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Report to the Congress; by Elmer B. Staats, Comptroller General.

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Quality Mfg., Inc., Eastaboga, AL; Western Lift Truck, Inc.
Congressional Relevance: Congress.

An examination of contracts for repair and overhaul of Government property revealed the need for improvement. GSA awarded "time and materials" contracts, which call for specified rates for labor performed, amounting to \$24.4 in fiscal year 1975. Findings/Conclusions: Improper charges were found in eight contracts audited by GAO. Overhead labor charges were improperly added to contract costs. Many contractors failed to show how Government-furnished material was used, and some billed GSA for materials not used on orders. GSA did not question contract ceilings based on contractors' estimates, and failed to follow up results of audits on improper billings. GSA was in general agreement with GAO findings and has initiated action to collect \$464,000. Recommendations: The Administration of GSA should: establish procedures to prevent overcharges on "time and material" contracts, obtaining more staff if necessary, followup on matters uncovered in GSA audit reports; and review contracts to determine needs for further audits. (HTW)

REPORT TO THE CONGRESS



*BY THE COMPTROLLER GENERAL
OF THE UNITED STATES*

Administration Of Repair Contracts Needs Improvement

General Services Administration

In fiscal year 1975 various contractors repairing equipment for the Government were paid \$24.4 million that included substantial overcharges.

GAO audited eight contracts and in every case found improper charges. As a result, action has been started by the General Services Administration to collect \$464,000, and further collections are expected. A series of corrective actions has been promised.



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20546

B-146929

To the President of the Senate and the
Speaker of the House of Representatives

This report identifies ways to improve contracting for
the overhaul and repair of Government property.

Our review was made pursuant to the Budget and Account-
ing Act, 1921 (31 U.S.C. 53), and the Accounting and Audit-
ing Act of 1950 (31 U.S.C. 67).

We are sending copies of this report to the Director,
Office of Management and Budget; the Secretary of Defense;
the Administrator of General Services; and the Secretaries
of the Navy and the Air Force.

A handwritten signature in black ink, reading "Thomas R. Atchell".

Comptroller General
of the United States

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ABBREVIATIONS

GAO	General Accounting Office
GSA	General Services Administration

D I G E S T

In contracting for repair and overhaul of equipment, Federal agencies frequently use "time and material" contracts. Under such contracts, the Government agrees to pay a specified rate for each hour of direct labor performed. The specified hourly rate includes labor cost, overhead, and profit. Contractors are provided material by the Government or are to be reimbursed for material on the basis of costs incurred.

It is clear that under such contracts the contractors do not have an incentive to hold labor hours to a minimum because each hour charged to the contract adds to the contractors' profit and recovery of overhead charges.

There are more desirable types of contracts than time and material contracts, but in some circumstances there is no alternative to using these contracts. In view of the undesirable characteristics of these contracts, Government regulations emphasize that surveillance must be more stringent and extensive than on other types of contracts and that a ceiling should be established on costs to be incurred on each job. GAO audited eight of the time and material contracts performed by four contractors. (See app. I.)

FINDINGS

The contract ceilings established were generally based on contractors' estimates, were not questioned by General Services, and did not serve their intended purpose. General Services' management failed to follow up on the results of internal audit reports dealing with improper billings. Appropriate corrective action at the time would have prevented many of the problems GAO found. (See ch. 3.)

GAO found that labor totaling \$124,000 performed by employees not directly engaged in performance of repair orders was charged to contracts with the General Services Administration, even though such costs were covered by overhead charges and the contracts specifically stated only direct labor was an allowable charge. For example:

- Mikelco Incorporated charged \$2,907 for indirect labor on one repair order, 11 percent of total labor charged. The charge was supported with time cards for a bookkeeper, a purchasing agent, and two clerks.
- Midwest Maintenance and Construction, Incorporated, charged \$688 on a repair order, but the time cards were for employees not engaged in direct performance of the work. Charges for indirect labor were 13 percent of total labor charged. (See p. 6.)

Contract billings to General Services contained charges for labor which was not actually worked or which was devoted to other than contract work. For example:

- Mikelco charged 4,758 labor hours, \$28,837 for employees at a plant in one State to five repair orders being worked at a plant in another State. (See p. 6.)
- Quality Manufacturing, Incorporated, billed the Government for 92 hours including 41 hours which were erroneously charged after the work was completed. (See p. 6.)

A number of contractors located in region 7 ordered and received about \$2.2 million of Government-furnished materials during 1974 and 1975. These contractors were responsible for keeping accountable records of Government-furnished material in their possession. In some cases, GAO could not determine from the contractors' records how the material was actually used. The following conditions found at Mikelco, Inc., illustrate this condition:

- 360 paint brushes were charged to an item that was not painted.

--10 boxes of nails were charged to a job on which no carpentry had been done.

--48 gallons of red paint and 40 gallons of black paint were charged to an item which was painted yellow.

--150 sheets (4,800 square feet) of plywood were charged to a job which required only a small amount of lumber. (See p. 10.)

Contractors sometimes billed General Services for materials which were not used on the repair orders billed. For example:

--Mikelco charged two repair orders with 760 gallons of gasoline, most of which was used for other purposes including use in company vehicles.

--Midwest charged materials used to remodel its plant as direct materials to orders for the repair of Government equipment. (See p. 7.)

GAO did not determine the total overcharges but referred the matter to General Services for detailed review and collection.

CONTRACTOR COMMENTS

The contractors were given the opportunity to comment on GAO's findings when the work at each location was concluded. Mikelco did not provide comments. The other three agreed with some of GAO's findings and disagreed with others. For example, Midwest believes the definition of indirect labor contained in its contracts with General Services is open to various interpretations. Its comments were considered during report preparation.

AGENCY COMMENTS AND ACTION

General Services stated that it was in general agreement with GAO's report and that actions were being taken to correct the deficiencies. (See app. II.)

General Services also advised GAO that, on the basis of partial audits, actions have

been started to collect \$464,000 in identified overcharges and further collections are expected.

RECOMMENDATIONS

GAO recommends that the Administrator of General Services establish procedures adequate to assure that the Government is not overcharged on time and material contracts. GAO recognizes that this may require an increase in staff, and, if people are not available, General Services should consider requesting assistance from the Defense Contract Administration Services and the Defense Contract Audit Agency.

GAO recommends also that procedures be established to followup with appropriate action on matters uncovered in General Services internal audit reports. Furthermore, General Services should review all of its remaining time and material contracts to determine whether detailed audits and recovery of improper billings are needed.

CHAPTER 1

INTRODUCTION

In fiscal years 1974 and 1975, Federal agencies paid about \$42.5 and \$57 million, respectively, for the rehabilitation of various types of equipment under contracts awarded and administered by the General Services Administration (GSA). Each of 10 GSA regional offices (see app. III) award these contracts, and the Federal agencies located within those GSA regions are generally required to use the contracts in obtaining repairs.

Repair services for certain property, such as aircraft support equipment, construction equipment, and material-handling equipment, are obtained by awarding "time and materials" contracts. These contracts, which call for payment of a specified rate for each hour of labor performed, make up about 40 percent of the rehabilitation program. Repair orders placed under such contracts increased from \$18.3 million in fiscal year 1974 to \$24.4 million in fiscal year 1975.

Federal agencies having work done under time and material contracts include the Department of the Air Force; the Air National Guard; the Department of the Navy; the Department of the Army; Agency for International Development; the Forest Service, Soil Conservation Service, the Department of Agriculture; and the Bureau of Indian Affairs, Bureau of Land Management, and Bureau of Reclamation, Department of the Interior; in addition to units of GSA.

Recent Air Force use of GSA time and material contracts is a major reason the rehabilitation program has been expanding. Currently, repair of Air Force equipment makes up about 85 percent of the orders placed under the contracts.

The Defense Contract Administration Services generally provides contract administration for the military services. However, GSA also provided contract administration for equipment owned by the San Antonio and Warner Robins Air Logistics Centers, including placing orders with the contractor, providing end item inspection and acceptance, and certifying contractor billings for payment. In other cases, agencies using these contracts perform these functions for themselves.

Federal procurement regulations specify that time and material contracts be used only when the extent or duration of work cannot be initially estimated and when it has been determined that no other type of contract is suitable. The regulations also specify that a ceiling price (maximum

allowable amount to be charged) be established for time and material and that effective cost control be required through constant Government surveillance of the contractor's operations.

These limitations were established because time and material contracts contain a built-in incentive for contractors to incur costs. This is because payments under these contracts are based upon the number of direct labor hours used at a specified hourly rate. Since the rate includes provision for overhead and profit as well as labor costs, each additional hour charged to the contract adds to the contractor's profit and recovery of overhead.

The time and material contracts awarded by GSA regions generally require contractors to submit a cost estimate on each repair order, which, when approved by the Government, becomes the cost ceiling. The amount actually charged for each repair order is to be based upon (1) the number of direct labor hours used multiplied by the specified hourly rate and (2) the actual cost of direct materials used or a percent of catalog price. Allowable contract charges should not exceed the cost ceiling, should not include separate charges for indirect labor or indirect materials that are provided for in the hourly rate, and must be supported by detailed and accurate accounting records.

CHAPTER 2

CONTRACT OVERCHARGES--IMPROVED

CONTRACT ADMINISTRATION NEEDED

On all eight time and material contracts we audited, the contractors (see app. I) billed the Government for unauthorized and unsupported labor and material charges. The improper charges went unchecked because GSA did not take corrective action, although such charges had been made known to GSA in its internal audit reports since 1973.

We informed GSA of our findings and recommended detailed reviews by GSA to determine and recover the total overcharges to the Government. GSA has told us that, on the basis of partial audits, actions have been started to collect \$464,000 in identified overcharges, and further collections are expected. An example of the questionable billings follows. The aircraft engine test equipment (see p. 5) was being repaired by Mikelco Incorporated at Bandera, Texas, at the time of our review. Charges accumulated on this repair order included \$12,456 for labor and \$18,521 for materials. Materials included \$11,565 for contractor-acquired property and \$6,956 for Government-furnished material. We questioned the propriety of many individual charges, and as a result Mikelco at Bandera deleted charges of \$7,090 for labor and \$6,668 for material. While our audit was still in process, the contractor submitted a partial billing that still contained improper charges. Nevertheless, it was certified as accurate by GSA without examining supporting documentation.

A description of the charges on this order and the reasons why they were not proper are presented below.

<u>Description of charge</u>	<u>Reason charge was not proper</u>
Labor:	
Regular labor (\$5,950)	Supporting time cards showed this labor was actually expended on work at a plant in another State.
Regular and overtime labor (\$1,096)	These charges were for indirect labor and not allowable as direct charges to the contract.

Description of charge

Reason charge was not proper

Material:

Gasoline--520 gallons
Diesel fuel--57 gallons, Engine parts and material

No gasoline or diesel fuel was used in repairing the engine test equipment. At least 130 gallons of gasoline were used in a pickup truck and a car and improperly charged to the contract.

Welding (subcontract work) 1/

The charge was for repair of an oil pan which was not part of the test equipment.

Adapters--4 each 1/

The charge was for the purchase of four 6-volt batteries. However, batteries for the test equipment were provided by the Government.

Adapters 1/

The charge was for the purchase of a tool and was not an authorized charge.

Brackets--4 each
Packing--6 rolls
Lumber (2" by 12")--336 board feet
Lumber (2" by 4")--432 board feet

The brackets were actually sliding glass windows and the packing was felt. These building materials had not been used on the test equipment.

Various types and colors of paint totaling over 150 gallons, all of which were provided by the Government

The repaired equipment was not painted.

1/Charges included in the billing certified by GSA while our audit was in progress.

Also, we found improper charges on all of the contracts reviewed, as listed below.

LABOR OVERCHARGES

1. Labor totaling \$124,000 performed by employees not directly engaged in performance of repair orders was charged to the GSA contracts. However, the contracts stated that

only the labor of personnel directly engaged in performance of the work was an allowable charge. For example:

- Mikelco at Bandera, charged \$2,907 for indirect labor on one repair order, 11 percent of total labor charged. The charge was supported with time cards for a contract administrator, a supply manager, a bookkeeper, a purchasing agent, and two clerks.
- On another repair order, Midwest Maintenance and Construction, Incorporated, of San Antonio, charged \$688 for indirect labor, 13 percent of total labor charges. The charge was supported by time cards for a production controller, two quality inspectors, two supply workers, and a purchasing agent.

2. Contract billings contained charges for labor which was not actually worked or which was devoted to other than contract work. For example:

- Mikelco at Bandera charged 4,758 labor hours, \$28,837, for employees at a plant in one State to five repair orders being worked at a plant in another State. On one repair order, the out-of-state labor charges began 6 days before the equipment was shipped to the contractor for repair and continued for 4 days after the equipment was completed and accepted by the Government.
- Quality Manufacturing, Incorporated, billed the Government for 92 hours including 41 hours which were erroneously charged after the work was completed.
- Mikelco at San Antonio, billed for about 150 labor hours reportedly incurred on one repair order over a 9-month period, although the equipment involved was at a subcontractor's plant during that period.

3. The Government authorizes contractors to use overtime in order to reduce repair times. However, use of overtime on the GSA contracts resulted in increased costs without a reduction in repair times. For example:

- Mikelco at Bandera charged overtime at one and one-half times the regular hourly rate during a 6-week period. However, Mikelco charged no regular labor during the same time period and the repair order scheduled to require 2 months was still incomplete after 11 months.

4. Contractors adjusted their labor records, to avoid losses on repair orders when labor ceilings were exceeded and to increase charges on orders where the maximum number of labor hours had not been reached. The following instances found at Quality Manufacturing are illustrative of the practices we found.

- Quality billed for 623 labor hours on one repair order, the exact amount of the labor ceiling. Although the items had been in process for over 11 weeks, 63 percent of the labor charges, 393 hours, were made during the last 2 weeks. Time cards supporting 64 of the 393 hours had initially been charged to other repair orders but were subsequently altered and charged to the billed order.
- Quality Manufacturing reached the ceiling for labor charges on another repair order on May 23, 1975. After that date, time cards for 73 hours charged to the order were altered and charged to other jobs.

MATERIAL OVERCHARGES

1. Contractors billed for materials which were not used on the repair orders billed. This includes materials which were not usable on the equipment repaired and materials which were not usable in the quantities charged. For example:

- Mikelco at San Antonio charged two repair orders with 760 gallons of gasoline. Mikelco's representative admitted that most of the gasoline had not been used on the repair orders charged, but rather, for other purposes, including use in company vehicles.
- Midwest of Oklahoma City charged such materials as locks, doors, hinges, and sheet metal used in remodeling its plant to orders for repair of Government equipment.
- Mikelco at Bandera purchased shop and office equipment for company use and billed contract jobs as direct materials. Electric wall clocks were described on a billing document as gauges.
- Midwest of Oklahoma City charged two drive shafts to an item that required only one, and two electrical switches were charged when only one was used.

2. Even though the contracts provided that material charges be based on actual cost, the contractors used estimated costs for billing purposes. For example:

- Mikelco at San Antonio billed packaging materials costing \$14,720 to contracts jobs at estimated costs of \$22,456.
- Midwest of San Antonio billed the Government estimated costs of \$8,108 for repair parts which cost \$2,348.
- Mikelco at Abilene billed the Government \$3,300 for the manufacture of replacement parts. Mikelco's representative said that the charges represented the labor required to fabricate the parts, but he could not provide supporting time cards because the cards had been used to support labor charges to other jobs.
- Mikelco at Bandera charged \$6,065 for quantities of seven different parts to a single job order. Mikelco stated the parts came from company stock but could not provide support for the costs charged.

In addition to noting the overcharges, we noted deficiencies in the contractors' purchasing and pricing practices. These included failure to obtain competition, buying from affiliates, and pricing material at retail prices rather than cost. We also noted inadequate control over Government-furnished material. Examples are discussed below.

LACK OF COMPETITION

In GSA regions 7 and 4, where charges for materials are based on contractors' costs, regulations require contractors to procure materials at the most economical price reasonably available. In reviewing six contracts performed by Midwest, Mikelco, and Quality Manufacturing, we found that competitive bids from vendors were not routinely obtained or were not documented. Accordingly, there was no assurance that prices paid by the contractors and billed to the Government were the best available. Mikelco at San Antonio, for example, continued to procure yellow paint from the same vendor without getting competitive bids, although the unit price increased from \$6.95 to \$10.95 a gallon.

PURCHASES FROM AFFILIATES

Midwest purchased materials from affiliated 1/ supply companies at prices far in excess of those available

1/The president and the comptroller of Midwest were president and secretary-treasurer, respectively, of the supply company.

elsewhere. During the same period, the Air Force purchased identical parts from the original manufacturer at considerably lower prices, as shown below.

	<u>Midwest purchases</u>		<u>Air Force purchases</u>	
	<u>Quantity</u>	<u>Unit cost</u>	<u>Quantity</u>	<u>Unit cost</u>
Support	45	\$369	17	\$221
Seal	45	60	45	37
Seal	45	62	32	37
Cartridge assembly	45	313	37	124
Shaft	45	208	44	57
Oil slinger	10	77	53	12
Sleeve	10	59	63	13

We did not determine where Midwest's affiliated supply company obtained the parts or how much they actually cost. From the table above, however, it appears likely that the affiliate added a sizable price markup when transferring the parts to Midwest. Based on Federal procurement regulations, a markup of this nature generally is not an allowable contract charge. Transfer prices at other than costs are permitted in certain circumstances if they are found to be reasonable. In the case shown, however, the contractor's transfer prices appear unreasonable and should have been questioned by GSA.

IMPROPER MATERIAL PRICING PROVISIONS

The contracts in region 9 violated Federal procurement regulations by allowing contractors to bill materials based on retail prices rather than actual costs. As a result, Western Lift Truck, Incorporated, billed certain items at an average of 67 percent above cost and other items at 95 percent above cost. A carburetor, for example, was purchased for \$46 and billed to the Government at \$105. For materials such as lubricants, manufacturers' price lists were not available, and Western arbitrarily set the prices to be charged to the Government. Using this procedure, Western billed \$22.50 per ten gallons for hydraulic oil purchased for \$8.20.

INADEQUATE CONTROL OF GOVERNMENT-FURNISHED MATERIAL

The Air Force's Air Logistics Center provided selected materials at no cost to several contractors, as provided by the contracts. A number of contractors located in region 7 ordered and received about \$2.2 million in Government-furnished material during fiscal years 1974 and 1975.

These contractors were responsible for establishing adequate property control procedures and for maintaining accountable records for the Government-furnished material in their possession. GSA, however, did not provide adequate surveillance to assure that the contractors carried out their responsibilities. In some cases receipts and issues of Government-furnished material were not recorded on stock records. In other cases, Government-furnished material received was recorded on inventory records and later shown as issued to specific repair orders but was not used on the repair orders charged. We could not determine from the available contractor records how the material was actually used, and there was no assurance it was used for authorized purposes. The following conditions found at Mikelco illustrate this condition.

--360 paint brushes were charged to an item that was not painted.

--10 boxes of nails were charged to a job on which no carpentry work had been done.

--48 gallons of red paint and 40 gallons of black paint were charged to an end item that was painted yellow.

--150 sheets (4,800 square feet) of plywood were charged to a job which required only a small amount of lumber.

UNAUTHORIZED GOVERNMENT-FURNISHED MATERIAL

Contractor material requisitions are received at the San Antonio Air Logistics Center where they are either filled from inventories at that location or passed on to other Government supply sources to fill. Individual requisitions are not normally reviewed by Air Force personnel to determine if the types and quantities of materials ordered are proper, based on the equipment being repaired and the contract definition of direct materials. In the absence of an effective review by the Air Force, contractors requisitioned and were provided unauthorized items, such as office supplies, lighting equipment, and hand tools. Mikelco at San Antonio, for example, had requisitioned fluorescent desk lamps for use in office and shop areas although it was only authorized to requisition material to be used directly in equipment repairs. The need for improvement in the control of Government-furnished material has been brought to the Air Force's attention in an earlier GAO report (PSAD-76-78, Mar. 8, 1976). We have no further recommendations on this matter at this time.

GSA SUPERVISION

In the 17-State area covered by GSA regions 4, 7, and 9, there were about 33 time and material contracts. Inplant surveillance of these contracts by GSA representatives consisted primarily of periodic visits to inspect and accept repaired items. Contractor accounting, parts purchasing, and property control procedures were not adequately evaluated, and contractor billing documents were not audited prior to payment. In some cases, GSA made limited reviews of the billing documents it certified as accurate for the San Antonio and Warner Robins Air Logistics Centers, but the reviews were ineffective in detecting improper charges. Billing documents for other ordering agencies, such as the Agency for International Development and McClellan Air Force Base, received even less attention and were not audited by GSA or the ordering agencies.

We discussed the lack of onsite contract surveillance with GSA and questioned it as to the feasibility of increased staffing. GSA officials advised us they were seeking additional personnel authorizations but could not predict the outcome.

INADEQUATE USE OF COST CEILINGS

Cost ceilings on the GSA contracts we reviewed were generally established by the ordering agency's approval of labor and material estimates contractors submitted on individual repair orders. In many cases, the estimates were approved without adequate evaluation.

Air Force personnel who approved contractor estimates did not know the condition of the equipment to be repaired or which components required repair or replacement. Consequently, they could not accurately estimate labor and material required. In general, the Air Force accepted contractor estimates which did not exceed predetermined dollar limits. The dollar limits were based on percentages of equipment replacement costs or nationwide average costs to repair like items during the preceding year. Neither method considers the actual condition of the equipment to be repaired.

We noted several instances in which overstated cost ceilings on Air Force orders permitted contractors to charge for unneeded labor hours. We also found contractor billings for labor were usually equal to or varied only slightly from the ceilings established for work orders. In our opinion, the ceilings on Air Force work orders were not properly established and did not provide an effective control over repair costs.

CHAPTER 3

INTERNAL AUDIT

The need for improved contract surveillance had previously been brought to the attention of GSA contract administrators. In each region we visited, a GSA Office of Audits had reported many of the same deficiencies found during our review. Reporting the deficiencies found, however, did not bring about any real or permanent improvements in contract administration or contractor performance.

In 1973 the Office of Audits reviewed two contractors in region 7 and reported

- discrepancies in charges for labor and material,
- inadequate control of and accounting for Government-furnished material, and
- inadequate competition in procuring materials charged to the contracts.

Each of the above conditions still existed at the time of our review.

In May 1974 the Office of Audits reviewed a region 4 contractor and reported discrepancies in charges for both labor and material. Fourteen months later the Office of Audits reviewed the same contractor and found that conditions identified in the prior review still existed. They reported that (1) time cards were altered, (2) the Government was charged for labor hours not actually paid to employees, and (3) discounts on parts purchases were not passed on to the Government. Seven months prior to the second audit, the contractor had been awarded a new contract without a preaward survey to determine if conditions identified in the first audit had been corrected. The GSA contracting officer had certified that the contractor was a responsible bidder, based on its having successfully performed under previous contracts.

Following an audit of a region 9 contractor in January 1974, the Office of Audits reported that the contractor's accounting system and controls were such that the basis could not be determined for \$9,436 of \$21,249 in material costs billed to the Government. The auditors further concluded that in some cases the contractor billed on the basis of estimates rather than actual material usage.

In our review we found that region 9 contractors were still not required to maintain accounting systems adequate to support contract charges for either labor or material. The contractor we reviewed, Western Lift Truck, did not have time cards to support some labor charges, and some of the time cards provided were so incomplete we could not determine whether the labor hours were expended on Government or commercial work. Furthermore, the contractor's material control and accounting procedures were inadequate to support the types, quantities, and in some cases the unit prices of parts charged to the Government.

Although Federal procurement regulations indicate that adequate cost accounting systems are essential for cost-reimbursable-type contracts, GSA region 9 did not normally evaluate contractors' accounting systems when performing preaward surveys. Western was assumed to have an adequate accounting system since it had been in the equipment repair business for several years.

CHAPTER 4

CONCLUSIONS, RECOMMENDATIONS, AND

AGENCY AND CONTRACTOR COMMENTS

CONCLUSIONS

Time and material contracts provide contractors an incentive to incur unnecessary costs because hourly labor rates include labor, overhead, and profit. Consequently, each hour charged to the contract adds to the contractor's profit and to his recovery of overhead. Similarly, when contractors or their affiliates are permitted to profit directly from materials charged to the contract, there is an incentive to incur unnecessary material costs. Although there are more desirable types of contracts, in some circumstances, there is no alternative to using time and materials contracts.

In view of the undesirable characteristics of these contracts, Government regulations emphasize that surveillance must be more stringent and extensive than on other types of contracts and that a ceiling should be established on costs to be incurred on each job performed.

On the GSA contracts we reviewed, the ceilings were generally based on contractors' estimates that were accepted by the Air Force and not questioned by GSA. As a result, the ceilings did not serve their intended purpose. GSA surveillance was also inadequate.

Furthermore, GSA management failed to follow up on the results of initial audit reports dealing with this matter. We believe that appropriate corrective action on the reports would have prevented many of the problems discussed in this report.

RECOMMENDATIONS

We recommend that the Administrator of General Services establish adequate procedures to assure that the Government is not overcharged on time and material contracts. We recognize that this may require an increase in staff resources, and, if they are not available, GSA should consider requesting assistance from the Defense Contract Administration Services and the Defense Contract Audit Agency.

We recommend also that followup procedures be instituted to insure that appropriate action is taken on GSA internal audit reports. Furthermore, in addition to the

reviews started at our request. GSA should review its remaining time and material contracts to determine whether detailed audits and recovery of improper billings are appropriate.

AGENCY COMMENTS

GSA stated in its formal comments (see app. II) that it was in general agreement with our report and that the following corrective actions were being implemented:

- Contractors will be required to (1) maintain a written procurement system to insure that parts are purchased competitively, (2) reconcile labor hours with payroll records at least quarterly, (3) maintain time cards in ink, and (4) document the use of intercompany labor. Additionally, instructions have been furnished to the regions on the administration of time and material contracts and controlling Government-furnished material.
- Every consideration is being given toward improving surveillance of contractor operations. These considerations include assistance from the Defense Contract Administration Services and using inspection capability from other program areas. Furthermore, attempts are being made to determine if present procedure could be adapted to permit another method of contracting. When applicable, the benefits of negotiating these contracts will be evaluated.
- Upon request, GSA's Office of Audits will conduct preaward reviews of contractors' accounting systems and post audits of the actual billings under time and material contracts. Deficiencies in the contractors' accounting systems will be reported to the contracting officers. The accounting systems can be resurveyed, upon request, in accordance with established followup procedures.
- Selected audits are being made commensurate with the present funding situation. In addition, attempts are made to reprogram funds in order to contract out a larger part of the contract audit workload.
- GSA regional offices have been notified of the findings of this report and requested to review their time and material contracts for heavy equipment repair. If any improprieties are revealed, a detailed internal audit will be requested. A covering monthly report has been established to monitor regional progress in the conduct of their reviews.

We believe the above corrective actions, if effectively implemented, should provide assurance that the Government will not be overcharged. GSA should, however, review all of its time and material contracts instead of limiting its review to heavy equipment contracts.

CONTRACTOR COMMENTS

The contractors were also given an opportunity to comment on our findings when the work at each location concluded. Mikelco did not provide comments. The other three agreed with our findings in some instances and disagreed with others. For example, Midwest believes the definition of indirect labor contained in its contracts with GSA is open to various interpretations. Their comments were considered during report preparation.

CHAPTER 5

SCOPE OF REVIEW

We reviewed GSA contract administration procedures and audited selected time and material contracts in regions 4 (Atlanta), 7 (Fort Worth), and 9 (San Francisco). In region 7, where the cost of time and material contract orders was over 50 percent of the national total, we audited the five largest contracts, three performed by Mikelco and two by Midwest. In regions 4 and 9, we audited one contract performed by Quality Manufacturing and two contracts performed by Western Lift Truck, respectively. Our audits consisted of evaluating contractors' operating procedures which affect contract costs and of examining supporting documentation for selected billing documents.

We also discussed various aspects of contract administration with officials of the following agencies which used the time and material contracts.

San Antonio Air Logistics Center
San Antonio, Texas

Warner Robins Air Logistics Center
Warner Robins, Georgia

McClellan Air Force Base
Sacramento, California

Agency for International Development
New Cumberland Army Depot, Pennsylvania

Mare Island Naval Shipyard
Vallejo, California

NAMES AND LOCATIONS OF

CONTRACTORS COVERED IN OUR REVIEW

Midwest Maintenance and Construction, Incorporated
Oklahoma City, Oklahoma
San Antonio, Texas

Mikelco Incorporated
Abilene, Texas
Bandera, Texas
San Antonio, Texas

Quality Manufacturing, Incorporated
Eastaboga, Alabama

Western Lift Truck, Incorporated
Sacramento, California
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UNITED STATES OF AMERICA
GENERAL SERVICES ADMINISTRATION
WASHINGTON, DC 20405



August 5, 1976

Honorable Elmer B. Staats
Comptroller General of the United States
General Accounting Office
Washington, DC 20548

Dear Mr. Staats:

Thank you for your letter of May 26, 1976, transmitting a copy of the draft report to the Congress entitled "Repair Program for Government Property -- Effective Surveillance Needed."

This report is a consolidation of regional GAO audits concerning the contractor operating procedures of eight time and material contracts for heavy equipment repair issued and administered by our regional offices at Atlanta, Fort Worth, and San Francisco. The thrust of the report is that GSA is not providing adequate contract administration and contractor surveillance as required by the Federal Procurement Regulations for time and material contracts. As a result, some contractors were overcharging the Government for labor and materials. We are in general agreement with this report subject to the comments below.

With regard to statements contained on pages 13 through 16 of the report, the General Services Administration (1) provided a degree of control for government furnished material (GFM) in Region 9, but the control was not commensurate with the volume in Regions 4 and 7; (2) responded to the corrective action recommended in the internal audit reports of 1973 and 1974 by correcting contract provisions and adding three Quality Assurance Inspectors; (3) routinized contractor estimates for excessive charges; and (4) made visits over and above those required to inspect and accept end items; however, they were not of sufficient frequency to improve in-plant surveillance.

With respect to item (2) above regarding our response to internal audit recommendations, we believe that the actions taken were commensurate with the volume of business at that time.

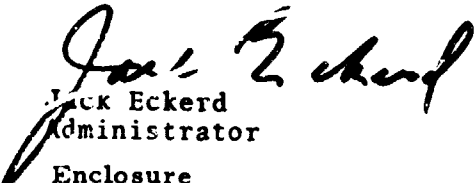
GSA management did follow up on the results of internal audits. As indicated above, there was response at both the Central Office and

regional office levels with respect to changes in contract provisions and additional personnel. It is agreed that many of the problems would not have occurred if appropriate corrective action had been taken. However, it must be stated that at the time corrective actions were taken, they were commensurate with and adequate for the volume of business. For instance, the most rapid growth occurred in Region 7 where volume under these contracts increased from \$1.6 million in FY 1973 to \$12.4 million in FY 1975.

We believe that recent and current efforts to implement the recommendations contained in this report, and those of the follow-on internal audit reports, will serve to increase the benefits that will accrue to the Government through this maintenance and repair program. In this regard, we are reviewing the entire program with respect to resource requirements, concepts, and procedures.

We are pleased to provide you, as an enclosure to this letter, our comments on each specific recommendation.

Sincerely,



Jack Eckerd
Administrator

Enclosure

**GSA comments on GAO draft report to
the Congress entitled "Repair Program
for Government Property -- Effective
Surveillance Needed"**

Recommendation. That GSA establish adequate procedures to assure that the Government is not overcharged.

Comment. Actions have been initiated to improve those areas identified in the GAO report and recent GSA audit reports to ensure that the Government is not overcharged. These actions include changes in contract provisions that require the contractor to (1) maintain a written procurement system to ensure that parts are purchased competitively; (2) reconcile labor hours with payroll records at least quarterly; (3) maintain time cards in ink; and (4) document the use of intercompany labor. Additionally, instructions have been furnished to the regions on the administration of time and material contracts and controlling GFM.

Recommendation. That if GSA cannot obtain additional resources, then it should request assistance from Defense Contract Administration Service (DCAS) or Defense Contract Audit Agency (DCAA).

Comment. We are presently exploring every possible avenue that will improve the rate and quality of in-plant surveillance. These considerations include assistance from the Defense Contract Administration Services (DCAS) and GSA inspection capability in other program areas. Furthermore, we are attempting to ascertain if present procedures could be adapted for another method of contracting. When applicable, we will also evaluate the benefits of negotiating these contracts.

Recommendation. That followup procedures be instituted to insure appropriate action taken on GSA internal audit reports.

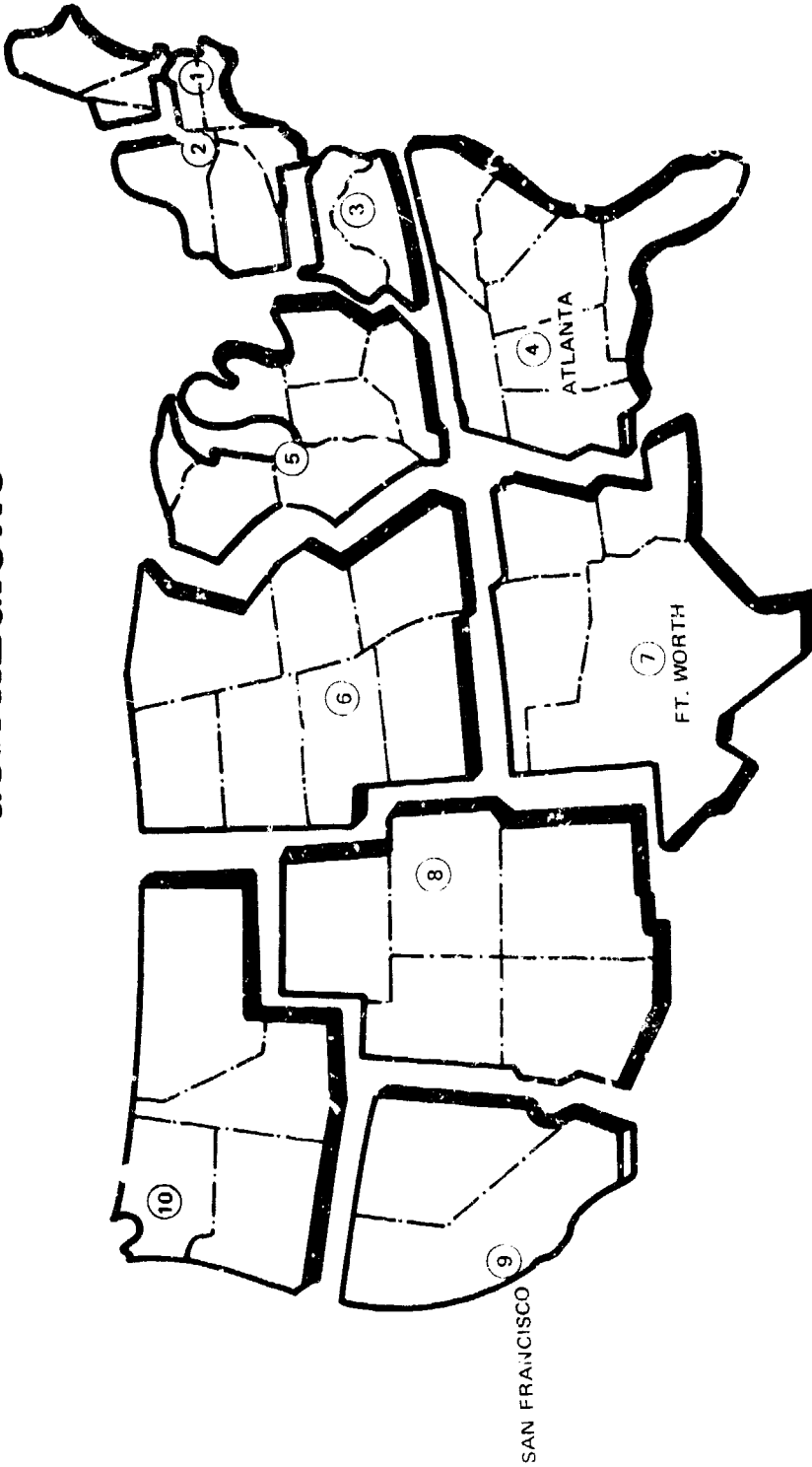
Comment. Upon request, the Office of Audits conducts preaward reviews of contractors' accounting systems and post audits of the actual billings under the time and materials contracts. Deficiencies in the contractors' accounting systems are reported to the contracting officers. The accounting systems are resurveyed, upon request, in accordance with established followup procedures.

Selective audits are being made commensurate with our present funding situation. We are attempting, however, to reprogram our funds to allow us to contract out a larger part of the contract audit workload.

Recommendation. That GSA review other T & M contracts to determine whether detailed audits are required.

Comment. We have alerted the GSA regional offices as to the findings of this report and requested that they review their time and material contracts for heavy equipment repair. If any improprieties are revealed, a detailed internal audit will be requested. A covering monthly report has been established to monitor regional progress in the conduct of their reviews.

GSA REGIONS



PRINCIPAL OFFICIALS
RESPONSIBLE FOR ADMINISTERING
ACTIVITIES DISCUSSED IN THIS REPORT

	Tenure of office	
	From	To
<u>GENERAL SERVICES ADMINISTRATION</u>		
ADMINISTRATOR OF GENERAL SERVICES:		
Jack Eckerd	Nov. 1975	Present
Dwight A. Ink (acting)	Oct. 1975	Nov. 1975
Arthur F. Sampson	June 1972	Oct. 1975

DEPARTMENT OF DEFENSE

SECRETARY OF DEFENSE:		
Donald H. Rumsfeld	Nov. 1975	Present
James R. Schlesinger	July 1973	Nov. 1975