



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

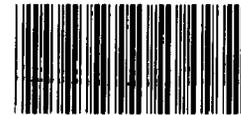
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MISSION ANALYSIS AND
SYSTEMS ACQUISITION DIVISION

B-206836

MAY 10, 1982

The Honorable John G. Tower
Chairman, Committee on Armed Services
United States Senate



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Dear Mr. Chairman:

Subject: Evaluation of Unit Cost Reports Submitted Under
Public Law 97-86, Section 917 (GAO/MASAD-82-36)

Your letter of February 5, 1982, asked us to examine unit cost reports submitted by the Secretary of Defense in compliance with Public Law 97-86, Section 917 and report on the validity of the cost data provided therein. You also asked us to inquire into problems which preclude the accurate and timely reporting of such data and suggest improvements which might be made. At a subsequent meeting with your office, a request was also made for suggestions on improving the legislation. Preliminary information on the unit cost reports and the legislation were supplied to your office on March 24, and 30, 1982.

We reviewed 19 unit cost reports submitted to the Congress by the Department of Defense (DOD) in March 1982. We examined the documents for completeness, currentness, and accuracy to evaluate the validity of the data presented therein. We were not able to accomplish a complete indepth evaluation to the extent we would have preferred because of the time constraints imposed. We believe, however, that our work was sufficient to provide some observations on the validity of the report and also offer some suggestions as to how to improve unit cost reporting.

Overall, DOD has made a dedicated and reasonably successful effort to comply with the requirements of Public Law 97-86 with respect to submitting unit cost reports. Some reports, however, were lacking in completeness and accuracy. We also believe that the time constraints imposed on program managers and service Secretaries when verifying and deciding before reporting on whether a unit cost breach has occurred could interfere with accurate reporting. Further, in the interest of improving the efficiency of reporting, we believe consideration should be given to combining unit cost reports with a modified selected acquisition reporting system.

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COMPLETENESS, CURRENTNESS, AND ACCURACY
OF UNIT COST REPORTS

The unit cost reports submitted to the Congress in March 1982 were for the most part reasonably complete, current, and accurate. There were, however, some cases where the program estimates did not include all costs, were not consistent with independent estimates, and will soon be outdated because of changes and uncertainties in the program.

In the case of the Army's Pershing II missile and the AH-64 helicopter programs, we found that the current program cost estimates did not include all program costs. Specifically:

--The program cost estimate for the Pershing II missile is presently being revised by the Army and is expected to be completed in May 1982. Costs for support equipment such as vehicles, generators, trailers, and communication equipment were excluded from the unit program cost estimates. The Army's estimates for the costs of this equipment will not be available until June 1982.

--The AH-64 helicopter program cost estimate excluded such items as \$200 million for a combat mission simulator, \$13 million of military construction costs, and \$500,000 for survivability and communication equipment.

For the most part, with only two exceptions, the unit costs reported were in line with estimates prepared independently by several cost estimating sources in the services and the Office of the Secretary of Defense. Specifically:

--After the issuance of the unit cost report on the Patriot air defense system, a new cost estimate was made within the Army and coordinated with the program office. As a result, the program cost was increased about \$600 million over the cost estimate included in the report to the Congress. The increase was attributed to the use of erroneous inflation indexes, requirements for additional procurement funds, and increases to cover a contractor's proposal which was higher than the Army's estimate.

--The Air Force's unit cost report on the Defense Satellite Communication System reported a program acquisition unit cost of \$119.9 million. The subsequent Secretary of Defense letter to the Congress certifying the need to continue the program provided a different estimate of \$137 million. Between March 8, 1982, when the unit cost report was submitted and April 7, 1982, when the Secretary of Defense's certification was submitted, the Secretary approved a \$200 million increase to the program. We believe the Secretary of Defense's actions were based on an independent review of the program which estimated program costs 14 percent

higher than the Air Force's estimate. The independent estimate also showed a potential for substantial cost growth in fiscal year 1983 and later years.

We also found that changes underway in several programs could soon outdate the reports or there were uncertainties which made certain information in the reports questionable. Specifically:

- Soon after submitting the unit cost report, the Air Force's Maverick program was restructured and some quantities were deferred to later years. The cost impact of this deferral is not known at this time. Also, uncertainties may exist because the report is projecting a 10-percent cost saving (about \$379 million) based on successfully competing the program or entering into multiyear contracting.
- Although there was an overall program cost increase of \$81.9 million on the Army's Hellfire missile program, it was not reported because the program acquisition unit cost was not breached. The increase occurred because the procurement was stretched out over a longer period of time. However, the increased program cost did not affect the acquisition unit cost because substantial quantity increases compensated for the increase. Since explanations are required only if unit costs are breached, the stretchout costs were not reported.
- The primary reason for the breach in the F-16 aircraft unit cost is explained as due to the addition of a more expensive version of the aircraft. We found that the Air Force is not certain as to whether it will buy the more expensive version, and therefore, we question whether the report accurately reflects future requirements.
- A substantial amount of the program acquisition unit cost breach in the F-15 aircraft unit cost was due to the reported projected acquisition of a more expensive version of the F-15 aircraft. As in the case of the F-16, the Air Force is uncertain as to whether it will procure such an aircraft. Again, in this case, we question whether the report accurately reflects future requirements.

PROBLEMS WHICH MAY INTERFERE WITH
TIMELY AND ACCURATE REPORTING

Although each of the initial unit cost reports submitted by the services and the subsequent Secretary of Defense's certification of the need for continuing programs was submitted on time, there are potential problems which could interfere with the timing and quality of the reports.

As the services see it, to some extent, the unit cost reports' requirements for timely and accurate reporting appear to conflict. The law states that a program manager should immediately report cost increases when there is a "reasonable cause to believe" that the thresholds will be breached. When revised program cost estimates are being prepared and contracts are being negotiated or modified, program managers may be reluctant to report potential breaches until firm data on cost is obtained. A dilemma is created if the problem is reported but a breach does not occur. The program manager could be criticized for not providing accurate information. Conversely, if the problem is not reported immediately, but cost increases materialize, the program manager could be faulted for not being timely and perhaps cited for violating the law. We believe that when in doubt it would be best to report the possible breach.

Another problem is the time limits for reporting programs to the Congress. The law states that the service Secretary should promptly report program acquisition unit cost increases and procurement unit cost increases when there is reasonable cause to believe that the thresholds will be breached; no specific time limit was set. The primary problem is the sometimes lengthy process for cost analysis and other study to confirm the extent of the breach and to examine possible alternative courses. While we believe some deadline should be established, we recognize the complexity of making determinations in some programs. In our opinion, DOD and the committee should negotiate some deadline which meets the Congress' need yet recognizes DOD's need for adequate time to confirm that a cost breach is occurring.

IMPROVING UNIT COST REPORTING

With regard to suggested improvements that might be made to unit cost reporting, we believe consideration should be given to combining such reporting with selected acquisition reporting. DOD has previously made this suggestion. The Director of the Congressional Budget Office made a similar suggestion in a recent statement before the Senate Committee on Governmental Affairs.

Unit cost reports should be considered in light of the Selected Acquisition Reports which already provide much similar information and probably could be modified to accommodate this requirement. Such reporting could be accomplished by substituting unit cost reports for the quarterly March 31, June 30, and September 30 Selected Acquisition Reports and retain the December 31 Selected Acquisition Report on an annual basis. A unit cost report would also be submitted at any time the cost threshold is breached during the year. In our opinion, the value of the present quarterly Selected Acquisition Reports other than as of December 31 is questionable considering that usually significant program changes are reported only annually in the December 31 report.

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All unit cost reports submitted to date were based on program data reflected in the fiscal year 1983 budget submission. Thus, the timeliness and accuracy of reports submitted at other times throughout the fiscal year and the reporting of changes not reflected in an approved program have yet to be tested. We will examine unit cost reports as they are submitted to the Congress and plan to report on their completeness, currentness, and accuracy.

We did not submit a copy of this letter to DOD for comment due to time constraints. We believe, however, based on discussions with DOD officials, that our observations and suggestions are not at wide variance with DOD viewpoints.

Sincerely yours,



for

W. H. Sheley, Jr.
Director