Conclusions

We believe that there is an alternative to an across-the-board increase which appears to be more equitable and which, at the same time, should bring a more realistic return to the Government. This would be to authorize rent-free use of the presses when used on Government work and to increase the rental for commercial use of the equipment.

The overall use of the presses has significantly increased since the inception of the program. Although the predominance of use is for Government end-items, significant amounts of commercial sales are now being processed through the presses. Also, the present procedure provides no assurance that Government end-item prices are not significantly increased by the pyramiding of higher tier indirect expenses and profit on the rent cost included in prices to the Government of forgings and extrusions. The authorization of rent-free use for Government work would also be consistent with the general leasing practices governing other types of IPE used by contractors and subcontractors on Government orders.

In comparison with current rates of return on Government bonds and commercial paper, the 1 to 2 percent annual return on the Government's investment in heavy presses is not acceptable, in our opinion, from a financial point of view. We proposed, therefore, that DOD reexamine its current policy of not authorizing rent-free use of Air Force heavy presses used on Government work and that priority effort be applied to increasing the Government's return through rental arrangements.

Agency comments

The Deputy Assistant Secretary has advised us that DOD, in conjunction with the Air Force, is reexamining existing arrangements pertaining to rental charges for use of these presses and is considering such aspects as the waiving of rental charges for Government work, the increasing of rental returns on commerical use, and the feasibility of selling some of the presses to Defense contractors.

Modernization of industrial plant equipment

Prospects of continued large Government investment in machine tools in possession of contractors

The basic policy of DOD, as stated in ASPR, is very restrictive as to furnishing new Government-owned facilities, including, industrial plant equipment, to contractors. It provides generally that new facilities shall not be furnished where an economical, practical, and appropriate alternative exists.

The Department of Defense program for replacement of Government-owned machine tools was initiated in 1956 for the purpose of maintaining such tools in a modern condition. To accomplish this objective, the military departments were to include in their annual budget requests from 2 to 5 percent of the acquisition cost of the machine tools listed in departmental inventories. The replacement of machine tools is distinguished, in DOD directives, from the provision of additional facilities to increase production capacity.

According to DOD reports, the cost of machine tools in military inventories as of October 1966 was $2.8 billion, with most of these tools in possession of contractors. Fiscal year 1966 expenditures amounted to about $51.5 million for modernization and replacement purposes. Such expenditures had risen from an average of $27.4 million in the 1958 through 1963 fiscal year period. Expenditures of $65.8 million were forecast for the fiscal year 1967.

Anticipated savings not always realized as planned

Department of Defense Directive 4275.5 requires that the replacement of machine tools be justified on economic grounds. This directive recommends that machines not be replaced unless their cost can be amortized through operating savings in a period of about 3½ years.

The justification, which is prescribed under another DOD instruction, 4215.14, must show that the savings were based on a comparison of the operating costs of the machines then in use with the operating costs of a new machine which could replace the older machines. The reduction in cost is then computed for a 12-month period immediately following the date of preparation of the estimate on the basis of existing and anticipated production requirements known to the contractor. Annual amortization costs of the machines are also considered in computing the saving. One year after each modernization item is released for production use, the contractor is required to submit a postanalysis report to show actual cost savings for that year.