

11. Transportation and installation costs

"We found that these costs had in some cases been applied as a percentage factor to the acquisition cost of IPE being rented by contractors. One contractor added a factor of 3.5 percent, another contractor added a factor of 1 percent. That these costs can be significant is illustrated by the fact that, in one case, a contractor increased the rental base for IPE by as much as \$800,000 through the addition of a factor for transportation and installation." (page 43)

Comment: Since we apply the 3.5 percent factor to the acquisition cost of IPE to account for transportation and installation costs resulting in an \$800,000 addition to the base for IPE on which we pay rent. Northern Ordnance appears to be adding the highest amount for transportation and installation costs among the contractors studied and thereby increasing the rental it pays to the Government. We have recently reviewed this matter indicating that this 3.5 percent factor is somewhat higher than can be supported by the historical records of actual costs of transportation and installation, and a lower factor should be used.

12. Real property

"For example, replacement of a portion of the plant's electrical distribution system costing about \$104,100 was determined not to be of a capital nature because it replaced an existing system. We noted, however, that the capacity of the system to provide service was significantly greater after its installation and that the useful life of the property was extended by at least 10 years." (page 45)

Comment: The plant's electrical distribution system is an integral part of the Government buildings. It is not normal industry practice to capitalize the replacement of a small part of a capital asset. Although \$104,100 is a significant expenditure, it is only a small part of the buildings costing several million dollars. The replacement of the obsolete and unsafe switch gear for which repair and replacement parts could not be obtained does not in any way extend the useful life of the buildings of which the switch gear is a part. A smaller part of the project involved the furnishing of larger lighting transformers to safely accommodate the presently installed capacity. It was determined by appropriate DOD authority in accordance with generally accepted accounting principles that these changes did not require a change in the Government's asset accounts.

13. Real property

"In another instance, an atmospherically-controlled room was constructed at a cost of about \$37,800 to house four gear machines and related test equipment but the cost was expensed because the room did not alter the exterior dimension of the plant." (page 45)

Comment: The expenditure of \$37,800 involved two separate projects, both involving modifications of existing precision gear manufacturing facilities. The costs of the first modification to house the precision gear equipment was treated at the request of the Government as installation charges in connection with the gear equipment, which costs have been appropriately reflected in the installation expense account mentioned under Item 11 above so that they have been added to the base for rental purposes even though the capital account has not been changed. The second portion of this expenditure involved repairs to existing walls and other commonly acceptable expensible items.

14. Special tooling and special test equipment

Need for better identification

"We found at one contractor's plant that, some tools were not marked for identification and identification could be made only by reference to engineering drawings." (page 49)

Comment: During the GAO survey only 5 items (out of a total of approximately 13,000) were determined to be improperly marked because the identifying marks had been obliterated by painting during normal tool refurbishment. Since these tools could be readily identified by reference to drawings, we do not consider that the temporary painting over of the markings on the 5 items represent a significant lack of control on our part.

15. Physical inventories

"At a third plant, we found that the inventory taking had been limited to determining whether a particular item was on hand, without regard to the quantity of identical items that should be on hand." (page 50)