officer concluded that \$8.37 million should be deducted from the in-house cost to make it comparable with the contractor bid, making in-house performance more economical. The GAO concluded that, despite the recognition that the PWS was flawed, the Navy believed that the contract would save money. The GAO reported that, on April 19, 1988, the Chief of Naval Operations (CNO) authorized contract award based on (1) the Navy IG report, which concluded that the PWS, though flawed, was sufficient to support the NASJAX mission, (2) the U.S. claims court settlement which relied on the equity of the A-76 appeals process, and (3) the final appeals decision, which favored contracting. (pp. 2-9/GAO Revised Draft Report)

Now begins on p. 2.

oo DoD RESPONSE: Partially Concur. The GAO draft report description of events surrounding the Navy decision-making process is ambiguous in two key areas; the description of the appeal process and role of the U.S. Claims Court settlement agreement. The report explicitly notes that "the appeal officer concluded that by deducting \$8.37 million from the in-house cost... in-house performance would be more economical." The GAO discussion of the appeal officer adjustments after the CNO requested re-examination of two elements in the initial appeal decision is less explicit. The re-examination resulted in the restoration of \$3.09 million in material costs and \$1.93 million in related personnel costs. It also resulted in the restoration of \$1.55 million in one time conversion costs and some other minor adjustments. Together, these adjustments resulted in a decision favoring contract performance. While the appeal officer opposed awarding the contract because of problems he saw with the Performance Work Statement, his response to the CNO noted that re-examination of the two elements resulted in a decision under A-76 procedures favoring contract performance.

See comment 1, p. 31.

Now on p. 5.

See comment 2, p. 31.

Now on p. 5.

See comment 3, p. 31.

The U.S. Claims Court settlement between Apex International and the Government required the Navy to rescind the cancellation of the solicitation. This action had the effect of requiring the completion of the interrupted appeal process. Under OMB Circular A-76, award of the contract is required if the appeal decision favors contract performance. Prior to entering into this agreement, Navy officials had determined that the statement of requirements addressed in the request for technical proposals (RFTP) and in Apex technical proposal were sufficient to support the NAS JAX mission if a contract were awarded. Given these circumstances, the Navy authorized award of the contract to Apex on April 19, 1988.

Throughout the report, the GAO refers to the PWS, comparing the original PWS with the more detailed, revised PWS later developed by the NAS JAX. In fact, the requirements portion of the RFTP, the original PWS in the GAO terminology, cannot be viewed separately without the contractor technical proposal. Under the terms of the RFTP, the contractor technical proposal also becomes a binding part of the contract. Thus, any discussion of the inadequacies of the PWS that does not consider the contractor's proposal will lead to a disagreement over the nature of the deficiencies and the resulting costs. The DoD acknowledges that omissions and imprecisely described work requirements may result in an increase in the cost of contracting. The DoD does not, however, agree with the worst case increases projected by the GAO.

- o FINDING C: Incomplete Cost Consideration. The GAO reported a number of major problems with the PWS and the cost study, finding the work statement to be incomplete and ambiguous due to poor preparation, inadequate review and ineffective management of the cost study process. The GAO found that the NAS JAX PWS:

- omitted significant segments of required work;
- incorrectly interpreted and classified work;
- understated the cost of materials; and
- inadequately described tasks to be performed.

The GAO concluded that the faulty PWS could result in the Government paying between \$4.85 million and \$7.46 million more than anticipated over the 3-year life of the contract, and potentially even more because of ambiguities in the contract, possibly offsetting projected savings of \$6.1 million. The GAO further concluded that, if the higher estimate is realized, contract costs will exceed those that would be incurred by retaining the Public Works Department functions in-house. (pp. 1-2/GAO Revised Draft Report)

Appendix II  
Comments From the Department of Defense

See comment 4, p. 31.

See comment 5, pp. 31-33.

Now on pp. 7-8.

See comment 4, p. 31.

- oo DoD RESPONSE: Partially concur. The DoD acknowledges that omissions and imprecisely described work requirements may result in a contract cost increase. It is the DoD position, however, that any such adjustments will not result in the higher GAO estimate. The different GAO and DoD estimates derive principally from two factors: one, a disagreement over the effect the contractor's technical proposal, which is a part of the contract, will have on the definition of requirements (discussed in more detail in the DoD response to Finding B); and two, a disagreement as to how much of the indefinite quantity workload is already reflected in the contractual requirement for 20,468 craft hours of Service Contract Act work and for 55,837 craft hours of Davis Bacon Act work.
  
- o FINDING D: Work Omitted From The Performance Work Statement. The GAO reported that the PWS omitted 1,784 line items or about half of the equipment requiring periodic maintenance. According to the GAO, the omissions include the air conditioning, heating and electrical systems maintenance in a number of buildings, resulting in the understatement by \$1.44 to \$1.5 million in labor costs required to perform periodic maintenance. The GAO further reported that the PWS also omitted recurring service work for 143 facilities, equipment and systems, which the GAO calculated translates to an omission of 4.57 labor years, equalling approximately \$620,000 to \$650,000. (pp. 12-15/GAO Revised Draft Report)
  
- oo DoD RESPONSE: Partially concur. The DoD acknowledges that omissions may increase the contract cost. The DoD disagrees, however, on the extent of these omissions and the increased costs that may result. The specifications outlined in the RFTP are performance specifications written for entire systems, which by nature are not detailed and which rely upon the technical proposal to completely define the requirement. (See the DoD response to Finding B for a more detailed discussion of this issue.) The new PWS, which the GAO compared against the RFTP, is a performance/task-oriented specification and discusses the components of each system in minute detail. The fact that some items in the new PWS were not included in the RFTP does not mean that all such work is necessarily omitted insofar as it is addressed in the technical proposal, which, along with the RFTP, defines the contractual requirements.

See comment 5, pp. 31-33.

- o FINDING E: Incorrect Interpretation and Classification of Work. The GAO reported that the contract, is comprised of (1) a fixed price and (2) and indefinite quantify portion. The GAO estimated that between 15 to 26 labor years of recurring service call work (items exceeding the 16 hour and \$250 thresholds) would fall into the indefinite quantity portion of the contract. The GAO estimated that this work could cost an additional \$1.98 to \$3.67 million. (pp. 15-16/GAO Revised Draft Report)

DoD RESPONSE: Partially concur. The DoD disagrees on how much of this incorrectly categorized indefinite quantity workload is already reflected in the contractual requirement for 20,468 craft hours of Service Contract Act work and for 55,837 craft hours of Davis Bacon Act work.

- o FINDING F: Understated Costs For Material Reimbursement. The GAO reported that NAS JAX cost estimates for materials used were inaccurate because they (1) were not based on actual materials usage experience and (2) used questionable inflation assumptions. The GAO found that the Navy applied a 60/40 labor to materials ratio to estimate material usage, when more accurate methods could have been used. The GAO estimated that these errors caused contractor bids to be understated by \$0.81 to \$1.32 million. (pp. 16-18/GAO Revised Draft Report)

Now on pp. 8-10.

- oo DoD RESPONSE. Concur. The DoD notes that the estimate used in the cost comparison represented a valid approach to identifying material costs, given the incomplete and unverifiable nature of the information available at that time. Additional data developed since the comparison indicates that material cost during the comparison period may vary from the earlier estimate, particularly the proportions of reimbursable and nonreimbursable material. Given this additional information, the GAO estimate of the cost for reimbursable material is reasonable.

- FINDING G: Unquantifiable Costs Due To Incomplete And Ambiguous PWS. The GAO found that it was not possible to precisely estimate the additional cost for work required but not stated in sufficient detail to hold a contractor liable. The GAO reported that the PWS work descriptions inadequately specified the tasks to be performed in 2,075 of 2,877 line items. The GAO found that the PWS listed the equipment and systems requiring maintenance, but did not specify what was to be done. The GAO concluded that the lack of specificity leaves the Navy vulnerable to higher than anticipated costs for work due to contractor uncertainty about what work was intended, the extent of the work and how much falls under the fixed price portion of the contract. The GAO further concluded that any unspecified work would have to be negotiated with the contractor and paid for above the contract price. The GAO also concluded that the contractor could file a claim against the Government due to the poorly defined work descriptions. They further concluded that contract could be difficult to manage and performance and quality difficult to measure, due to the ambiguities. (pp. 19-21/GAO Revised Draft Report)
- DoD Response: Partially concur. The DoD acknowledges that omissions and imprecisely described work requirements will result in a contracting cost increase. The DoD disagrees, however, on the extent to which the unspecified work would have to be negotiated with the contractor and paid for above the contract price. (See the DoD response to Findings B and C, as it pertains to the disagreement over the effect that the contractor's technical proposal will have, along with the specifications in the RFTP, in determining the contractual requirements. Also, see the related discussion on performance specifications versus more detailed, task-oriented specifications in the DoD response to Finding D.)
- FINDING H: Cost of Displaced Workers Severance Pay. The GAO reported that both Office of Management and Budget (OMB) and Navy guidelines allow 2 percent of Federal personnel cost to be added to the contractor bids for severance pay. According to the GAO, the NAS JAX twice requested that the percentage be increased, but the Chief of Naval Operations (CNO) denied the request. The GAO concluded that the Navy decision to disallow additional severance pay in the cost comparison is consistent with existing guidelines, historical experience, and the contractor proposal to recruit NAS JAX employees as a top priority. (pp. 21-23/GAO Revised Draft Report)
- DoD RESPONSE: Concur.

See comment 4, p. 31.

Now on pp. 11-12.

Appendix II  
Comments From the Department of Defense

- FINDING I: Cost of Displaced Workers--Permanent Changes of Station (PCS). The GAO reported that Navy instructions allow a 10 percent cost factor for PCS cost to be added to the contractor bids in the cost comparison. The GAO found that the NAS JAX requested an exception to increase the percentage based upon local conditions, which the CNO denied on the basis actual experience with the PCS costs has shown them to be close to the 10 percent standard. The GAO concluded that it had no basis to disagree with either the NAS JAX or CNO position on the PCS, noting both had merit. In recognizing both, however, the GAO low range estimate agreed with the CNO that no additional cost will be incurred due to PCS (pp. 23-24/GAO Revised Draft Report)

- DoD RESPONSE: Concur.

RECOMMENDATIONS

- None.

Now on pp. 12-13.



The following are GAO's comments on the Department of Defense's October 17, 1988, letter.

## GAO Comments

1. We agree that our presentation of the appeal process may not have been clear and we therefore have clarified the description of these events. (See p. 5.)
2. We disagree that the report is ambiguous as to the role of the U.S. Claims Court settlement. Both our report (on p. 4) and DOD's objection state that the settlement rescinded the cancellation of the solicitation, thus requiring completion of the interrupted appeal process. While the U.S. Claims Court proceedings delayed the appeal process, it did not alter the appeal decision.
3. We agree that the RFTP should be considered in the context of the contractor's technical proposal. As stated, first on page 6 and later on page 18, we fully considered the contractor's technical proposal as it related to work described in the RFTP. Our detailed comments on DOD's assertion that our estimates were not accurate are discussed in comments 4 and 5.
4. One of the reasons DOD gave for disagreeing with our cost estimates is a disagreement over the effect of the contractor's technical proposal on the definition of the contract's requirements. We carefully reviewed both DOD's RFTP and the contractor's technical proposal and found that the original PWS omitted 2,471 line items of equipment requiring periodic maintenance, but it included 687 line items that did not require periodic maintenance, for net omissions of 1,784 specific line items of equipment. Similarly, 143 buildings and facilities were omitted that require routine maintenance. According to the contractor's technical proposal, any omissions would be identified through physical inventories and condition inspections of facilities, systems, and equipment, and any resulting work would be negotiated. We estimated that these omissions, when taken together, would add up to \$2.06 million to \$2.15 million in additional costs.
5. The second reason DOD gave for disagreeing with our cost estimate centers on whether the indefinite quantity work load we questioned is already provided for in the contract. The contract included 20,468 craft hours of minor work and 55,837 craft hours of specific work. As a result of DOD's comment concerning our highest estimate, we reexamined the evidence we used to derive our estimates, discussed in greater detail how NASJAX had developed its estimates of craft hours for minor and

specific work included in the contract, and attempted to reconcile our estimates of cost growth with NASJAX's estimates of contract craft hours.

We determined that the craft hours included in the contract could not be reconciled with the data system used by NASJAX to develop those craft hours. For example:

- The data system contained 3,892 more craft hours of minor work than were included in the contract.
- The data system contained 8,150 craft hours of minor work for service calls exceeding 16 hours of labor, but NASJAX personnel could not agree as to whether any of these craft hours were actually included in the contract.
- Of a total of 1,687 jobs listed in the NASJAX data system, the system did not show the amount of labor used to do 464 minor jobs. On the basis of the overall average labor per minor job of 37.3 hours, the data system, and consequently the contract, understated minor work by an estimated 10,700 craft hours.
- The data system included no labor for service calls based on the \$250 materials cost threshold. We identified 928 of these service calls for which we originally estimated labor costs to increase the contract cost by a range of \$1.98 million to \$3.67 million. According to the PWS, these service calls should have been included in the contract. DOD believed that some of the service calls that we included in our estimate duplicated some contained in the NASJAX data system. In our follow-up work, we were able to trace over 1,800 transactions from the NASJAX data system to the documents we had originally used in deriving our estimate. We found one transaction that was duplicated. However, in the course of this additional work, we identified 2 to 4 labor years of additional service calls that exceeded the \$250 criteria and had not been included in our estimate. On the basis of these additional calls, we increased our low estimate to \$2.34 million and our highest estimate to \$4.35 million. These revised estimates now appear in table 1 on page 7.

We discussed the data system with NASJAX officials who said that it had been developed expressly for preparing the PWS. They agreed that the system was inaccurate and unreliable, but they said it was the best information available at the time.

After reexamining the Navy's estimates, discussions with NASJAX personnel, and the documents we used to develop our original estimates, we believe that the Navy's estimate of craft hours was understated and that

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our highest cost estimate for the contract is conservative and perhaps understated.

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# Major Contributors to This Report

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