

2-407.6(a)(2) revised

→ (2) For the purposes of (1) above, preference shall be given in the following order of priority:

- (i) certified-eligible concerns (1-801) that are also small business concerns (1-701),
- (ii) other certified-eligible concerns,
- (iii) persistent labor surplus area concerns (1-801) that are also small business concerns (1-701),
- (iv) other persistent labor surplus area concerns,
- (v) substantial labor surplus area concerns (1-801) that are also small business concerns,
- (vi) other substantial labor surplus area concerns,
- (vii) other small business concerns.

16-101.1(iii) revised

- (iii) General Provisions (Supply Contract) (Standard Form 32) (Pending publication of an edition of the form later than the June, 1964 edition, the clause set forth in 1-805.3(a) shall be substituted for the present provisions of clause 22, Utilization of Concerns in Labor Surplus Areas.);
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16-102, 16-204, and 16-205 caption revised and footnote added

→ **16-102 Forms for Negotiated Supply or Services Contracts (Standard Forms 18, 26, DD ASPR Form 1270, Standard Form 32, DD ASPR Form 748*, and Standard Forms 33, 33A, 36, and 30).**

→ **16-204 General Provisions—Cost Reimbursement Supply Contracts (DD ASPR Form 748).***

→ **16-205 General Provisions—Fixed-Price Supply Contracts (Standard Form 32).***

* Substitute the clause in 1-805.3(a) for clause 22 on Standard Form 32, 1964 edition, and for clause 25 on DD ASPR Form 748, Jan. 1965 edition; substitute clause in 1-805.3(b) for clause 43 on DD ASPR Form 748, Jan 1965 edition.

21-115(e) sentence added

Also enter this code if the action was awarded by labor surplus set-aside preference to a certified-eligible concern as defined in 1-801.1(i).

ITEM VII--EQUAL EMPLOYMENT OPPORTUNITY

A: DPC #42

In Item IV of DPC #42 dated 27 May 1966, procedures were published regarding the conduct of an equal employment opportunity compliance review prior to the award of formally advertised supply contracts of \$1,000,000 or more. To reflect the reassignment of responsibility for conducting these reviews, effected by DOD Directive 1100.11, Item IV, DPC #42, is hereby canceled and superseded by the following procedures:

a. Procuring Activities shall include in each IFB for supplies a notice that prior to the award of a contract in the amount of \$1,000,000 resulting from the invitation, the proposed contractor, and his first-tier subcontractor to whom he intends to make awards of \$1,000,000 or more, will be subject to an EEO compliance review (ASPR 12-306.5(c)) before the award of the contract.

b. (1) Prior to the award of a formally advertised supply contract of \$1,000,000 or more, the PCO shall request the performance of a compliance review of the employment practices of the prospective contractor, and all of his known first-tier subcontractors with subcontracts of \$1,000,000 or more, except in those cases (i) covered by c and d below or (ii) where a compliance review has been conducted within six months prior to the award. The Office of Contract Compliance (OCC) in Defense Contract Administration Service Regions (DCASR) will conduct compliance reviews for all contractors except in special cases where this responsibility has been assigned to another agency or department. In these cases, the references to DCASR in this DPC shall be deemed to mean the agency or department responsible for compliance review of the particular contractor. In order that the DCASR may arrange for the performance of the compliance review, it will be notified by the PCO of the name of the apparently successful supplier and selected subcontractors (including the place or places where the work is to be done) concurrently with the initiation of action by the PCO to determine the responsibility of such supplier. Such notification will be forwarded by the most expeditious means to the appropriate DCASR-OCC. The appropriate DCASR office will be the Region in which performance on the contract will occur. DCASR geographic boundaries are defined in DoD Directory of Contract Administration Services Components (DoD 4105.59). Where the necessary contact is by phone, written confirmation will follow.

(2) To qualify for the award of the contract, the proposed contractor and his first-tier subcontractors specified in b(1) must be found, after such compliance review, to be in compliance with the Equal Employment Opportunity Clause (ASPR 12-802(a) as amended in Item VIII, DPC #36 dated 21 October 1965) in current contracts; or in cases where they have no current Government contracts which include such clause, be found to be able to comply with such clause in the proposed contract. The PCO will be notified within 10 working days whether, on the basis of the review, the contractor is considered to be qualified for award in terms of compliance with the EEO clause. This notification will be

given by the DCASR. If the PCO is not notified within the 10-day period and a request is not made for an extension of time, the PCO may proceed with the award, and the DCASR office involved will follow the procedure contained in e below. When the DCASR determines that a proposed contractor should not be awarded a contract due to the fact that such proposed contractor is not in compliance with the EEO clause, it will so notify the PCO. Such notice shall be independent of that contained in DD Form 1524. Similar notification will be given to the Secretary of the Department concerned by the Deputy Director, DSA Contract Administration Services (CAS).

c. The procedures set forth in a and b above and any determinations thereunder shall not apply to any contracts when the Secretary of the Department concerned determines that such contracts are essential to the national security and award without following such procedures and determinations is necessary to the national security. Such cases shall include, for example, items urgently needed for current operational requirements and commodities involving a short option period. Upon making such a determination, the Secretary of the Department involved will notify the Deputy Director, DSA-CAS, within 20 calendar days.

d. The procedures set forth in a and b above shall not apply where the PCO determines that such procedures would delay the award beyond the time for acceptance specified in the bid or extension thereof.

e. Where awards are made without a compliance review as provided in b(2) and d, a review will be performed by the DCASR-OCC as soon as possible thereafter, but in no case, later than 30 days subsequent to receipt of notification.

B: DPC #46

Item III of DPC #46, dated 30 June 1966, provides for a change in ASPR 12-806.4 which would add paragraph (f). The wording of this change is now altered as follows:

(f) The following will be included in all Invitations for Bids for supplies where the award may amount to \$1,000,000 or more:

The Equal Opportunity Compliance Review

In accordance with regulations of the Office of Federal Contract Compliance, dated 3 May 1966 (31 Fed. Reg. 6881), except as otherwise authorized, an award in amount (actual or estimated) of \$1,000,000 or more may not be made under this solicitation unless the bidder and each of his known first-tier subcontractors (to whom he intends to award a subcontract of \$1,000,000 or more) are found on the basis of a compliance review, made within the 6 month period next preceding the award, to be able to comply with the required equal opportunity provisions of this solicitation.

Mr. RUMSFELD. Is there any reason that was not submitted with your testimony?

Mr. MORRIS. It just came off the printing press last night, sir. We did not expect it this morning, as a matter of fact.

Mr. RUMSFELD. I would like to look at it while someone else is asking questions.

Chairman PROXMIRE. Mrs. Griffiths?

Mrs. GRIFFITHS. Thank you very much. I would like to say to you, Mr. Secretary, not in criticism of you, but I do not agree with your statements. I think the Defense Department has spent 180 years trying to keep from finding out what things cost. Quoting from your statement, you point out that often, therefore—

We have no other source for the item than the prime contractor or the source he identifies in the manual which accompanies the equipment.

Mr. MORRIS. That is right.

PRICES PRIMES PAY FOR SUBCONTRACTED ITEMS

Mrs. GRIFFITHS. The challenge we face is the degree to which we can justify adding personnel to our procurement organizations.

For years I have had a bill in here that would require that the prime supply the price he paid for subcontracted items, and the other subcontractors supply that price. The Defense Department has opposed this.

Why, may I ask, do you oppose it? Why don't you get the prices on these items, ship them out to DIPEC and let DIPEC list them on the computers. I think it would be the simplest thing in the world. It might be a little difficult to start with. But in the end, you would know what the price was and where the items were purchasable.

Mr. MORRIS. I believe that we are endeavoring to do, so far as is practical, exactly what you say. It is not DIPEC, but the Battle Creek, Mich., computer operation.

Mrs. GRIFFITHS. The last time I was out there (DLSC) they did not even have the price of any item on anything.

Mr. MORRIS. We endeavor to maintain prices on catalog items where we have it.

PRICES ON ALL ITEMS

Mrs. GRIFFITHS. Why don't you get it all?

Mr. MORRIS. As indicated in our statement, we have the problem with new equipment coming into inventory each year, of adding some 4 million potential new items to our stock. We must, at provisioning time, select that 10 to 15 percent of the items which we and the contractor think are likely to wear out and require replacement.

When we get that kind of provisioning listing, we do obtain from the contractor an identification of source, and of estimated price. Our buyers are furnished this information insofar as possible, as a guide to them when a rebuy does occur.

There are many of these 4 million items that are not identified during provisioning, and the only source of knowledge we have at the time one of them happens to require replacement—as occurred in some of Mr. Pike's cases—is to go to the manufacturers' parts manual or tech-

nical manual that he gave us with the equipment, and try to determine the stock number. Frequently the only source available, therefore, is the prime manufacturer himself. Sometimes he will give us a vendor number, in which case we can check it through Battle Creek, Mich., and go to that source, and buy without paying the overhead cost of the prime who produced the end item.

The problem is, there are just millions of items on which we cannot possibly expect to maintain this kind of complete knowledge.

Mrs. GRIFFITHS. Why not? What is wrong with maintaining it?

Mr. MORRIS. Well—

MAINTAINING PRICES WITH COMPUTERS

Mrs. GRIFFITHS. We have all these nice computers, and a whole bunch of people standing around in the Defense Department. Why don't you put them to work?

Mr. MORRIS. Mrs. Griffiths, we think our people work pretty hard. We estimate to do a theoretically perfect job on every small purchase item would take another 10,000 people. We just could not justify the cost. We could not possibly save enough to pay for their salaries.

Mrs. GRIFFITHS. If you put them to work, and you found it out once, and put it on those computers, I don't think you would have any trouble at all maintaining it. And, believe me, if you saved a billion dollars, you could put 10,000 people to work.

\$25 MILLION POSSIBLE SAVINGS ON SMALL ITEMS

Mr. MORRIS. We estimate we can save possibly \$25 million in this particular small purchase area we are talking about—\$25 million. It would cost us at least \$60 million to put enough people on the payroll to check out every possible small buy that could occur over the life cycle of a given piece of hardware.

TOTAL PACKAGE PROCUREMENT

Mrs. GRIFFITHS. I think that you underestimate the amount of money you can save.

I would like to ask you, on this total package procurement—in fact, how much money is involved in total package procurement?

Mr. MALLOY. Mrs. Griffiths, if I may, the total package procurement concept is a new procurement technique that is just now coming into use. The first use of that type of procurement was on the Air Force large purchase of the C-5-A transport, which is about a billion-dollar program in total for over a hundred of those large airplanes.

There were perhaps up to a dozen other large systems—always very large procurements—that used this technique.

The Navy's procurement, for example, of their FDL ships, the fast deployment logistic ships, which did not go through to fruition because of funding problems, was set up on the total package procurement concept.

Mrs. GRIFFITHS. Now, does this mean that the contractor supplies the specifications, then finally bids on the item—or is the person who makes the item; is that right?

Mr. MALLOY. Well, under this type of competition, all of the contractors contending for the contract, compete for the opportunity to do the development work and the production, all in one contract.

Mrs. GRIFFITHS. And how much are you going to breakout of these items and let other people bid on eventually, and how soon?

Mr. MALLOY. Well, it is hard to say how much we should breakout of a given total package procurement. We have, as we indicated in the Secretary's statement, a breakout program specifically for spare parts, and we have other policies that cover breakout of any item where this is in the Government's advantage.

PROCUREMENT OF COMPUTERS

Mrs. GRIFFITHS. How do you purchase new computers? And from whom?

Mr. MORRIS. We have had a very firm policy for several years, under which we endeavor to obtain competition among the several computer manufacturers at the time a new system is being designed. If there is any departure from that, meaning that we go sole source to only one manufacturer, this must come up on a case-by-case basis to me personally for approval. (See app. 10, p. 556.)

DEVELOPMENT OF SPECIFICATIONS BY IBM

Mrs. GRIFFITHS. Well, now, I would like to give you a few things to disapprove.

I understand that for all practical purposes IBM has written specifications and supplied the computers, and that if you break these out, broke out the parts, you would save an astounding sum of money.

I understand further that one computer manufacturer makes an item about as big as that table which would replace in the IBM system an item about half the size of this room. That the IBM part has so many moving parts that it is necessary to buy it in duplicate for one computer.

Why don't you stop this?

Mr. MORRIS. We would be very pleased to investigate the case—

Mrs. GRIFFITHS. Or look into it and supply the information?

Mr. MORRIS. Could you give us more detail?

Mrs. GRIFFITHS. I am telling you. It is IBM. I will give you the name of the part afterward.

Mr. MORRIS. Fine.

DOD DOES NOT OBJECT TO GAO NAMING CONTRACTORS HOLDING EQUIPMENT

Mrs. GRIFFITHS. Now, I would like to ask you this. Do you have any objection to the fact that GAO is going to supply the names of these 21 contractors that are using Government-owned equipment on their own commercial products?

Mr. MORRIS. No, ma'am.

Mrs. GRIFFITHS. Then I would like you also to supply the names of the contracting officers that are permitting this. And the names of any property people. Do you have some property person in the plants?

Mr. MORRIS. Yes.

Mrs. GRIFFITHS. Well, supply those names, too—and I would like to know how much experience those people have had, and what kind of training, and how long the contracting officers have been letting this go along.

I would also like to know what kind of training the contracting officer has that permitted a bid in which the contractor rented the equipment. I am sure you won't have any objection to supplying that.

Mr. MORRIS. We will be glad to respond.

Mrs. GRIFFITHS. The name of the contracting officers and what kind of training they had.

Mr. MORRIS. GAO has not yet identified to us these cases.

Mrs. GRIFFITHS. They are going to. We have got the information that they are going to.

(Information following was subsequently supplied:)

We have contacted the GAO and asked them to supply the names of the 21 contractors covered in their review of the controls of Government-owned property in contractors' plans (B-140389) dated 28 November 1967. When these contractors are identified to us, we will obtain the names of the contracting officers, the property administrators, and supply to the committee the information requested by Congresswoman Griffiths.

(DOD later supplied the following:)

We have considered how to best respond to Mrs. Griffiths' request for the names of the contracting officers who are responsible for permitting contractors to use government-owned equipment for the manufacture of commercial products. We have again reviewed the GAO report dated November 24 covering the use of government-owned property in contractors' plants and we have considered the numerous facilities contracts and the amendments thereto which govern the use of the facilities at plants reviewed by GAO.

It is apparent that the terms and conditions of the contracts, some of which were executed many years ago and which have been amended many times over the years to expand or modify the conditions covering the availability of the government-owned property, were properly executed and were in compliance with the ASPR pending at the time.

The GAO has considered the contract conditions and the individuals involved. In Appendix 2, Pages 85 through 89 of the Report to the Congress dated November 24, GAO has published the names of the principal officers they identified as responsible for the administration of the activities discussed in their report. We believe these officials are properly designated and are, in the final analysis, responsible for the performance of this function. Local contracting officers and property administrators should be held accountable for acting in accordance with published policies and procedures.

With respect to the training which contracting officers receive, the DOD testimony covered briefly the training courses now established to provide uniform joint training and career development in the procurement field. In addition to our regularly scheduled training programs, traveling teams are sent to major procurement activities to orient procurement personnel in new techniques and programs. While not all contracting officers receive training each year, we are trying to maintain schedules which permit 8,000 students each year to complete one or more of the 43 DOD approved courses.

Mrs. GRIFFITHS. Now, I would like to ask you this—because, of course, you see, this is not going to show up as war profiteering, as Mr. Rumsfeld has pointed out, because under the rules a contractor could do that, and under the rules the Renegotiation Board is going to permit him 6 percent on the cost. But, it is going to show up as a real wind-fall when you start handing out the dividends, or start paying the management that thought it up. So, the contracting officer, in my opinion, and the negotiator, did an exceedingly poor job, and the Defense Department ought to be very concerned about that.

SALARIES OF CONTRACTING OFFICERS

Now, I would like to ask you—how much money are you paying these 25,000 procurement personnel? What is the average amount paid a negotiator?

Mr. MORRIS. I would have to supply a precise figure. I think one could use a rough figure of \$10,000.

Mrs. GRIFFITHS. And, what would you say is the largest purchase made by a negotiator that is drawing \$10,000?

Mr. MORRIS. Any major purchase running into hundreds of millions would take an entire team of people to accomplish, of course. But our top negotiators—Mr. Malloy is our top procurement official. He is a grade 18 in the Department of Defense. A grade 18 earns something in excess of \$25,000. The majority of our negotiators are around grade 15.

Mrs. GRIFFITHS. What is the top procurement Mr. Malloy makes? How much money do you spend at one time, Mr. Malloy—a billion dollars?

Mr. MALLOY. Mrs. Griffiths, in my present position as a Deputy Assistant Secretary in charge of procurement on Mr. Morris' staff, I do not personally place any procurements.

Mrs. GRIFFITHS. I see. I would like to know the amount that these people that are paid \$10,000—what is the top purchase that they make.

Mr. MALLOY. I think we would have to do a little research in order to supply that to you.

Mrs. GRIFFITHS. I will give you some research right now, that you won't have to do. I was a procurement official; I was a negotiator. And for \$5,000 I made purchases that amounted to more than \$1 million at one time. I would like to know how much of that is still going on in the Defense Department.

6,094 AWARDS OF \$2 MILLION OR MORE IN 1967

Mr. MORRIS. In fiscal year 1967, contract awards of \$2 million or more numbered 6,094—2 percent of all actions over \$10,000.

Mrs. GRIFFITHS. Because you are dealing with people that are being paid \$500,000 annually. So that you have a situation where people are intimidated. I would like to know—I might say I was not.

I would like to know also what steps the Defense Department took—I read recently where some contractor went down to Cape Kennedy and inquired casually from someone standing around how things were going, and the person told him. He was immediately, at the request of the contractor, demoted. It was at the contractor's equipment he was talking about. How much of that still goes on in the Defense Department, and why did you let him do that?

Mr. MORRIS. Sounds like a rarity to me. To get into a classified site without proper credentials.

Mrs. GRIFFITHS. Well, the contractor—there wasn't a problem at all. I read this in the paper. The man took a year to get his job back.

METHOD OF MAKING LARGE PROCUREMENTS

Mr. MORRIS. I think the public does need to understand the very thoroughgoing way in which large procurements, those of several million dollars and up, are conducted.

There is a team headed by a top negotiator, let's say a \$20,000-a-year man, that contains an engineer, a pricing specialist, and an audit specialist.

Mr. Petty, who is with us here today, runs an organization that spends its major time getting the facts for the negotiators on these important negotiated procurements:

Mrs. GRIFFITHS. Part of the facts that he cannot get are the facts on how much each item in the procurement costs, because you have already told us you do not have that.

Mr. MORRIS. In connection with his analysis during the negotiating phase, he goes into bills of material, our engineers determine what kind of fabrication methods are to be used, and so forth.

Mrs. GRIFFITHS. He cannot break it down very far—because you have said you do not have that information.

Mr. MORRIS. We are talking about different things, I believe.

Mrs. GRIFFITHS. Well, I am not.

Mr. MORRIS. We were speaking earlier of spare parts in the supply system.

Mrs. GRIFFITHS. But, if you cannot build up the price, part by part, Mr. Secretary, you are lost.

Mr. MORRIS. We do build up the price in respect to—

Mrs. GRIFFITHS. If you can build it up part by part then, why can't you build it up when you have a spare part alone. Why don't you know the price then?

Mr. MORRIS. There is quite a difference in buying a thousand—

Mrs. GRIFFITHS. No, there is not.

Mr. MORRIS (continuing). Tanks as part of a major procurement, and later having to replace a part on one of those tanks.

Mrs. GRIFFITHS. If you know the price of one part for any purpose, then you know the price of that part for all purposes. Now, you may not know whether you are making that—whether you have a whole factory set up to run off that part, or whether you have a factory set up to run off a hundred thousand of those parts. But I would not think you would have much trouble.

Mr. MORRIS. We wish we had you back in the Department.

PROPERTY HELD BY CONTRACTORS

Mrs. GRIFFITHS. I will tell you now—we would save some money.

We were talking yesterday about the property owned by the Government, that Federal contractors have. Would you furnish us a list of the contractors and the amount of property by classes that each holds?

PARTIAL LIST OF CONTRACTORS HOLDING GOVERNMENT PROPERTY

Mr. MORRIS. We will endeavor to be responsive. This might become quite a list.

(The following was later supplied for the record:)

Approximately 5,500 manufacturers have some government Industrial Plant Equipment. The value of this equipment varies; however, one third of the firms have government equipment valued at more than \$50,000. Further, contractors have plants in several locations, particularly large corporations such as General

Electric or General Motors, and the list would be extremely large. Procurement agencies in all three military departments and DSA, who have the responsibility for maintaining the records, would have to be surveyed to acquire the data, which would take several weeks to accomplish. The following examples of active IPE in major contractor's plants indicate the magnitude of the problem, but show that records are in fact maintained.

Company	Number of items	Value	Number of locations
Aerojet General.....	3,583	\$45,628,738	12
Aerospace Corp.....	1,438	6,976,060	3
Boeing Co.....	3,232	36,403,822	18
Curtiss-Wright.....	2,103	35,733,313	6
Hughes Aircraft.....	5,031	23,153,820	11
Ling-Temco-Vought.....	2,923	41,823,449	6
Northrop Aircraft.....	2,471	23,900,585	16
Thiokol Chemical Corp.....	2,212	23,172,595	6
T-R-W, Inc.....	3,215	58,408,383	13
United Aircraft.....	2,080	35,860,094	8
Total.....	28,288	331,051,859	99

(See also app. 4(a) and 4(b), pp. 411, 463.)

Mrs. GRIFFITHS. Might take quite a long time. Since you do not have any records now.

Mr. MORRIS. We have records. I can assure you.

Mrs. GRIFFITHS. Easily available?

Mr. MORRIS. We know where the industrial plant equipment is. This is one of the responsibilities of each department, and of the Defense Industrial Production Equipment Center.

(On Jan. 15, 1968, the Department of Defense supplied the additional material below:)

ASSISTANT SECRETARY OF DEFENSE,
Washington, D.C., January 15, 1968.

Hon. WILLIAM PROXMIRE,
Chairman, Joint Economic Committee, Congress of the United States, Washington, D.C.

DEAR Mr. CHAIRMAN: This is in reply to two letters received from you dated 28 December 1967 wherein you requested a revised listing of Government-owned equipment located in individual contractor's plants, and other information.

On Friday, 12 January 1968, a copy of a tabulation was hand carried to Mr. Ray Ward showing, by contractor, the dollar value of Government equipment furnished by each of the military services as of 30 November 1967. Similar data for the end of fiscal years 1964, 1965, 1966 and 1967 are being prepared and will be forwarded to you by the end of January 1968. In addition, according to your request, we are preparing a further breakdown showing the value of Government-owned Industrial Plant Equipment at each of the foregoing dates, which the Department of Defense as a whole had furnished to various classes of industry. This summary will also be furnished to your committee by the end of January 1968.

In response to your query as to the method used to ascertain the value of other plant equipment in contractor's plants, I would like to iterate that financial reports of the value of this equipment are not centrally recorded, but are maintained by property administrators at the field level. However, each year a summary report is requested for a report to the Congress of real and personal property. It was from this summary report that the \$2.0 billion other plant equipment value was obtained. As I mentioned in my letter of 21 December 1967, a special report of this equipment as of 31 December 1967 will be available during February 1968. I will forward such detail to you then if it is still desired.

In order to clarify your specific questions regarding the value of industrial plant equipment located at Olin Mathieson's Saltville, Virginia facility, I am attaching a fact sheet containing full details of this matter. The amounts of \$3.3 million IPE and \$1.4 million real property are correct as of the 30 November 1967 data transmitted to you in my letter of 21 December 1967.

I would also like to take this opportunity to clarify a matter covered during hearings before your committee pertaining to the number of industrial plants holding Government property. Approximately 5,500 plants were cited during the hearings. Actually as of 30 November 1967, under our criteria, there were 5,361 plants, of which 2,256 possessed IPE, and the balance of 3,105 possessed only other plant equipment, material, or special tools and test equipment.

Sincerely,

THOMAS D. MORRIS,
Assistant Secretary of Defense
(Installations and Logistics).

(See p. 197.)

FACT SHEET—GOVERNMENT INVESTMENT IN PLANT EQUIPMENT AND FACILITIES—
OLIN MATHIESON CHEMICAL CORPORATION, SALTVILLE, VIRGINIA

1. The Olin Mathieson's Saltville, Virginia facility consists of two (2) separate plants: (a) the Air Force Plant No. 80 complex and (b) the contractor-owned plant, which is a chemical facility and contains only \$6,100 in Government-owned machines tool inventory.

2. The amount of \$15.6 million reported to Congress by the General Accounting Office included the Government's total investment at the two plants at Saltville. This \$15.6 million investment includes the acquisition cost of Industrial Plant Equipment (IPE) as well as the following.

a. \$1.4 million for Government-owned *real property* at Air Force Plant No. 80.

b. \$3.3 million for Industrial Plant Equipment (includes above mentioned \$6,100 of machine tools).

c. \$1.3 million for equipment other than IPE. (Other than IPE items include equipment the acquisition cost of which is less than \$1,000 and which is not centrally controlled by DIPEC but managed by the property administrators.)

d. \$2.2 million investment for the *installation* of Industrial Facilities.

e. \$2.7 million for Government-owned non-severable items located on contractor-owned property. These items were provided under a "buy back" agreement in the facilities contract and consist of such items as water mains, sewers, boiler house, and water treatment equipment. Such non-severable equipment (when it is not on Government-owned land) is not reportable as real property.

f. \$4.7 million for indirect costs (such as A&E) related to the procurement of the industrial facilities.

3. Summary of the \$15.6 million *investment*:

	<i>Millions</i>
(a) Real property-----	\$1.4
(b) IPE-----	3.3
(c) Other than IPE-----	1.3
(d) Installation costs-----	2.2
(e) Nonseverable Government-owned facilities-----	2.7
(f) Indirect costs-----	4.7

Total investment----- 15.6

4. Summary of the \$4.7 million *acquisition cost* of IPE and real property.

	<i>Millions</i>
(a) Real property-----	\$1.4
(b) IPE-----	3.3

Total acquisition cost----- 4.7

Mrs. GRIFFITHS. Thank you. My time is up.

CONTRACTORS REQUIRED TO REPORT ON PROPERTY

Mr. MALLOY. If I might, Mr. Chairman, just to elaborate on that—we do require contractors to give us reports—I believe it is 12 months' intervals—of the total value of Government property in the possession of contractors and these figures are reported and usually to the Congress. So we can provide that type of information.

Mrs. GRIFFITHS. If they do that, then why did the GAO find a person who said that it would take 20 men a year to identify the Government-owned property in his plant?

Mr. MALLOY. Well, I don't really think that was the situation in the GAO report. They were talking there about keeping detailed utilization records on all items of industrial plant equipment, even though costing \$1,000 or \$1,200. That was the discussion as to how much administrative cost that entailed.

Mrs. GRIFFITHS. Well, they were talking also just about identifying it.

Let me explain to you that I still have some friends that work on some of these problems, and they have told me that when some of this property goes into a contractor's plant, it is lost right then. There is no identification whatsoever. I think you ought to be quite clear on checking this out, because I do not think you have records.

Thank you very much, Mr. Chairman.

Chairman PROXMIRE. Congressman Curtis.

Mr. CURTIS. Thank you, Mr. Chairman.

First, let me say how pleased I am to see you back, Mr. Secretary, in this position, and say that I think you have made a good progress report—what I said in commenting to GAO that I look upon these only as progress reports. We are right in the middle still of a most difficult and probably never-ending area of improvement.

I was pleased to receive the emphasis in this report on training personnel in the procurement area.

As you know, your previous progress reports had developed to some degree what you were doing in the contract service area of creating a special corps.

When you were talking about procurement people, I assume you are talking about the original procurement, and not service contracting personnel. Is that right? Contract servicing personnel?

Mr. MORRIS. I believe we are in agreement there; yes, sir.

Mr. CURTIS. I think it is important to distinguish the two groups, because as I understand it you have one group that handles the original procurement, and then a different group that actually works on the administration of that particular procurement contract?

Mr. MORRIS. That is right, sir—checks the deliveries, pays the bills, does the inspection work.

Mr. CURTIS. And those people are largely out in the field, I guess, at the plants where these materials are being produced to comply with the contracts?

Mr. MORRIS. Many of them are, sir. Others work out of central offices.

DEVELOPING A SPECIAL CORPS

Mr. CURTIS. I thought it was excellent, as I say, that you—that the concept was initiated of developing a corps, which would include, I would imagine, promotions within that group, special on-the-job training, and out-of-job training and so on.

I wish you would supply for the record a little progress report on where we are, that would update us. I think the last time was about a year ago.

Mr. MORRIS. Be glad to.

(The following material was subsequently filed by the Department:)

On-the-job training is a continuous program at all supervisory levels of management. It is a responsibility given to all supervisors—written into their job descriptions. This type of training takes shape in the form of “show or tell” at the employees desk, written instructions and orientation of new employees to their job.

There are both planned and “when required” type of meetings held by supervisors to continuously update their personnel.

There is local training based upon formalized courses offered by the Army Logistics Management Center, Fort Lee, Virginia. Many Military installations, by the use of their own personnel for instructors, use course material from ALMC in classroom type of training during office hours.

To supplement the “on-the-job” as well as “out-of-the-job” training, local schools and colleges are used in after duty hours classes. There is also the self development effort by employees in the use of extension or correspondence courses offered to them by the Services.

The Department of Defense has resident and traveling training courses of study for the functional areas of procurement and contract administration. In addition, there are other courses of study related to these functional areas, such as, automatic data processing, management techniques, etc.

Listed below is the index of courses listed by schools. The key to the abbreviations is as follows:

(JT) Courses offered in conformance with Department of Defense Directive 5010.9 “Defense Logistics Management Training Program”.

(AF) Service peculiar courses offered by the Air Force.

(AR) Service peculiar courses offered by the Army.

(Joint Proc) Courses approved by the Defense Procurement Training Board.

The traveling courses of study (taken to the field activities) are those listed as Navy Sponsored Courses shown under the heading “Headquarters Naval Material Command.” There is one exception at the present which is the “Defense Procurement Executive Refresher Course” now located in Washington, D.C.

The courses for procurement are identified with a “P” and the contract administration with a “C”. Where there is an interest for both functional areas, it is marked with a “PC”.

Following the index of courses is the career (Master) development chart for the Civil Service Commission procurement career field. This shows the basic training requirements for advancement in this series. The quality assurance (inspection), production and engineering functional areas that are associated with contract administration area do not have similar basic requirements for advancement.

DoD 5010.9-C

INDEX OF COURSES LISTED BY SCHOOL

COURSE NUMBER	TITLE	PAGE NUMBER	COURSE NUMBER	TITLE	PAGE NUMBER
Department of Defense Computer Institute (DODCI)			475	Laboratory Management of Research and Development (AF)	70
Washington Navy Yard Annex Washington, D. C.			580	Logistics Management (AF)	84
			210	Maintenance Management Information Systems (JT)	45
DoD CI	Command and Control ADP Systems Course (JT)	24	242	Maintenance Management Orientation (JT)	46
DoD CI	Intermediate Executive Course (JT)	24	560	Management of Value Engineering in Defense Contracting (Joint Proc)	95
DoD CI	Senior Executive Course (JT)	25	269	Production Management (Joint Proc)	67
Air Force Institute of Technology Defense Weapon Systems Management Center Wright-Patterson Air Force Base, Ohio			370	Program Evaluation Review Technique (PERT/Time and PERT/Cost) (AF)	48
			440	Quality Control Management (Joint Proc)	78
Defense Weapon Systems Management Course (JT)		71	189	Quantitative Methods in Cost Analysis (JT)	61
Air Force Institute of Technology School of Systems and Logistics AFIT-SL Wright-Patterson Air Force Base, Ohio			435	Reliability (AF)	76
			375	Scientific and Technical Information (JT)	31
178	Advanced Contract Administration (Joint Proc)	57	418	Statistical Quality Control I (Joint Proc)	78
191	Cost Analysis (JT)	58	428	Statistical Quality Control II (Joint Proc)	79
252	Advanced Maintenance Management (AF)	48	570	System Program Management (AF)	70
279	Advanced Production Management (Joint Proc)	66	365	Systems Simulation for Analysts and Programmers (AF)	29
172	Advanced Systems Buying (JT)	58	232	Weapon Systems Maintenance Management (AF)	46
130	AMA Directorate of Materiel Management (AF)	79	USAF Air Training Command Amarillo AFB, Texas		
165	Base Procurement/BCE Related Management (AF)	59	823	Defense Metals Identification (JT)	73
550	Base Supply Management (AF)	81	AZR 61170-1	Redistribution and Marketing (AF)	74
168	Business Law (AF)	59	OBR 6421	Supply Operations Officer (AF)	86
175	Contract Administration (Joint Proc)	60	OAR 6411	Supply Staff Officer (AF)	85
166	Contract Law (JT)	60	OZR 6534-1	Advanced Base Procurement Management (AF)	57
176	Cost Reimbursement Incentive Contracting (JT)	61	USAF Air Training Command Chanute Air Force Base, Illinois		
380	Defense Data Management (JT)	30	OAR 4311	Aircraft Maintenance Staff Officer (AF)	43
385	Engineering Data Management (AF)	34	OBR 4341	Aircraft Maintenance Officer (AF)	44
192	Evaluating Contractors' Estimating Systems (Joint Proc)	65	OZR 4344	Maintenance Analysis (AF)	45
	Graduate Logistics Course (AF)	31			
222	Industrial Maintenance Management (JT)	44			
160	Industrial Property Administration (Joint Proc)	65			
150	Initial Provisioning (AF)	83			
355	Intermediate Management Information Systems (AF)	29			

COURSE NUMBER	TITLE	PAGE NUMBER	COURSE NUMBER	TITLE	PAGE NUMBER
USAF Air Training Command Sheppard AFB, Texas			8B-F5	Missile Packaging (JT)	53
OBR 6721	Accounting and Finance Officer (AF)	100	8B-F4 • C	Packaging Administration (JT)	52
OZR 6784	Auditing Data Processing Systems (AF)	23	8B-F16	Packaging Design (JT)	56
OAR 6731	Budget Officer (AF)	100	8B-F2	Packing and Carloading (JT)	53
AZR 68750	Computer Programming (AF)	27	8B-F7, 822-F7	Preparation of Freight for Air Shipment (JT)	54
ARZ 68750-1	COBOL Programming (AF)	26	8B-F1, 822-F1	Preservation and Intermediate Protection (JT)	55
OZR 6834	Data Systems Analysis and Design (AF)	29	8B-F3 • C	Preservation and Packaging (JT)	56
OZR 7500-2	Development and Management of Training Materials (AF)	75	8B-F19	Preservation for Shipment or Storage of Fixed- or Rotary-Wing Aircraft (JT)	104
OBR 6851	Electronic Data Processing Officer (AF)	100	U. S. Army Finance School Fort Benjamin Harrison, Indiana 46216		
AZR 68750-2	FORTRAN Programming (AF)	27	7E-F5	Auditing of Automatic Data Processing Systems (AR)	101
AZR 68750-3	JOVIAL Programming (AF)	27	7E-F20/ 531-F4	Financial Management Systems-Automated Application (AR)	101
OBR 6891	Management Analysis Officer (AF)	34	7D-F6/ 541-F3	Internal Review (AR)	101
OAR 6011	Transportation Staff Officer (AF)	88	7D-F1	Military Comptrollership (AR)	102
USAF TTC Keesler AFB, Biloxi, Mississippi			7D-F5/ 541-F2	Programming and Budgeting (AR)	102
OAR 3011	Communications - Electronics Staff Officer (AF)	106	7D-F4/ 541-F1	Techniques of Review and Analysis (AR)	103
OBR 3031	Communications Officer (AF)	106	U. S. Army Intelligence School Fort Holabird, Maryland 21219		
USAF TTC Lowry AFB, Denver, Colorado			3C-F8 • C	Advance Industrial Security Course (Joint Proc)	96
OZR 6534 • P	Advanced Base Procurement Management (AF)	57	3C-F7 • C	Basic Industrial Security Course (Joint Proc)	96
OAR 3211	Avionics Staff Officer (AF)	105	3C-F9 • C	Industrial Security Administrative Course (Joint Proc)	97
OBR 7431	Management Engineering Officer (AF)	105	3C-F5 • C	Industrial Security Management Course (Joint Proc)	97
OBR 6531-1 • P	Procurement Officer (AF)	105	3C-F6 • C	Industrial Security Orientation Course (Joint Proc)	98
PERT Orientation and Training Center Vanguard Building 20th & L Streets, NW, Washington, D. C.			United States Army Logistics Management Center Fort Lee, Virginia 23801		
• P C	PERT Orientation Executives (Joint Proc)	49	8A-F1 • P C	Army Logistics Management (AR)	80
• P C	PERT Orientation Middle Management Training Workshop (Joint Proc)	49	8A-F5	Associate Army Logistics Management (AR)	80
Joint Military Packaging Training Center Aberdeen Proving Grounds, Aberdeen, Maryland 21005			8B-F17 • C	Defense Advanced Disposal Management (JT)	72
822-F4 • C	Basic Packaging (JT)	50	8A-F2	Army Project Manager (AR)	67
8B-F6, • C	Equipment Preservation for Shipment or Storage (JT)	51	*Nonresident courses are offered in these subjects. See Section 5, paragraph B.		
8B-F8, 822-F8	Inspection of Packaged and Packed Household Goods for Storage and Shipment (JT)	51			

COURSE NUMBER	TITLE	PAGE NUMBER	COURSE NUMBER	TITLE	PAGE NUMBER
8B-F12	Defense Advanced Inventory Management (JT)	82	7E-F18	Introduction to ADP System Analysis and Design (JT)	99
8D-F12 • PC	Defense Advanced Procurement Management (JT)	62	7E-F15 • PC	Management Statistics (JT)	21
8B-F10*	Defense Depot Distribution Management (JT)	83	7A-F26	Managerial Communication (JT)	41
8B-F18 • C	Defense Disposal Executive Development Seminar (JT)	74	8D-F28	Managing the Value Engineering Program (JT)	95
8A-F12	Defense International Logistics Management (JT)	33	5L-F2	Managing Research and Development Activities (JT)	30
8B-F11*	Defense Inventory Management (JT)	82	7C	Manpower Validation (AF)	35
5K-F1	Defense Logistics Instructor Development (JT)	84	5A-F1	Mathematical Programming (JT)	21
8D-4310/• PC	Defense Procurement Management (Joint Proc)	63	7A-F24	Methods-Time Measurement (MTM) (JT)	36
8D-F1*	Defense Specification Management (JT)	63	7A-F9 • PC	New Organization Concepts for Top Management (JT)	37
8A-F3*	Maintenance Management (AR)	47	7A-F12	Operations Research Appreciation (JT)	22
8D-F18 • C	Quality Control Management (Joint Proc)	78	7A-F8	Organization Planning (JT)	37
5L-F3	Research & Development Management Orientation (AR)	103	7A-F13	PERT/Cost (AR)	48
	*Nonresident courses are offered in these subjects. See Section 5, paragraph B.		7A-F14	PERT/Cost Appreciation (AR)	50
			8D-F27 • PC	Principles and Application of Value Engineering (Joint Proc)	94
			5A-F3	Probabilistic Methods in Operations Research (JT)	22
			7A-F15	Quantitative Decision Making (JT)	23
			5L-F1	Project Planning and Control Techniques (JT)	71
			8D-F21 • C	Quality Assurance Appreciation (JT)	68
			8D-F18 • C	Quality Control Management (Joint Proc)	78
			7A-F16	Real Time Systems (JT)	37
			7A-F28 • PC	Reliability Program Management (JT)	77
			7E-F16 • C	Sampling Procedures for Reliability Testing (JT)	76
			7A-F6 • PC	Seminar for Chiefs of Management Offices (JT)	38
			7A-F5 • PC	Seminar for Middle Managers (JT)	36
			8D-F22 • C	Seminar for Quality Managers (AR)	78
			7A-F17	Standard Time Data (JT)	38
			8D-F23 • C	Statistical Quality Control I (Joint Proc)	78
			8D-F24 • C	Statistical Quality Control II (Joint Proc)	79
			7A-F18	Systems and Procedures Analysis (JT)	39
			7A-F27	Techniques of Managerial Communication (JT)	42
			7A-F25 • PC	Top Management Seminar (JT)	41
			7A-F19	Work Methods and Standards (JT)	39

**U. S. Army Management Engineering Training
Agency, Rock Island, Illinois 61202**

7E-F7 • PC	Automatic Data Processing Appreciation (JT)	24
7E-F11	Common Business Oriented Language (COBOL) (JT)	26
7E-F10	Computer Programming (JT)	28
8D-F26 • PC	Contractor Performance Evaluation (Joint Proc)	69
7E-F8	Data Collection and Transmission Appreciation (JT)	28
7E-F17	Data Processing Profitability and Application Studies (JT)	99
7E-F19	Defense Computer Installation Management Seminar (JT)	25
7E-F13	Design and Analysis of Experiments (JT)	21
8D-F19	Designing Quality Programs (AR)	75
7A-F10	Economic Analysis for Decision Making (JT)	33
5A-F2 • C	Elements of Reliability and Maintainability (JT)	76
8D-F20 • C	Evaluation of Producer's Quality Programs (JT)	77
7D-F7	Financial Management for Managers (JT)	34
8D-F25 • C	Inspection Planning (JT)	77

COURSE NUMBER	TITLE	PAGE NUMBER	COURSE NUMBER	TITLE	PAGE NUMBER
7A-F20 • PC	Work Methods and Standards Appreciation (JT)	68	U. S. Naval School Transportation Management Naval Supply Center Oakland, California		
7A-F21	Work Planning and Control (JT)	40			
7A-F22 • PC	Work Planning and Control Appreciation (JT)	40			
5L-F2	Managing Research & Development Activities (JT)	30			
U. S. Army Transportation School Fort Eustis, Virginia 23604					
822-F10	Air Transportability (AR)	93		Advanced Transportation Management (NV)	91
8C-F2	Air Transportability Planning (AR)	93		Air Traffic Management (NV)	92
8C-F3 • C	Defense Advanced Traffic Management (JT)	86		Cargo Handling (NV)	107
8C-F4 • C	Installation Traffic Management (AR)	89		Intermediate Transportation Management (NV)	91
U. S. Army Armor School Fort Knox, Kentucky 40121				Introduction to Transportation Management (NV)	91
8A-F8/ 510-F2	Command Maintenance Management Inspection, Inspector (AR)	46		Management Techniques for Distribution Officers (NV)	94
8A-F13	Junior Officers' Preventive Maintenance (AR)	43		Marine Terminal Management (NV)	90
8A-F20	Senior Officers' Preventive Maintenance (AR)	42		Transportation Management (NV)	90
U. S. Army Quartermaster School Fort Lee, Virginia 23801				Transportation Staff and Planning Function (NV)	94
AZA-60750	Airdrop Loadmaster (AR)	92		Warehouse Operations (JT)	88
AN-461A/860-43E2P			Headquarters Naval Material Command (MA10213) and Field Locations (See Schedule of Navy Sponsored Courses)		
8F-4210	Army-Air Force Exchange Operations (AR)	89	CM • PC	Art and Technique of Negotiating Contract Modifications (Joint Proc)	59
8G-4223/ 551-F2	Commissary Management (AR)	88	PN • PC	Cost and Price Analysis and Negotiation Technique (Joint Proc)	61
8G-F2/ 551-F3	Defense Metals Identification (JT)	73	ER • PC	Defense Procurement Executive Refresher Course (Joint Proc)	62
8E-A114/ 941A	Food Service Supervision (AR)	87	IC • PC	Defense Advanced Incentive Contracting Workshop (Joint Proc)	64
8E-F2/ 801-F1	Open Mess Management (AR)	35	IS • PC	Defense Incentive Contract Structuring Workshop for Top Management (Joint Proc)	64
4N-461A/ 860-43E2P	Parachute Packing, Maintenance and Airdrop (AR)	92	MY • PC	Defense Multi-Year Procurement and Two-Step Formal Advertising Seminar (Joint Proc)	65
8B-4960	Petroleum Officer (AR)	85	SP • P	Defense Small Purchase Course (Joint Proc)	63
8G-F1 • C	Property Disposal Operations (AR)	72	MT • C	Procurement Management For Technical Personnel (Joint Proc)	66
822-F9			TS • PC	Termination Settlement and Negotiation (Joint Proc)	66
8D-4130	Subsistence Officer (AR)	87			
U. S. Naval Postgraduate School Monterey, California					
• PC	Defense Management Systems Course (JT)	32			

FIGURE III
MASTER DEVELOPMENT PLAN

	Business Analyst GS-1101	Procurement and Production GS-1102	Contract Administration GS-1102	Price Cost Analyst GS-1102	Industrial Property GS-1101	Industrial Specialist GS-1101
59. Planning and Control of Business Management						
58. Administrative Techniques for Managers						
57. Communication Techniques for Managers						
56. Problem in Supervision						
55. Advanced Seminar for Federal Executives						
54. Systems and Procedures						
53. Electronic Computers in Business						
52. Introduction to Management Theory						
51. Emergency Management of the National Economy (Correspondence Course)						
50. Human Relations Workshops and Seminars on Trends in						
49. Personal Management (Varying)						
48. Senior Executive Course (50-hours)						
47. Personnel Management for Executives (8-Day Conference)						
46. Effective Scheduling						
45. Business Communication						
44. Defense Material Management						
43. Top Management Seminar						
42. Defense Management Systems (Budgeting, Programming, Analysis)						
41. Technical, Analytical and Systems Courses for Managers (Varying)						
40. Defense Procurement Executive Refresher Course (1 week)						
39. Managing the Value Engineering Program						
38. Administrative Analysis and Research (Varying)						
37. Management and Control of Production (1 week)						
36. Automatic Skills Improvement (1 Semester)						
35. Principles of Industrial Management (1 Semester)						
34. Fundamentals of Management (Varying)						
33. Work Simplification (Varying)						
32. Conference Leadership (Varying)						
31. Quality Assurance Abstracts (12 weeks)						
30. Statistical Quality Control (1 week)						
29. Statistical Quality Control (12 weeks)						
28. Local Analysis for Business Managers (Varying)						
27. Operations Research (1 week)						
26. Statistical Quality Control I (2 weeks)						
25. Technical, Analytical and Systems Oriented Courses (Varying)						
24. Management Statistics (12 weeks)						
23. Statistical Quality Control (6 weeks)						
22. Introduction to Supervision (5-12 hours)						
21. Defense Advanced Procurement Management (3 weeks)						
20. PMU/Cont (1 week)						
19. Advanced Contract Administration (3 weeks)						
18. Advanced Systems Buying (2 weeks)						
17. Art and Technique of Negotiating Contract Modifications (1 week)						
16. Cost Estimation and Application of Value Engineering (2 weeks)						
15. Cost Control Management (2 weeks)						
14. Quality Control Management (2 weeks)						
13. Defense Advanced Incentive Contracting Workshop (1 week)						
12. Termination Settlement and Negotiation (6 Days)						
11. Cost Analysis and Contract Cost Principles (ASAP Sect. IV: 1 week)						
10. Management of Value Engineering in Defense Contracting (1 week)						
9. Contract Law (12 weeks)						
8. Contract Law (4 weeks)						
7. Cost and Price Analysis and Negotiation Seminar (Part I - 2 weeks; Part II - 1 week)						
6. Defense Small Purchases (1 week)						
5. Production Management (7 weeks)						
4. Industrial Property Administration (3 weeks)						
3. Contract Administration (5 weeks)						
2. Defense Procurement Management (5 weeks)						

LEGEND:

*Mandatory

#Mandatory, if required by the mission

NOTE: Courses (or equivalent as determined by established tests or by the OSD(I&L) Coordinator for Defense Management and Education) identified by * or # must be completed within 12 months of the date of promotion to the next level or in the senior level to the next grade.

May 1966

Mr. CURTIS. How many people are in that particular corps. I understand you have 25,000 in the procurement area?

DCAS HAS A STAFF OF 23,000

Mr. MORRIS. In the DCAS, Defense Contract Administration Service, I believe another 21,000, approximately, at this time. General Hedlund can correct me.

General HEDLUND. About 23,000.

Mr. CURTIS. About 23,000. Has anything been done to develop the procurement officers, the procurement personnel, into a comparable concept of a corps?

Mr. MORRIS. Yes, sir. We have during the past 3 years been developing a career promotional program for what you have described as the original buyers. For example, we now have at Ogden, Utah, a central data center where we have the complete personnel history record on all personnel in grades 13 and above, including their periodic performance evaluations. As a vacancy occurs in any military department or DCAS, that central data bank must be interrogated by the organization having the vacancy. The data bank furnishes a list of the 20 top people located anywhere in the Department of Defense who are eligible for consideration for that opening.

Mr. CURTIS. But, you do not have the procurement group formalized to the extent that you have the contracting service people.

Mr. MORRIS. It is not a centralized organization, no sir. It is decentralized among the three military departments and DCAS.

Mr. CURTIS. Why, if you found it valuable in the contract servicing area, wouldn't it be valuable in the procurement area?

Mr. MORRIS. We have centralized procurement of common-use items in the Defense Supply Agency. That is a movement in the direction that you speak to, sir.

Procurement people, however, in terms of these complex and large contracts, must be closely associated with the systems design people, the engineers and the program managers, such as in the purchase of the C-5-A, for example. They must work hand in hand, day to day with those people who know how to make the most prudent buys. You could not centralize those people physically without denying the Department of the best kind of procurement planning correlated with development and design planning.

Mr. CURTIS. You are advancing me a theory. You are giving me an argument of why you are not—which certainly is to be borne in mind.

On the other hand, inasmuch as we are talking essentially about techniques, rather than specific knowledge—although you certainly do have to have knowledge—but the techniques, I think, probably at this stage are much more important. The techniques of procuring ought to be similar. In fact, that is the very reason, as I understand in your report here, you are calling them in and giving them these lectures and the training films and so on—because you do recognize that the techniques—

Mr. MORRIS. This is quite true, sir. Our training program of 43 courses is a centrally administered program available to all of these people. We bring them in for these purposes.

Mr. CURTIS. If I may be pardoned for uttering a suspicion, it seems to me what you really run into is the same fight we always do from the three services. If you leave them to themselves, of course, they want control over any branch they can. We have never even coordinated the Chaplains' Corps, or the procurement of materials for the chaplains in the Army, Navy, and Air Force. We are still worshipping God according to the Army, Navy, and Air Force, and so it is here.

I recognize these arguments, and some of them have validity. But with this situation we have, the vast quantities, and the need for these improved management techniques, that should be overriding. We cannot afford, in my judgment, this parochialism. And I think—I hope that just as you were able to gird your loins and develop the Service Contracting Corps, you would move toward this. Maybe you are and maybe this is just one of these problems that you just have to fight out with finesse.

1.8 MILLION ITEMS UNDER INTEGRATED MANAGEMENT

Mr. MORRIS. I think the important fact is that since 1961 we have brought 1.8 million items under integrated management, including procurement of those items, whereas there were only 40,000 in 1961.

Mr. CURTIS. If I were training procurement officers, I would train them in one common school, and then let them go to the Navy, Army, or Air Force, whichever happened to be the service—but I would know they were following what is our best information of good procurement practices.

COMMON SCHOOLS FOR PROCUREMENT

Mr. MORRIS. This we are doing, sir. We have common schools for all military departments and DSA, in the procurement field.

Mr. CURTIS. All the more reason for following it out and developing a corps that would develop this esprit de corps and exchanging of knowledge.

Mr. MORRIS. We agree, sir.

AUDIT GROUP SEPARATE FROM PROCUREMENT AND SERVICE CONTRACT GROUPS

Mr. CURTIS. Now, there is a third group, as I understand—there may be more—but then you have your audit group. They are separate and distinct from your procurement people, your Service Contract people. Am I correct?

Mr. MORRIS. That is correct, sir.

Mr. CURTIS. How is that group developing? What is the stage of its development along a corps concept, or is it still separated into the three services?

Mr. MORRIS. I think we have made much progress here. There is a Central Defense Contract Audit Agency. The head of this agency, Mr. Petty, is with us, and he may wish to comment on your question.

DCAA A SINGLE AGENCY

Mr. PETTY. We are a single agency. We have no parts in Army, Navy, or Air Force.

Mr. CURTIS. So you really are a corps?

Mr. PETTY. We have reached the point you are suggesting that these kinds of activities should reach.

Mr. CURTIS. Very good.

Have I missed any major group in this process—procurement, servicing, and auditing?

Mr. MORRIS. Those are the key tools of the whole procurement process, sir.

Mr. CURTIS. I just want to be sure.

By the way, about how many do we have in auditing? What is the total personnel?

DCAA HAS STAFF OF 3,900

Mr. PETTY. We have about 3,900 people on board in the Defense Contract Audit Agency at this time.

Mr. CURTIS. I see.

One other thing I would like—and this can go for the record. Most of these personnel in all three of these services are civilian rather than military. Am I correct in that?

Mr. MORRIS. The large majority are civilian.

Mr. CURTIS. There are in each one military personnel?

Mr. MORRIS. That is correct, sir. And they are exposed to the same kind of training the civilian gets.

ROTATION OF MILITARY STAFF

Mr. CURTIS. But your military personnel tend to be on this rotation system that you have in the military, which detracts, I would think, from this kind of concentration. Am I right in that statement?

Mr. MORRIS. More and more of the services are tending to professionalize people in the procurement occupation—the military personnel.

Mr. CURTIS. Yes. But they cannot professionalize if they rotate them. That is my point.

Mr. MORRIS. If the rotation is within the procurement organization or complex generally, it keeps building their expertise. You are quite right that they are rotated to nonprocurement jobs very frequently, and this does inhibit full career specialization.

Mr. CURTIS. There may be a reason. I am not arguing against it. Just trying to understand.

NO MILITARY PEOPLE IN DCAA

Mr. PETTY. I would like to comment that the Defense Contract Audit Agency is now an entirely civilian organization. We have no military personnel assigned.

Mr. CURTIS. Very good.

I would be interested in—

Chairman PROXMIRE. May I ask—before this gentleman sits down—Mr. Petty, will you identify yourself?

Mr. PETTY. William B. Petty, Director, Defense Contract Audit Agency.

Chairman PROXMIRE. Thank you, Mr. Petty.

MILITARY PEOPLE IN SERVICE AND PROCUREMENT AREAS

Mr. CURTIS. I would appreciate, for the record, what reason there might be—and there could be good reason—why you think you need military personnel in the service contract area, and in the procurement area.

Mr. MORRIS. Be very glad to give you this, sir.

Mr. CURTIS. And then, also, what are the ratios. You have, say, 25,000 in procurement; about how many would be military, would you say?

Mr. MORRIS. Let us furnish that for the record.

Mr. CURTIS. And, also, in the service contract; you have some there, too?

Mr. MORRIS. Fine, sir.

(The information furnished for the record follows:)

In the Procurement area the ratio military to civilian is approximately 3.5%.

In the Contract Administration area staffing runs approximately 23,000 in Defense Contract Administration Services and 17,000 in the Services, or a total of 40,000. The ratio military to civilian is approximately 3%.

Military personnel are rotated from *operating billets* to procurement and contract administration assignments and bring to these positions the experience of the "field operations". To put it differently, the military "front line" experiences with end products or the end of the line in logistics support, can, when rotated back to the procurement or administration job, aid in improving the contracting for and administration of contracts.

PRICE REDETERMINATION

Mr. CURTIS. Now, I get to the thing I am most concerned about. The relationship between the three services. Maybe I can zero in on the question I have asked before.

In your redetermination clauses, price redetermination, as I understand it your procurement group is the one that does this—not the service group or the audit. Am I right?

Mr. MORRIS. This is a negotiator's responsibility, I believe.

Mr. MALLOY. That is correct. We do not have many redetermination type contracts these days. But, if we were to take a type of contract we do use such as an incentive contract, the actual negotiation of the final pricing is done by the procuring contracting officer. However, he has had all of the support that he needs from both the Contract Audit Agency reports and the reports of the contract administration people in the field. These are support to him.

Mr. CURTIS. Well, this is what I am looking to see—to the extent—I know that is the ideal, or I would hope it is the ideal, and you are stating it reassures me of that.

I do have a concern as to how well it works, because it seems to me, whether you call it incentive contracts—it is the same thing—you are in effect looking over again what your price was. And the contract service officers seem to me to be the ones most knowledgeable in determining what the new price should be, what the incentive should be, as opposed to your original negotiators.

I can see why your original negotiators should be in it. But I would think it would almost be a team rather than a coordination—where

you have your man who did the servicing, or the team that did, and the original negotiators almost—I think they can use the audits—I do not think you need them actually aboard.

Would you comment on that.

TEAM APPROACH TO NEGOTIATION

Mr. MALLOY. Congressman, I agree completely with you—the larger procurements—we actually do have the field man, who is most knowledgeable of the details of a contractor's operation, participate in the negotiation with the men at the buying office. Quite often we do the same thing with the auditors. We bring the field auditor in and he joins the team. So this is a good system. It is one that we follow. It is one that has certain limitations, of course, in terms of the cost to bring the people back in, and the time it takes to do this. But on large procurements it is very sound.

Mr. CURTIS. Well, I think the system as we have outlined here is sound. Sure, I can see where costs could enter in. But, to maintain a system, even though on a specific contract, it might look like it is costly by maintaining the system—but, you gain the cost back many times over.

Mr. MALLOY. Yes. I might mention one other facet of this that you may be interested in.

There are many circumstances which might involve the pricing out of some spare parts under a contract, or the pricing out of a change order, particularly lower dollar value change orders under a contract, where the total responsibility for doing the pricing is delegated out to the field personnel, and they actually handle the transaction in the field—because in that area, they do have the competence you are suggesting. It is the most efficient way to do it.

Mr. CURTIS. I see my time is up.

To me, this is the essence of what is going to move us forward, in line with Mrs. Griffiths' comments. If the Government is going to do the job to represent the Government's interest vis-a-vis the private sector; I have a very high opinion, I might say, of our private sector.

Mr. MORRIS. So do we, sir.

NEED FOR COMPETENT EMPLOYEES

Mr. CURTIS. I think they are competitive. Sure, there needs to be a real competition to see to it that gouging does not develop. But it is true if we do not have people trained and competent to meet those competent people, it does not result in a good system. And this emphasis I do feel you are placing on this in upgrading the skills and the recognition that the people in these three areas deserve, if we are going to attract and hold in those services the kind of men and women that we do need, the kind of men and women like Mrs. Griffiths—she might not have been a Congresswoman if we had a good career for people like her there.

Chairman PROXMIRE. Much more valuable here, however valuable she would be as a procurement officer.

FOUR-DAY PROCUREMENT CONFERENCE

Mr. MORRIS. We had this 4-day conference of our 280 top procurement personnel just a month ago. After 4 days, I think, their prime conclusion was the human element is the most important ingredient to further progress in this field.

CONFLICT-OF-INTEREST LAWS

Chairman PROXMIRE. Of course, we have not mentioned at all the laws that prohibit procurement officials from becoming part of a firm which has supplied procurement to the Government.

Do you think that the laws are sufficiently restrictive in this regard? It concerns me very deeply, concerns all people that I have talked to about this. You have a man who—in some cases military, some cases civilian—he is a procurement official. He leaves the Defense Department—is it 1 year or 2 years?

Mr. MORRIS. One year I believe.

Mr. CURTIS. For 1 year he is not permitted to work for a firm which has sold to the Government. But, after a year he is free to do so. And, of course, the pay, the compensation can be enormous. And this can be something in the back of the mind of such procurement officers when they deal with these big firms. On the other hand, we do not like to interfere with the freedom of any American citizen.

Do you feel the laws are adequate in that regard?

Mr. MORRIS. Let me first correct myself. Mr. Malloy said it is 3 years.

Mr. MALLOY. I might say just to further clarify, that in the case of a military man, he is prohibited for all time from doing business with the service that he has served with. So he has that prohibition that lasts without limitation.

Chairman PROXMIRE. So if he is an Army man, he cannot do—

Mr. MALLOY. Cannot sell to the Army.

Chairman PROXMIRE. Cannot do business with the Army?

Mr. MALLOY. That is correct.

Mr. MORRIS. I do think, Mr. Chairman, our laws and our own administrative regulations, Executive orders and directives, are quite adequate and sufficiently restrictive to prevent abuses. (See "Standards of Conduct," Hearings, 1965, pp. 141-177.)

DEFENSE MOBILIZATION ORDER 8555.1

Chairman PROXMIRE. Is Mr. Sanderson here, of the Office of Emergency Planning?

Mr. SANDERSON. Yes, sir.

Chairman PROXMIRE. Mr. Sanderson, I understand that your office is reasonable for setting standards on the use of this equipment?

Mr. SANDERSON. That is right, sir.

Chairman PROXMIRE. Government-owned—and in the hands of the contractors. And Mr. Staats was anxious that you have a chance to be here. If you have any statement at all that you would like to make in connection with what has been said this morning, or what Mr. Staats has said before, we would welcome it.

Mr. SANDERSON. We have worked closely both with GAO and the Department of Defense on this report and are still working on it. I can submit for the record a copy of our policy that has existed for 10 years in this area.

Chairman PROXMIRE. Very good.

(The following was subsequently supplied as promised:)

[Reprinted from the Federal Register of Nov. 23, 1963 (28 F.R. 12581)]

DEFENSE MOBILIZATION ORDER 8555.1 (FORMERLY DMO VII-4, VII-1A AND VII-1B) NOVEMBER 13, 1963

EXECUTIVE OFFICE OF THE PRESIDENT,
OFFICE OF EMERGENCY PLANNING,
Washington, D.C.

DMO 8555.1—OEP POLICY GUIDANCE ON GOVERNMENT-OWNED PRODUCTION EQUIPMENT

1. *Purpose.* This Order consolidates and revises existing policies on Government-owned production equipment, including machine tools, which policies are necessary to maintain a highly effective and immediately available machine tool and equipment reserve for the emergency preparedness program of the U.S. Government.

2. *Cancellation.* This Order supersedes Defense Mobilization Order VII-4 (Revised) of March 10, 1958 (23 F.R. 1727); DMO VII-1A (DMO-18, Amdt. 1 (18 F.R. 4518), redesignated at 18 F.R. 4597 and 18 F.R. 6736); and DMO VII-1B (DMO-18, Amdt. 2 (18 F.R. 4518) redesignated at 18 F.R. 4597 and 18 F.R. 6736).

3. *Scope and applicability.* The policies and provisions of this Order apply to all Federal Departments and Agencies having production equipment emergency preparedness functions assigned by Executive Orders. They shall relate to the classes of Government-owned production equipment listed in Appendix A of this Order. This Order is not designed to affect any existing leases of Government-owned production equipment. Such exceptions as from time to time may be necessary to the policy outlined herein shall be made only with prior approval of the Office of Emergency Planning.

4. *Definitions.* a. "Production equipment," as used herein includes all items of equipment having an acquisition cost of \$500.00 or more that fall within the categories of machinery and equipment listed in Appendix A of this Order.

b. "Idle production equipment," as used herein means all items of production equipment for which no use is contemplated or planned within 90 days, except such equipment as is devoted exclusively to maintenance or is on shipboard or assigned to owning agencies' developmental activities. Idle equipment does not include production equipment in packaged form, in standby lines, or in active base packages, unless or until it has been withdrawn therefrom and has no contemplated use for a 90-day period.

c. "Packaged form," as used herein means Government-owned production equipment assigned to a specific program, contractor, and plant in either an in-use, idle, or partially idle status and which equipment as an entirety, or when combined with equipment owned by the contractor, is capable of producing at a specific level, a particular military or defense-supporting item or items at that plant, by that contractor, as defense requirements may necessitate.

d. "Standby line," as used herein means a complete set of installed Government-owned equipment, in an idle status, maintained intact in reserve condition and which, when activated, is capable of producing at a specific level of output.

e. "Active base package," as used herein means idle production equipment located in an active production facility when such equipment has been retained to provide production acceleration capability in the event of emergency, or to be used following a change-over to a new modified production item.

f. "Package," as used herein means those complements of production equipment held in packaged form, standby lines, and active base packages, as defined above.

5. *Disposition of production equipment—*a. *Policy—*(1) *Department of Defense.* Production equipment owned by the Department of Defense for which there exists a known or anticipated emergency preparedness need shall be held in efficient operating condition at or near the plants which will operate them in event of an emergency. In the event no such storage arrangement is possible, the equipment may be stored in central Government warehouses, but, in such cases, all efforts

should be exerted to maintain intact complete complements of production equipment. In those cases in which complements of equipment are not wholly Government-owned, every effort should be made to keep together as much as possible of the total equipment complement.

(2) *Other Government agencies.* Production equipment owned by government agencies other than the Department of Defense, shall be stored adjacent to manufacturing establishments only if there exists a known or anticipated defense mobilization need therefor at such location and if storage arrangements provide for the maintenance of the equipment in efficient operating condition. Where adjacent storage is not required to meet a known or anticipated defense mobilization need, the equipment should be placed in storage by the owning agencies under the most economical arrangements that are compatible with maintenance of the equipment in efficient operating condition.

b. *Provisions.* (1) All equipment in packages shall be reviewed periodically to insure their essentiality to mobilization requirements and to guard against obsolescence. Packages or parts of packages found to be obsolete or no longer essential to mobilization requirements shall be reported as idle equipment to be screened for redistribution or disposal.

(2) In any instance in which a department or agency cannot meet urgent production schedules, because equipment essential to this end is not immediately available within the department or agency or cannot be promptly obtained from other Federal agencies or from private industry, equipment in packages shall be made available on a loan or replacement basis for this purpose. Upon termination of a loan, the borrowed equipment, if required, will be returned to its package.

(3) Continued maintenance of a modern and efficient production equipment mobilization base and planning and programming toward that objective should be advanced by the inclusion and consideration, where feasible, of requests for the following purposes as a part of the regular, annual cycle:

(a) Procurement of equipment to meet current production schedules, including equipment necessary to permit return of items borrowed from packages.

(b) Replacement of obsolete items in packages by equipment currently regarded as efficient for this purpose.

(c) Provision for modernization and replacement of production equipment to keep pace with technological advances in both munitions design and in equipment essential to its efficient production.

(4) *Non-defense leasing.* No Government-owned production equipment shall be leased for non-defense production purposes except when plans for such leasing have been prepared by the owning agencies and approved by the Office of Emergency Planning.

(5) *Uniform rental rates.* All new agreements and agreement renewals entered into by any agency of the Federal Government, under which private business establishments are provided with Government-owned production equipment, shall be subject to the following schedule of rental rates (expressed as percentages of the installed acquisition cost of equipment):

	Monthly rental rates (percent)
Age of equipment:	
0 to 2 years-----	1 $\frac{3}{4}$
Over 2 to 6 years-----	1 $\frac{1}{2}$
Over 6 to 10 years-----	1
Over 10 years-----	$\frac{3}{4}$

These rental rates shall be uniformly charged by all Government agencies in leasing Government-owned equipment when the rental charge is to be a periodic cash payment or when it is to be utilized in computing a contract price reduction and shall be levied on an equipment availability basis without regard to the character or extent of its use under such agreements. No exception to the rates shall be made without prior Office of Emergency Planning approval.

(6) *Other leasing guidelines*—(a) *Contract provisions*—i. *Term.* Leasing agreements shall be drawn to cover the span of time needed to carry out their purpose, with latitude for adjustment to meet changed circumstances.

ii. *Purchase option.* A purchase option provision shall be included only in exceptional cases, or where prescribed by law.

iii. *Renewal option.* Provision for renewal shall be excluded from equipment leases.

iv. *Maintenance.* Agreements shall require that equipment be returned in the condition received, ordinary wear and tear excepted.

v. *Installation charges.* Agreements shall provide that the lessee bear installation charges in whatever manner is best suited to the particular circumstances.

vi. *Transportation in and out and removal costs.* Agreements shall provide that these costs be borne by the lessee in a manner best suited to the particular circumstances.

vii. *Equipment modernization costs.* Agreements shall provide that, when equipment is modernized by substantial rebuilding at Government expense, the acquisition cost of the equipment be adjusted upward to take account of the increased value that such rebuilding and modernization represents.

viii. *Statement of rental consideration.* For each contract, under which a private contractor is provided with Government-owned production equipment, a statement shall be included in the contract or the contract file, as appropriate, specifying the periodic dollar amount of rent to be paid, whether such payments are made in cash or are offset or credited against payments made to the contractor by the Government for end-products produced for Government account.

(b) *General considerations.* i. Government lessor agencies should not be regarded as being in the leasing business as an end in itself or in the same sense as private industrial establishments.

ii. Government-owned production equipment should not be leased to private industry until its unavailability from private sources has been established.

iii. The rental rates and leasing guidelines outlined herein have no application to wholly-owned Government facilities operated by private contractors on a cost-plus-fee basis.

iv. Government agencies providing Government-owned production equipment to private contracts shall insure that no contractors are afforded a favored competitive position thereby.

6. *Central inventory and effective utilization of idle Government-owned production equipment including machine tools.* The following agencies are in possession of such equipment and tools or have the right of repossession in the interest of national defense:

Department of Defense.

Department of the Army.

Department of the Navy.

Department of the Air Force.

General Services Administration.

Atomic Energy Commission.

Department of Commerce.

Department of Health, Education, and Welfare.

National Aeronautics and Space Administration.

a. *Policy.* To accomplish effective utilization of these tools and equipment two central inventory records of idle Government-owned production equipment and machine tools (for those classes listed in Appendix A, or as may from time to time be determined by the Office of Emergency Planning with the advice of directly affected agencies) will be established and maintained, one in the Department of Defense, the other in the Department of Commerce, Army, Navy, and Air Force idle equipment will be reported to the former and that of all other Federal agencies to the latter. Transfers between agencies listed above will be accomplished in accordance with the provisions of the Federal Property and Administrative Services Act of 1949, as amended, and GSA regulations.

b. *Provisions.* (1) Equipment and tools in these central inventories will be made available to the agencies listed above on the basis of essentiality and urgency of needs.

(2) The Department of Defense will exercise the functions of recording, directing on-site inspection, and directing the issuance of shipping orders when reassignment within the Department of Defense is involved.

(3) The above listed agencies will furnish the information necessary (see Appendix B for minimum descriptive requirements) to establish and currently maintain such central inventories; provide for the expeditious shipment of such equipment and tools in accordance with Department of Defense or Department of Commerce instructions; and arrange for such transfer, lease, sale, or other disposition as may be necessary in the best interests of the Government and in conformity with property accountability requirements.

(4) Procedures implementing this directive will be established by the agencies concerned in consultation with each other and conform as nearly as is practical with existing procedures governing the present idle equipment inventories.

(5) The agencies listed above will submit to the Office of Emergency Planning all listings of production equipment which are excess to their needs prior to being reported to GSA for utilization and donation screening in accordance with the Federal Property and Administrative Services Act of 1949, as amended, and

GSA regulations. Upon expiration of 30 days after submission of each listing, the agency concerned may proceed with reporting the equipment to GSA unless the Office of Emergency Planning directs otherwise.

7. *Use of idle Government-owned production equipment for disaster relief.* a. *Policy.* Idle Government-owned production equipment in the central inventories maintained by the Department of Defense and the Department of Commerce will be made available as needed to producing establishments crippled by major disasters.

b. *Provisions*—(1) *Determination of disaster.* Determinations that particular events constitute major disasters will be made in accordance with Public Law 875, 81st Congress. Authority to arrange for the immediate leasing of such equipment to damaged facilities within major disaster areas, when necessary to the resumption of normal operations, is hereby granted to the Department of Defense and the Department of Commerce with respect to items in idle inventories. The procedure established in this section shall remain in effect only for such period of time as the areas in question are classified as disaster areas under authority of Public Law 875, 81st Congress, or until the Director of the Office of Emergency Planning shall find that the application of the procedure to those areas would no longer serve to meet the objectives of this section.

(2) *Leases and rentals.* Leases authorized for disaster relief shall be only for such period of time as is necessary for lessees to obtain delivery on equipment to replace that which has been damaged or destroyed. In no case shall a lease be entered into for more than a one-year term. If at the close of a one-year term replacements are still not available, an existing lease may be extended for an additional period until deliveries can be effected or one year, whichever is the shorter. Equipment leased for disaster relief shall be subject to the uniform leasing practices set forth in subsections 5b(5) and 5b(6) of this Order, except that the monthly rental charges shall begin 90 days after the arrival of the equipment at the lessee's plant.

(3) *Issuance of authorizations.* Authorizations to lease and ship will be issued by the Department of Defense or Commerce within 24 hours of receipt of request, when duly constituted Department of Defense or Commerce officials find that such leasing is necessary to restore normal production. Details of the formal lease will be worked out as quickly as possible thereafter between the lessee and either the owning agency, or the General Services Administration acting for the owning agency.

8. *Reports.* Such reports of operations under this policy as may be required by the Office of Emergency Planning shall be submitted to the Director of the Office of Emergency Planning and made public at his discretion.

9. *Effective date.* This order is effective the date of issuance.

Dated: November 13, 1963.

JUSTICE M. CHAMBERS,
Acting Director,
Office of Emergency Planning.

APPENDIX A

CLASSES OF EQUIPMENT INCLUDED UNDER THE PROVISIONS OF THIS ORDER¹

Class number	1956 Department of Defense production equipment code	Description
1.....	3411-11 through 3411-99.....	Boring machines.
2.....	3412-11 through 3412-99.....	Broaching machines.
3.....	3413-11 through 3413-99.....	Drilling machines.
4.....	3414-11 through 3414-99.....	Gear cutting and finishing machines.
5.....	3415-11 through 3415-99.....	Grinding machines.
6.....	3416-11 through 3416-99.....	Lathes.
7.....	3417-11 through 3417-99.....	Milling machines.
8.....	3418-11 through 3418-99.....	Planers.
9.....	3419-11 through 3419-99.....	Miscellaneous machine tools.
10.....	3441-11 through 3441-99.....	Bending and forming machines.
11.....	3442-11 through 3442-99.....	Hydraulic and pneumatic presses.
12.....	3443-11 through 3443-99.....	Presses, mechanical power.
13.....	3444-11 through 3444-99.....	Manual presses.
14.....	3445-11 through 3445-99.....	Punching and shearing machines.
15.....	3446-11 through 3446-99.....	Forging machinery and hammers.
16.....	3447-11 through 3447-99.....	Wire and metal ribbon forming machines.
17.....	3448-11 through 3448-99.....	Riveting machines and/or dimpling machines.
18.....	3449-11 through 3449-99.....	Miscellaneous bending and forming machines.

¹ Note: Classes of equipment will from time to time be added to or deleted from this listing through issuance of amendments to this appendix.

APPENDIX B

MINIMUM INFORMATION TO BE FURNISHED IN REPORTING IDLE GOVERNMENT-OWNED PRODUCTION EQUIPMENT AND MACHINE TOOLS

- (a) Standard commercial description.
- (b) Standard commodity classification code.
- (c) Government tag number.
- (d) Location.
- (e) Condition.
- (f) Owning government agency.
- (g) Manufacturer's name.
- (h) Serial number.
- (i) Opinion as to whether special, single purpose, or general purpose.

[F.R. Doc. 63-12241 ; Filed, Nov. 22, 1963 ; 8:46 a.m.]

[Reprinted from the Federal Register of Sept. 5, 1964 (29 F.R. 12646)]

(Defense Mobilization Order 8555.1 ; Amdt. 1)

DMO 8555.1—OEP POLICY GUIDANCE ON GOVERNMENT-OWNED PRODUCTION EQUIPMENT

DELETION OF CERTAIN PROVISIONS

1. Defense Mobilization Order 8555.1 dated November 13, 1963 (28 F.R. 12581) is hereby amended by deleting paragraph 6b(5).
 2. This amendment is effective the date of issuance.
- Dated : August 31, 1964.

FRANKLIN B. DRYDEN,
Acting Director,
Office of Emergency Planning.

[F.R. Doc. 64-9047 ; Filed, Sept. 4, 1964 ; 8:47 a.m.]

Chairman PROXMIRE. We will be in touch with you later about the possibility of legislation in this area.

Thank you very much.

Now, I would like to point out—a reporter sent up to me a little note—that November 30 is the fifth anniversary of the Truth in Negotiations Act. So it just has taken apparently 5 years to make it effective. And it is good at long last that we seem to be accomplishing this.

PROGRESS STATEMENTS REQUESTED OF DOD

These things do take a long time. But I think this committee has been useful in this regard, and certainly the Comptroller General has been enormously useful, and you have been cooperative.

Now, having said that, let me disagree a little bit with my good friend Tom Curtis in his assessment of your report as a progress report. It purports to be. But I am inclined to feel it is too much of a prospective kind of report. I think it would be very helpful for us if you could report to us, say at the 6-month intervals, on the actual progress that has been made with respect to the following:

No. 1, progress in implementing the Truth in Negotiations Act—training and so forth.

No. 2, the increase in advertised bidding, or the decrease—what has happened in advertised competitive bidding. I understand it has decreased in the last year, although you point out that it increased since 1961.

Mr. MORRIS. Right, sir.

Chairman PROXMIRE. No. 3, the increase or decrease in the breakout program.

No. 4, inventory management.

No. 5, integrated management of items.

No. 6, progress with GSA, the General Services Administration, on the National Supply System.

No. 7, progress in inventorying of IPE—that is the inventory of Government-owned property in the hands of private contractors.

No. 8, purging inventory lists.

And finally, No. 9, test of effectiveness of short-shelf programs.

Mr. MORRIS. We would be pleased to do this, Mr. Chairman. We get monthly reports on most of these items, and can easily give you 6-month reports.

ADEQUACY OF MANAGEMENT IMPROVEMENT PROGRAMS IN DOD

Chairman PROXMIRE. You see, what concerns me a great deal—we know that Secretary McNamara has been a tremendously able man, and you have done a fine job in this enormous procurement job you have. And yet there does not seem to have been in our view a sufficient internal concern with making these efficiency reforms. The GAO has done a good job. It seems to me so much of the initiative has come from the GAO or from Congress, in pushing competitive bidding, short-shelf life, truth in negotiations, inventory control, the National Supply System—all these things seem to have originated with the GAO instigations. And it concerns me that this very big department that you have, very heavily staffed, with competent people, has had to wait for Congress to push you in these directions rather than taking the initiative yourself.

Mr. MORRIS. Sir, we do not like to be self-serving. But I have been in and out of Government now for 30 years. I have never seen a more able, devoted, hard-working group of managers than exists in the Department of Defense today, both in uniform and in civilian clothes.

Chairman PROXMIRE. I would not question that at all. Of course, the circumstances with the Vietnam war, and so forth, are very difficult. But the fact is, we have had to come with this again and again. And often we have to come back and keep repeating and hammering away before we make progress on some of these things.

Mr. MORRIS. Yet we do a disservice to the many people in this program if we did not give them much credit for what has happened in the past decade. These improvements have to be done by people. They have to be motivated—not just directed, but motivated. That is our job. Congress motivates us. We have to motivate our people. I think we have done a good job.

Chairman PROXMIRE. Let me give you an example. We had the testimony yesterday from the Comptroller General in which he said about Vietnam:

The army is not yet in a position to know with a reasonable degree of confidence what stocks are on hand and what stocks are actually excess to their need.

Then in questioning we pointed out the dimensions of this. I asked Mr. Fasick to give us the estimate of what this means in terms of dollars and he said this:

We did at one time during my visit, and these figures have since been adjusted, but they cited figures out of a hundred and twenty thousand items over there, they had about 45,000 items that were in excess of three times the requisitioning objective.

I said, "Is it fair to say this means they have three times as much as they need with respect to these particular items?"

And he said, "For these items."

Now, of course, there is a war going on. But it is a war that has been pretty much the same level over the last year and a half or so.

As you say, you have had literally hundreds of officials going over to try and remedy the situation and improve it. And this seems to be—represent quite a shocking waste—to think that in a very large proportion of all these items, they have three times as much as they need.

Mr. MORRIS. Sir, to us this really suggests the opposite. Our troops have not once "been restricted in their operations against the enemy for want of essential supplies," to quote General Westmoreland.

Chairman PROXMIRE. That is the most important. I would agree. But, nevertheless, there is a terrific area of excess.

Mr. MORRIS. In hindsight, we know how this happened. We knowingly let it happen because we wanted them to be fully supplied. I think the important thing is that the data were given Mr. Fasick by people on the ground. They had found this out. They were correcting these problems. They were not waiting for GAO to find them. We are greatly encouraged—Mr. Brooks and I—by the vigor and intelligence with which General Westmoreland, General Abrams, General Palmer, General Scott, and the top logistics people, are approaching these problems in the midst of a war. They don't have to be told to do it. They are doing it because they want to prudently manage the effort over there.

PHYSICAL INVENTORIES AT ARMY DEPOTS

Chairman PROXMIRE. Well, I am still left with the feeling that we are wasting an enormous amount of money in this area. And especially when we have reports such as the report we have from the Comptroller General that 55 percent of the Army depots had had no physical inventory, and 45 percent had not even had a simple inventory over a recent 18-month period.

Mr. MORRIS. I have checked into this, sir. It is true that—

Chairman PROXMIRE. And that is in this country.

Mr. MORRIS. The Army Materiel Command did suspend its regular inventory program during the buildup. They have reinstituted the program, including the sample inventory techniques.

Chairman PROXMIRE. I make this point—not only from the fact that you cannot manage an inventory, you are bound to have excess, waste, shortages, if you don't know what you have. But also from the standpoint of recognizing if we are going to provide the most prompt and efficient kind of service to Vietnam, you have to have an inventory where you know where things are.

DISCREPANCIES IN INVENTORIES

Mr. MORRIS. And we do, really.

The report of the GAO deals with the little discrepancies that show up in a 4-million-item inventory. Their report shows that the net

difference between gains and losses in dollars was only 1 percent in 1965 and 1.4 percent in 1966.

Chairman PROXMIRE. Another point shows about a 25-percent discrepancy, as I recall.

Mr. MORRIS. That was the gross value—

Chairman PROXMIRE. From \$10.4 billion to—

Mr. MORRIS. These were the gross adjustments up and down. The net trade-off between the two was only a 1-percent difference in one year and 1.4 in another. I am told our largest merchandising houses consider 2 percent net adjustment to be quite satisfactory.

Chairman PROXMIRE. How do we know, though, if we have not taken these inventories comprehensively? How do we know how far off we are?

Mr. MORRIS. These are the adjustments which were reported in 2 prior years. The Army did suspend its regular physical inventory for a period of 2 years and has now reinstituted it.

Chairman PROXMIRE. Can you give me what proportion of the depots have taken complete physical inventories in the last year—all of them? Army depots.

Mr. BROOKS. Not this last year, sir. The program is just getting going again.

Chairman PROXMIRE. Now they are getting going. When did that start?

Mr. BROOKS. It started with a location survey in, I believe, November of this year—this month—they are starting the complete round of physical inventories in January.

Chairman PROXMIRE. So that in calendar 1968, you expect that you will have a hundred percent?

Mr. BROOKS. It is intended to be completed by January 1, 1969.

Chairman PROXMIRE. Does this apply to the Navy, too?

Mr. MORRIS. Navy and Air Force did not stop their normal inventory procedures.

Chairman PROXMIRE. Yet the Comptroller General pointed out some very serious discrepancies and weaknesses as far as the Navy and Air Force inventory managements are concerned, too.

Mr. MORRIS. They all have had a very similar experience in terms of net adjustments. I checked into the Comptroller General's report. The net adjustments averaged 1 to 1½ percent. I think this is always going to be the case, with 4 million items in inventory. (See pp. 362, et seq., for further discussion on inventory controls.)

NEED FOR NAVY DAIRY

Chairman PROXMIRE. We have had some amusement and, of course, some real concern, about the waste of money—or what some of us feel is the waste of money—with regard to the Naval Academy in Annapolis maintaining a dairy in competition with dairy farmers. The President criticized this in his message when he signed the defense construction authorization act.

Is there any economic reason for continuing the Navy dairy?

Mr. MORRIS. Sir, this case apparently is somewhat unique in that you can build a case on either side of this from an economic point of view.

The studies of which I have been informed on show that our costs in-house are lower if we examine out-of-pocket expenses only, but that commercial costs are lower if we take into account all the indirect costs such as interest and depreciation. It was a sort of borderline case.

Chairman PROXMIRE. It doesn't sound borderline to me. Why not take into account all costs? After all, you have all costs.

Representative CURTIS. A-76 says you are supposed to.

Mr. MORRIS. The real issue here is from a policy point of view whether the Navy should be in the dairy business.

Chairman PROXMIRE. It looks like a pretty easy one to answer.

Mr. MORRIS. Congress—

Chairman PROXMIRE. It milks the taxpayer plenty.

Mr. MORRIS. Congress answered by prohibiting us from going out of the business in the military construction authorization bill this year. The President's message spoke eloquently to that action.

Chairman PROXMIRE. There is no health reason.

Mr. MORRIS. No, sir; none that I know of.

Chairman PROXMIRE. Since the President challenged the action of the Congress on this issue, is the executive branch going to refer the matter to the Attorney General for an opinion as to whether the separation of powers has been violated?

Mr. MORRIS. There are no plans to do this, sir.

DOD PROGRAM OF EXCHANGE-SALE IMPACT ON UTILIZATION AND DONATION PROGRAMS

Chairman PROXMIRE. I would like to ask a question on behalf of Mrs. Griffiths. She certainly has done a splendid job this morning, but she had to leave. She says, "The schools in my State have need for typewriters, other office machines, trucks, cars, machines of many kinds. Getting these as surplus helps the budget of State and local governments, which lose so much tax base to the Federal Government, and especially the DOD. I understand that the DOD has or is about to embark on a large-scale exchange-sale program which will virtually dry up the donable program. The other Federal agencies will lose also, since this property never becomes excess in the technical sense. What is the status of your program and what is the rationale?"

Mr. MORRIS. Sir, the regulations of the executive branch provide that where a new typewriter or other piece of equipment is needed and a used one is in the possession of the buying agency and has a value from a trade-in point of view, that that trade-in shall be made.

EXPECT SAVINGS OF \$10-\$20 MILLION A YEAR

We did suspend several years ago the full operation of this exchange sale procedure. We have recently determined that it is prudent to institute that procedure, just as GSA has been practicing it for some years for budgetary reasons. This will save us, as I recall, from \$10 to \$20 million a year, and we think that that is an important increment of savings at this time.

EFFECT OF CONTRACTOR-HELD EQUIPMENT ON TAX BASE

Chairman PROXMIRE. Congressman Curtis raised this point I thought very well the other day, expressing his concern on the effect

of Government-owned equipment in the hands of contractors on the tax base of localities and States and of course many of them have real property taxes and this takes it off the roll.

But I will yield to Congressman Curtis. My time is up.

Representative CURTIS. Thank you, Mr. Chairman.

Let me say that I thought your criticism of my comments on the progress report is well taken and I join you. There was a great deal of future planning which of course we do want.

IMPLEMENTING CIRCULAR A-76

I had this on my list of interrogation on the implementation of circular A-76. I am very disturbed, you see—when you make statements like this—and maybe you have to—in regard to this Navy dairy.

Now, there is another problem involved here—and believe me I am about ready to do all I can to get the muzzle on it.

There is this business of executive department people lobbying Congress on their time and with their money.

The Executive has some control over them, I hope, to stop this kind of business.

COST OF U.S. PUBLICITY

I have a news item here—\$425 million goes for U.S. publicity—tax money used for a wide campaign of information.

Much of this is the Executive lobbying the Congress with taxpayers' money, using their time, and then when they are successful in their lobbying, then Congress—and rightly so—Congress should be criticized. But it makes the Executive speak with two voices. And there has been just too much of this going on.

COMMISSARIES

But I might say until there is courage exhibited in the Defense Department on the subject of commissaries, which is in violation of the law right now—it is in further violation of the spirit of A-76—and I sympathize with high-ranking generals and admirals who benefit from commissary privileges here in Washington—and I certainly have made it clear I am not trying to take it out of the hides of the enlisted men—I want to raise their compensation in lieu of these benefits. But let's do it by law, and let's don't do it by violation of law.

They are not going to get A-76 implemented until these examples are eliminated.

Now, I appreciated your attachment E which shows the cases that you have shut down and applaud it, because there we can see that something is going on.

I would also like, though, if you would supply a list of examples where you made the decision the other way and permitted in-house operation to exist instead of letting it go. That would give our committee a little better insight into how you are applying A-76.

Mr. MORRIS. There is some mention in the examples, sir.

Representative CURTIS. Are there?

Mr. MORRIS. Yes.

Representative CURTIS. I assume these were where you had them out-house—I mean not in-house—I don't mean out-house.

Mr. MORRIS. Items 7 and 10 are illustrations, sir, of approvals, and we in our text did cite the case of the 10,000 contract technicians formerly procured under contract, who will now be converted to civil service.

TAXES AS AN ELEMENT OF COST

Representative CURTIS. Yes.

Well, those are good.

Now, if I may, for the record, quarrel a bit with the failure of A-76 to include local taxes as one of the cost items. The private sector bears these.

But I want to relate local taxes to what services they procure—sewage, water, police protection, fire protection, traffic, schools, parks, recreation. All of these are—whether you are doing it through the private sector or whether it is the Government doing it itself—these are services that are part of the cost of operation.

Furthermore, the burden it places on local communities when you put Government installations in an area and withdraw them from the tax base—they don't bear their fair share of the cost of sewers—and if it is public water—certainly police protection and fire protection, and these costs are real costs.

To not have this as one of the factors in the cost accounting that lies at the base of determining whether Government shall do it in-house or whether it shall be contracted out to the private sector is quite vital.

So this is simply for the record, but also to pass on to the Defense Department, who, if they will examine it from their angle, I think might agree.

The whole theory of the impacted school area bill was on the assumption that if the Federal Government moved into a community, and withdrew from the tax base certain property, that would be from school revenues, and yet the personnel gains the benefit from having a good school system—therefore pay in lieu of taxes. I think that illustrates the logic and the great importance of this factor.

RELATION OF \$15 BILLION CONTRACTOR-HELD INVENTORY ON TAX BASE

This moves me now to this other area of \$15 billion of Government property that is used—industrial plant, materiel, special tooling, and so forth—which I think—and this I don't know, and have asked the GAO to get me information, and anyone who can give it to me—I think is largely withdrawn from the property tax base as well as the merchant and manufacturers tax—I am referring now to inventory of material—which your private sector pays the local taxes on.

Now, there may be some communities, through their laws, that have been able to get at it through the rental provisions.

Have you a comment on that?

STATES MAY TAX USE OR POSSESSION OF GOVERNMENT PROPERTY BY CONTRACTORS

Mr. MORRIS. Sir, we did attempt to check into this briefly. It is our understanding that a State may tax a contractor's use or possession of Government-owned property if it enacts legislation authorizing such

taxation and the tax is not discriminatory. This principle was established in three Michigan tax cases decided by the Supreme Court in 1958.

Representative CURTIS. That is very helpful. And it would be helpful to know how many implemented—maybe this needs a lot of publicity so that the local communities will realize that here is a source of taxes that will make government costs go up, but this is still a good cost accounting provision. (See p. 65.)

Now, let me get into an area where I think I am quite critical—the inventory control of this Government equipment.

I asked the GAO whether this figure that they gave us of \$11 billion and \$4 billion, which is approximately your figure of \$15 billion—whether this was acquisition cost or cost that had been depreciated. And they said acquisition cost.

Is this true?

Mr. MORRIS. That is correct, sir.

RENTAL RATES FOR EQUIPMENT

Representative CURTIS. Well, that surely is not very good inventory control as far as using this for the purposes which you described in here of how much you are going to set your rental—a piece of equipment that is depreciated by 50 percent certainly should not have the same rental that a brandnew piece has nor—I am talking about your initial contract—if it is a continued contract, you take that into account. But how can you utilize your inventory control if you don't have your depreciated values instead of your acquisition costs?

Mr. MORRIS. I would say, sir, that this question is particularly pertinent to the rental costs assessed against the contractor for the use of the equipment. The present formula was developed in years past by OEP and ourselves, and does provide a sliding scale of rental charges based on age of equipment.

INVENTORY AS A CONTROL

Representative CURTIS. We are talking about an inventory control. We are not talking about that. We are talking about—it can be passed over to you—here is the way I have described it—maybe monthly, just your list and the number of people who actually made their monthly reports on the equipment. This means, I would think, that you would have every item on your computer read, even hundred dollar items, because you are talking about things that phase in and phase out. And if the report is not—if there has been a dereliction of reporting, you know which items you don't have the report on, and then probably you have a breakdown in the report on key things that you need to know. This is what I mean by using your inventory as a control.

Mr. MORRIS. I see.

Representative CURTIS. And I don't think you have that, do you?

DOD DEDICATED TO ITEM CONTROL OF EXPENSIVE EQUIPMENT

Mr. MORRIS. We did comment, sir, we are dedicated to getting a better item-by-item utilization control and reporting over at least the expensive items of equipment.

Representative CURTIS. Yes. But I am talking about, again—I am repeating myself—the central control, which means having the full inventory—that is the central. And that has to have accurate and complete figures on acquisition costs probably in the beginning, which through your computation, through the monthly reporting, is adjusted downward, so you know what your depreciated costs are, and also when some of this is generated as obsolete equipment it then becomes surplus. But you have got to have the inventory in the beginning. I don't think you have such an inventory.

DSA TO MAINTAIN INVENTORY CONTROL OF EQUIPMENT

Mr. MORRIS. It is the function of our DSA special agency to maintain central inventory, and this we are enhancing.

Representative CURTIS. Apparently it is not even set up. I cannot get a straightforward answer to that, as to whether you really have it. I don't think you have it. And this is a lot of your trouble. If you haven't got it, just say so. I hope I am not hypercritical.

Mr. MORRIS. We want you to have the facts, sir. I would like General Hedlund to comment on this.

General HEDLUND. Yes, sir. We have an inventory of items of industrial plant equipment valued over \$1,000 original cost reported to us by the military services and in DSA, and we are working toward its completion. At present this runs about \$4.3 billion.

Representative CURTIS. That is one of the things I asked yesterday of GAO—maybe I said you have got some inventory like I am talking about some of the components of the \$15 billion. And that is what it comes down to. What you are saying is one of these components you have.

DSA CENTRALLY MANAGES HIGH-VALUE ITEMS

General HEDLUND. Industrial plant equipment.

Representative CURTIS. Yes. But, I am talking about the whole ball of wax, the \$15 billion. And, also, even on yours—I don't know why you would—now that we have data processing—why you stay below a thousand dollars, unless you are saying that anything below a thousand dollars is not capital equipment. We are only talking about capital equipment.

General HEDLUND. I would like to say we manage, centrally, those items of industrial plant equipment over \$1,000 by design. These are the high-value items. We have those in our inventory records. But, this does not mean that we pay no attention to those under a thousand dollars, because in our contract administration program, we have a process by which contractors must have a property accountability system which we approve.

REVIEW ALL CONTRACTOR-HELD PROPERTY ONCE A YEAR

We go in, once a year, in all the contractor facilities which we administer, and review the extent to which they are complying with approved property accountability, for all items, of all value. This review is made by our Contract Administration Services property administrators. So, we do have a control on contractor's plant equipment or plant equipment in contractor facilities up and down the line.

Representative CURTIS. Well, maybe we are getting into semantics. You use the word "management," and I am talking about "control," which is really sort of oversight over management. I don't expect this inventory I am talking about to be used for management. I would expect your management would go on. But I am talking of something that is a control item to see what management is doing, whether they are complying—and also that you have your basic data.

GAO REPORT SEEMS TO DIFFER FROM TESTIMONY

The reason I suspect this does not exist—it may exist from what you are saying—but I suspect it does not—I am talking about the control aspect, not management—lies in the fact of the GAO report which shows such a—really a lack of control over and lack of knowledge over this tremendous amount of equipment that is in the hands of private contractors. It could not exist, in my judgment, if you had the kind of control I am speaking about.

GAO ADDRESSED ITSELF TO 400,000 TOOLS VALUED AT \$4.3 BILLION

Mr. MORRIS. I believe it might be helpful to comment this way.

I think GAO has addressed this \$4.3 billion segment that consists of some 400,000 tools. This is what the DSA has full central knowledge of. I believe GAO is commenting on our lack of proper supervision and surveillance of the utilization of that equipment.

Representative CURTIS. Oh, sure. But part of the reason—and I am just guessing—it would have been so clear to any management that you had to have utilization with accuracy, or you would not be doing the job. And, I think that this was not called to top management's attention because you really did not have this kind of a control setup. Otherwise it would not have taken GAO so long to dig in and come up with such a kind of record. The management would automatically say "Good night, what about these figures of how these private contractors are using our equipment or not using it."

SECRETARY MORRIS CONSIDERS GAP TO BE IN KNOWLEDGE OF USE AND NOT OF THE EQUIPMENT

Mr. MORRIS. So the gap has been central knowledge of utilization, not central knowledge of the equipment and where it is located.

INVENTORY CONTROL SEEMS LACKING

Representative CURTIS. A gap of utilization suggests that you did not have the other. I am saying it just suggests it. And the more I try to interrogate to find out what you have got there in the way of inventory in the sense of control, I think I am probably hitting paydirt—I don't know.

Mr. MORRIS. Let me summarize, sir. DSA does have an actual physical record of each equipment and its location in this 400,000 IPE area. In respect to real property, we likewise have a full inventory. DSA does not keep it; however, we must make annual reports to Congress on this.

In connection with the material item we referred to, each military department, in its appropriate bureau or command keeps inventory control over the materials in the hands of its contractors.

Representative CURTIS. Maybe—I will try again. Maybe what I am getting at is the difference, as I see it, between a library and an archive. An archive is where you have the thing but it is not in a form where it can be utilized. You may have such lists, but they are not up to date and so on, so that they can be utilized. A library has the books so that you can utilize them.

This is what I am—I dare say you have got a list. But is it up to date? That is why I used depreciation costs, the value after depreciation, as opposed to acquisition costs.

Now, it would be an archive item if all you had was the acquisition cost. And the testimony yesterday indicated that is what you did have—acquisition cost—that the \$15 billion is that rather than depreciated cost. This was only a checkpoint to me, to see whether this was in a form where you used it, or was just something that was in the archives, as it were.

DOD PLUGGING UTILIZATION GAP

Mr. MORRIS. The important point to us is we must know, not only know what we have and where it is, but that we do know where it is being used, how fully it is being used, when it is not being used on our work.

Representative CURTIS. But the record shows you did not know that. You said yourself there was a gap in your knowledge of utilization.

Mr. MORRIS. Correct, sir. That is the gap we are plugging.

Representative CURTIS. All right. But I hope you will take a look to see whether the comments I am making indicate that there are not some other gaps or maybe we have a canyon here.

Mr. Chairman, I have one other question.

BUY AMERICAN ACT POLICY

There is another report here on this problem of "Buy American" differential. This is really a question more to the Bureau of the Budget, because they are supposed to be— (See pp. 312, 550.)

Chairman PROXMIRE. They will be here Thursday.

Representative CURTIS (continuing). They are supposed to be reconciling the differences that exist in GSA, which has a 6 or 12 percent "Buy American"; Defense has a 50 percent, as I understand it. But at least on this—how much has—has Defense done anything on issuing any general policy on "Buy American" differential, or is it right across the board 50 percent?

DOD USES A 50-PERCENT DIFFERENTIAL

Mr. MORRIS. We installed, sir, in 1962, a 50-percent differential to be applied to the bids of firms offering a foreign product, meaning one that has 50 percent or more foreign content.

Representative CURTIS. That is across the board?

Mr. MORRIS. Right, sir.

Representative CURTIS. Except for those items that Congress put in under this kind of lobbying techniques I have described—not necessarily government in this instance—a complete embargoing area of textile products, and a long list.

Has the Defense Department ever taken a policy position on the complete embargo that exists in regard to purchasing materials at the most efficient and least cost?

DOD ENDEAVORING TO HELP BALANCE-OF-PAYMENTS PROBLEM

Mr. MORRIS. No, sir. We are simply trying to minimize our procurements of foreign materials chiefly by our installations located overseas in the interest of the balance-of-payments problem.

Representative CURTIS. We are talking about procurement domestically, too. People import into this country. And I would hope that the military is in the business of trying to get products at their cheapest cost, under policies that may be set elsewhere in the Government for entirely different reasons. As far as the military is concerned, I would think you would be trying to get materials and services at the lowest possible cost.

Mr. MORRIS. This is our firm policy, with the single exception of this "Buy American" problem.

Representative CURTIS. And the double exception of the complete embargo on a wide range of products. I mentioned textiles as one.

Now I am asking what—if there is a policy on this?

BERRY AMENDMENT

Mr. MALLOY. If I might respond, Congressman Curtis, I think the items that you are referring to are contained in the so-called Berry amendment, which is an annual provision of the Department of Defense Appropriation Act.

Representative CURTIS. I found out about it just a couple of years ago.

Mr. MALLOY. These provisions have been there for a number of years. I don't know of my own knowledge what position the Department took back at that time.

Representative CURTIS. How about now?

Mr. MALLOY. I do know of an instance this year in which the Congress added a new item to that list. I believe it was called synthetic coated fibers. In that instance we were asked for our views as to whether that should be added and we advised the Congress that we were opposed to the addition of that item until further study could be made. The Congress, however, did add it to the appropriation listing.

Representative CURTIS. Let me hope the policy of the Defense Department is not just to go along with what exists. This should be under review.

COST OF DOD POLICY

How much do you suppose it costs Defense to—the application of this "Buy American" differential and complete embargo? I have seen various estimates, and it is in the hundreds of millions of dollars.

Mr. MORRIS. We have no data, sir, that we can offer on this.

Representative CURTIS. Well, isn't this important—to be able to make policy. Let me take the other side of the coin, because I am concerned about our domestic producers, and I want to be sure that they have a fair shake on this thing. In order to make a policy decision of what they need—do they need 50 percent? Because certainly the Defense Department ought to have the data available to those of us who have to make policy in this other area of what it is costing.

If you are cost conscious you ought to be able to say—"Look, but for these things, and but for the small business set-aside we would—if these were not there we would be spending x hundreds of millions of dollars less." Then we are in the position of weighing the two.

Mr. MORRIS. The judgment was made that this was a desirable policy to apply in the interest of the adverse balance of payments. We know as a result many foreign bidders have ceased bidding. We thus have no way of knowing what the bids would be in many cases today and thus cannot develop precise figures.

Chairman PROXMIRE. It seems to me that Secretary McNamara, told us a couple of years ago at that time he estimated the cost of the "Buy American" policy by the Defense Department, the 50 percent, was something like \$67 million a year. It may have been Secretary Ignatius.

Mr. MORRIS. I have inquired, sir, and we have no figures I can offer you at this time. (See p. 86, "Hearings, 1966?")

Representative CURTIS. This I think is unfortunate.

Let me get this in context for the record.

This is not to criticize the U.S. Government vis-a-vis other governments—as frequently as reported to the American people—because the "Buy France," the "Buy Britain," the "Buy German" imposed by these societies is considerably more restrictive than "Buy American," I would observe.

But I am concerned in trying to get to the bottom of what it is costing us, the Government, to get the weapons and the services to provide our defense. And even though a policy decision may have been made, I think it is important for the Defense Department to have the figures in this area so that this policy can be reviewed.

Now, I ask that it be done. The Bureau of the Budget—I asked them several years ago. The Bureau of the Budget has not even reconciled the various "Buy American" applications of the various departments of the Federal Government. The Defense is 50 percent, GSA is 6 percent. There is no rationality on the thing at all. And this embargo that the Defense Department has on a wide range of goods has not been rationalized.

Well, I will leave the subject there for further development.

STATUS OF IPE INVENTORY

Chairman PROXMIRE. I just have a couple of very brief items.

Last May, when General Hedlund's predecessor, Admiral Lyle, appeared, he indicated that we were only a small part of the way along on getting inventory information on this Government-owned contractor-held and used equipment. He said the following, and I quote:

We are also conducting a one-time equipment inventory reconciliation program. The program will provide adequate and compatible central inventory records of

the industrial plant equipment located at contractor facilities under Defense contract administration and services cognizance. This two-year program envisions a reconciliation of approximately 83,000 industrial plant equipment items in the hands of 1,081 contractors. At the conclusion of the first three months of 1967, 18,000—

That is 18,000 out of the 83,000—

industrial plant equipment items reported to be or found to be in the possession of 248 contractors have been reconciled and records corrected.

This suggests that as of last April 1 there was still a long way to go. We had only recognized approximately—less than 25 percent of the items that were owned by the Government in the hands of contractors.

Is that correct, General Hedlund?

General HEDLUND. I will have to speak to that in these terms.

We are trying through this overall reconciliation to purify our records. Obviously you can find errors in those records—some equipments go in and others come out. Within the Defense Supply Agency at contractors plants we administer, we have completed about 70 percent of our reconciliation at this time.

Chairman PROXMIRE. So that as of March it was about 23 or 24 percent and as of now it is about 70 percent.

DSA RECONCILIATION TO BE COMPLETED DECEMBER 1968

General HEDLUND. That is within the Defense Supply Agency.

Chairman PROXMIRE. It sounds like you are way ahead of schedule. He said it was a 2-year program.

General HEDLUND. If I may complete my statement—we will finish the DSA administered portion in December of 1968. So we have about a year to go there. The military services, as you know, also manage various contractors' facilities, basically those concerned with weapon systems and major end items.

SERVICES TO COMPLETE RECONCILIATION IN 1969

And they all have reconciliation programs which they will complete in 1969. So, again I want to leave the point that while we do have an inventory, we are trying to purify it. We will be picking up some additional items of equipment as the reconciliation program progresses, but I would hope by the end of 1969 we will have an accurate and complete inventory.

DOD'S POSITION ON 14 RECOMMENDATIONS IN GAO REPORT

Chairman PROXMIRE. Fine. I would like to ask you, for the record, Secretary Morris, if you would reconcile each of the 14 recommendations in the final GAO report, specifically, point for point with your position on them, because there do seem to be perhaps some areas of disagreement with GAO that have not been brought out. You have indicated, in general, you approve. But we are left a little fuzzy on where you are on each specific recommendation. (See app. 4(a), p. 455.)

Mr. MORRIS. We will do so.

DEPARTMENT OF DEFENSE COMMENTS ON GENERAL ACCOUNTING OFFICE REPORT

"REVIEW OF CONTROLS OVER GOVERNMENT-OWNED PROPERTY IN THE POSSESSION OF CONTRACTORS"

1. *Recommendation.*—We are therefore recommending to the Secretary of Defense that provisions of proposed ASPR changes be revised to meet the predominant need of providing utilization records and a means of analysis of whether the extent and manner of use of Government IPE is satisfactory. (Page 25).

Comment

The Armed Services Procurement Regulation (ASPR) is being revised to prescribe that the contractor be required contractually to establish and maintain a written system for controlling utilization of IPE. It also establishes the responsibility for each Contract Administration activity, and other DOD components, to conduct property system surveys to insure the effectiveness of such a system, and to show the extent and manner of use of Government-owned IPE. Finally, it provides for control, detection, and reporting of Government-owned IPE which is not being effectively and economically utilized by Defense contractors. This case is now receiving a comprehensive review throughout the Department of Defense (DOD), and by selected industrial associations.

Also, we are studying how to maintain utilization records on a machine-by-machine basis over at least the high value items of IPE. If our study proves the practicality of such an approach the ASPR will be modified accordingly.

2. *Recommendation.*—We are recommending to the Secretary of Defense that DIPEC's management controls be reviewed, and new or additional directives be initiated where required to insure that all equipment which could be utilized to meet anticipated needs is considered, and that suitable equipment is offered to authorized requisitioners in each instance when it is available. In this connection we are recommending that a program of personnel training and supervisory review be instituted to assure adherence to established policy and procedures. Further, we are recommending that the Department follow up on a DIPEC study of the 45-day screening period to insure that the period is extended as determined feasible. (Page 34.)

Comment

Defense Supply Agency (DSA) Manual 4215.1, "Defense Industrial Plant Equipment Center (DIPEC) Operations", contains DOD policies, procedures and systems for reporting idle IPE and for submitting screening requirements. When screening by DIPEC results in a determination of non-availability, or an item is allocated and then rejected for valid reasons, DIPEC issues a Certificate of Non-Availability. During the 45-day period following the certification of non-availability DIPEC continues to screen against new idle reports. If a suitable item is located within this period DIPEC advises the requesting agency. If the contract has been awarded, the requesting agency is required to provide DIPEC a copy of the contract. If procurement action has not been initiated prior to expiration of the 45-day period, re-screening is required. Extension of the screening period may be requested by identifying the initial request number and by indicating the day on which procurement action will be initiated. The examples cited by the GAO involve a failure to comply with established procedures, rather than an inadequacy in procedures. They do not demonstrate a need for a change to current existing procedures.

DIPEC has established a training program for all DIPEC commodity managers. Particular emphasis is being placed on the requirement to document the issuance of Certificates of Non-Availability or other specific conditions under which items in inventory are rejected as unsuitable for the intended use.

3. *Recommendation.*—We are recommending that ASPR 13-405 be clarified to show that prior approval is to be made on a machine-by-machine basis and that the term "25 percent non-Government use" be more precisely defined. In addition, we are recommending that ASPR be clarified to differentiate OEP approvals from local monthly approvals for rental purposes. (Pages 35, 37 and 38).

Comment

A requirement for prior approval by the Office of Emergency Planning (OEP) on a machine-by-machine basis for commercial use over 25 percent per machine would create a substantial administrative burden not commensurate with the

goals sought to be achieved. To maintain a factual utilization record by individual machine for commingled Government and contractor-owned plant equipment on a contract-by-contract basis is impractical. It would be very time consuming, disrupt the contractor's production planning process, and result in the addition of a costly administrative burden for both Government and Industry. A more practical approach, which we are pursuing, is one of more aggressive surveillance, maximum use of all plant equipment, and additional emphasis on the collection of adequate rentals. However, DOD has requested that OEP meet with us for the purpose of reaching an acceptable solution on this point, on the question of defining "25 percent non-government use," and the differentiation of OEP approvals from local monthly approvals for rental purposes. Also, as mentioned in our comment #1, we are studying how to maintain utilization records on a machine-by-machine basis for selected high value items of IPE.

4. *Recommendation.*—Accordingly, we are recommending that the Secretary of Defense, in connection with further consideration of a current DOD proposal for revision of the rental base, consider the determination, for rental purposes, of actual machine use on a machine-by-machine basis. Since it appears to us that the proposed method which is under consideration by DOD would be exceedingly complex to administer, particularly as to the effect of contract changes, we are also recommending consideration of this matter if not previously considered by the Department. (Page 42).

Comment

Several alternative proposals are being considered by the ASPR Committee concerning conditions for use of Government plant equipment. Our position regarding controls on a machine-by-machine basis is stated in the response to recommendations #1 and 3.

5. *Recommendation.*—We are recommending that, in order to improve control over the use of Government IPE, the Department consider the need for more stringent language in the present ASPR clause. (Page 45).

DOD has continuously taken the position that contractors should be held liable for any unauthorized use of IPE. However, we will consider the need for stronger language in paragraph (e) of the "use and charges" clause (ASPR 7-702.12) to assure adequate control over the use of Government-owned IPE in possession of Defense contractors.

6. *Recommendation.*—We are recommending, therefore, that DOD re-examine 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. (Page 50.)

Comment

The Air Force heavy press program, a unique situation because of the high cost of the presses, required special OEP approval on all leases. It continues to receive special emphasis. DOD, in conjunction with the Air Force, is re-examining existing arrangements pertaining to rental charges for use of these presses. We are considering such aspects as waiving the rental charges for Government work, increasing rental returns on commercial use, and the feasibility of selling some of the presses to Defense contractors.

7. *Recommendation.*—We are therefore recommending that the DOD place concentrated efforts on the revision and administration of the following aspects of its industrial facility modernization and replacement program: (1) inclusion in procedures of a requirement for specific consideration, and a statement, as to the contractor's ability or willingness to privately finance modernization proposals, (2) consideration of a revision of guidelines to make the provision of Government-furnished plant equipment more directly related to new, major defense programs, (3) a re-examination of the principle of recovery of savings through repricing of incentive-type contracts and subcontracts, and (4) improvement of the validity and review of justification and actual experience data, with particular attention to the aspect of commercial use. (Page 55).

Comment

It is DOD policy (DOD Directive 4275.5, Industrial Facility Expansion and Replacement) that the contractor be encouraged to replace old, inefficient government tools with more modern, efficient, privately owned tools. We will modify our current procedures to require specific consideration, and a statement, as to the contractor's inability or unwillingness to finance equipment modernization.

We will review the need to revise our guidelines as they apply to both new, and existing, major Defense programs. However, we feel that the problems highlighted in the GAO report stem primarily from administration of the modernization program, not inadequate guidelines. These deficiencies will be corrected through a program to improve the technical competency of our property administrators, by a more detailed evaluation of the validity and review of justification and experience data at the local level, and by a requirement for workload projections far enough in the future to allow for administrative and procurement lead time.

The ASPR Committee has had under consideration for some time the subject of recovery of savings under all types of contracts. The views contained in your letter of 30 March 1967 on recovery of savings in the repricing of incentive-type contracts are being considered by the committee.

8. *Recommendation.*—We are recommending that contracting practices and ASPR provisions be studied, with the objective of providing a method for appropriately accumulating, recording and reporting transportation and installation costs which are borne by the Government. (Pages 18, 68 and 69).

Comment

We agree that, as a general principle, the cost of plant equipment should include the cost of transportation for delivery to the current installation site, including the cost of installation. In order to comply with ASPR 7-702.12, it is necessary that cost of plant equipment include the costs of transportation to, and installation in, the present location of plant equipment in Defense contractors' plants for the purpose of charges for use of the equipment. Action will be taken to assure compliance with this requirement by amending ASPR after study of the most feasible way of obtaining equitable cost data, by accounting or statistical methods.

9. *Recommendation.*—We are therefore recommending that a study be made of methods by which DIPEC records could be used for Navy property management purposes, with the objective of eliminating duplicate recordkeeping by the Navy; and that the Department of Defense investigate the possibility of similar duplications in the other military services (Page 67).

Comment

Duplicate recordkeeping related to Navy-owned IPE in possession of contractors is being discontinued. The requirement for records will be satisfied by reliance upon both the contractor and DIPEC property records.

ASPR (Appendices B and C) is being revised to prevent duplication of property records in all Defense agencies. If other duplication is found in the Military Departments, corrective action will be initiated.

10. *Recommendation.*—We are therefore recommending that the Secretary of Defense establish a study project to determine the procedures to be used and the point in the contracting process at which financial control of special tooling should be established. Further, we are recommending that an appropriate section of ASPR be revised to require that proper internal control procedures be employed in the taking of physical inventories which would include appropriate segregation of duties of participating personnel. (Pages 20, 72, 79 and 81).

Comment

Based upon prior experience of both the Military Departments and commercial industry, special tooling has been and should continue to be considered as expendable (consumable) property. The provision of detailing in each contract the special tooling required to produce end items under the contract is considered an adequate basis of control. Normally, special tooling is produced solely for a particular process or machine. Upon determination by the contracting officer that this special tooling is no longer required by the Government, it should be disposed of in accordance with ASPR, Section VIII, Part 5. Therefore, we plan no change to the special tooling provision currently in ASPR.

DOD concurs with the recommendation that we require proper internal control procedures, which include segregation of duties of responsible contractor personnel taking physical inventories of Government property. We will further review the desirability of an ASPR revision (Appendices B and C) in this regard.

11. *Recommendation.*—Accordingly, we are recommending to the DOD that the ASPR be changed to require (1) financial accounting controls for Government-

owned material in the possession of contractors in order to assure adequate control and safeguarding of the assets and also reliable reporting of the amounts on hand, and (2) that proper internal control procedures be employed in the taking of physical inventories which would include appropriate segregation of duties of participating personnel. (Pages 20, 85, and 86).

Comment

Financial controls for material have been the subject of study for many years in DOD. These studies are being continued. In addition, a proposal will be submitted for consideration by the ASPR Committee for criteria to establish contractor requirements for accounting for contractor-acquired Government material.

DOD is currently revising its procedures to exclude from the previous definition of Government-furnished material those items sent to contractors for processing and return. Accounting for these items will be performed by the cognizant inventory control point or other activity of the DOD component in both quantitative and monetary terms. While the contractor will be required to keep item records for scheduling purposes, he will be relieved of financial property accounting.

12. *Recommendation.*—We are recommending that the Department increase management efforts to ensure compliance of ASPR requirements with regard to control of property by DIPEC. We are also recommending that the ASPR be revised to (1) require financial accounting control of Government-owned industrial plant equipment, special tooling, and special test equipment at non-profit institutions, (2) provide more specific criteria regarding "controlled" equipment which is not to be transferred to universities, particularly with respect to its application to industrial production equipment controlled by DIPEC, and (3) require proper internal control procedures in the taking of physical inventories, which would include appropriate segregation of duties of participating personnel. (Pages 22, 91, 96, and 97).

Comment

Paragraph C211.6, Append/x C, Manual for Control of Government Property in Possession of Nonprofit Research and Development Contractors, requires colleges and universities to maintain financial accounts for Government-owned real property and plant equipment. We agree that there has been a failure to exercise compliance with this requirement. We will take the necessary steps to assure compliance.

We question the advisability of requiring financial accounting for special tooling and special test equipment provided non-profit contractors. It is DOD policy to charge special tooling and special test equipment for use on the initial contract as an operating cost. As mentioned in our comment to recommendation #10, we feel it is not desirable to require financial accounting for special tooling. We hold the same view with respect to special test equipment.

We agree that industrial plant equipment costing over \$1,000 a unit, at colleges and universities, should be reported to DIPEC for management and control purposes. Also, available equipment of this type should be screened for utilization prior to donation to the nonprofit contractor under provisions of 42 U.S.C. 1892. A revision to DSA regulations and ASPR designed to meet this objective, will be processed.

13. *Recommendation.*—We are recommending that the DOD (1) place continuing emphasis on efforts to upgrade and improve the quality of property administrators and thus the effectiveness of their surveillance over Government-owned property in the possession of contractors, (2) consider what appropriate incentives should be provided to encourage the establishment and maintenance, by contractors, of an approved system for control over Government-owned property, and (3) initiate an effective program of internal audit of property administration. (Pages 23 and 99).

Comment

DOD has established a joint study project to evaluate current position classification standards for property administrators (GS-1103), establish position guidelines supplementing those of the Civil Service Commission, and provide qualification and performance standards. We consider this project of utmost importance. You may be assured that it will receive our close attention.

Under current ASPR procedures the contractor is required to establish and maintain an approved system for accounting and control of Government-owned property. We believe a specific ASPR (Appendices B and C) requirement for annual review of the contractors property accounting system is needed. The ASPR committee is considering adoption of such a requirement for both commercial and non-profit contractors. Motivation should not be in the form of an incentive or an award to accomplish a task otherwise required by the contract and sound industrial practice.

We concur that there should be additional emphasis on the audit of controls over, and utilization of, Government property in the possession of contractors. As noted in the GAO report, ASD(C) memorandum of December 27, 1966, to the Assistant Secretaries of the Military Departments (FM), the Director, Defense Contract Audit Agency, and the Comptroller, DSA, established areas of audit responsibility for both contract and internal auditors in Government property audits. Collaterally, the memorandum established procedures for assist audits as appropriate by either contract or internal auditors. This policy guidance, together with the internal audits scheduled or planned by the internal audit agencies of the Military Departments and DSA, should achieve the audit coverage contemplated by part three of the GAO recommendation.

14. *Recommendation.*—We are recommending, therefore, that the new ASPR section, which defines the duties and responsibilities of Government property administrators, incorporate a policy statement to this effect for the guidance of such officials. (Page 108).

Comment

DOD agrees it is reasonable to expect that those accounting principles and standards applicable to Government-owned property in possession of contractors should be equivalent to those applied in normal industrial practices. The new ASPR supplement, covering the duties and responsibilities of the property administrator, will be amended to require acceptable accounting principles and standards commensurate with that of sound industrial practices. If more exacting standards than sound industrial practices are necessary, the requirement will be established by contract provision.

Separate Comment

The GAO pointed out in its report that guidelines should be included in ASPR for determining when to capitalize or expense costs incurred on Government real property in possession of Defense contractors. (page 71). DOD will develop necessary criteria for capitalizing or expensing costs incurred on Government real property in possession of Defense contractors for inclusion in ASPR.

Chairman PROXMIRE. Give us as much detail on that as you can.

IDENTICAL BIDDING

Back in 1961 Senator Douglas and I were engaged—Senator Douglas took the lead, certainly—in asking about collusive identical bidding on advertised competitive procurement. In that year, later that year, the administration issued an order on collusive competitive bidding which has resulted in a steady diminution of it. This year there was an especially spectacular job—that is the latest year in which we have a record—according to the report I have before me now, issued last July, there was a drop of 32 percent in identical bids.⁶

I think Senator Douglas was right in doing this, and performed a real service in calling attention to it. But, of course, the area of collusive bidding that would be the greatest and result in the greatest cost would not be in the advertised competition bidding; I think we should continue to be alert, continue to have reports on it, and watch it very closely. But it would be in the so-called negotiated competitive bidding, it would seem to me, where the greatest danger lies.

⁶ See hearings, 1961, p. 26; see also, "Identical Bidding in Procurement, Sixth Report of the Attorney General," July 1967.

In the first place, these are larger items. Secondly, it is a much bigger area of procurement.

Thirdly, because there are so often one or two or three very large supply firms—there is more of a tendency for these firms to get together. They know each other, they are familiar with this, there is a perfectly human tendency, perhaps, for one to say, "We will take this one and you take the next one, and so forth."

Is there any way, I know this is hard to get at, is there any way that you could give us a report on this or investigate it or suggest what we could do about it to watch it more closely?

It seems to me here we can get a great deal more savings than we can in the advertised competitive bidding area.

Mr. MORRIS. Let me ask Mr. Malloy to comment on this.

Mr. MALLOY. Yes—Mr. Chairman, I am familiar with the report that you have in front of you. I don't recall whether it picks up both the negotiated and formally advertised or not.

Chairman PROXMIRE. It seems to us—and Mr. Ward has advised me that it is his view, too—that this is advertised competitive bidding.

Mr. MALLOY. Fine. I think that this is a complex enough subject that it would take a little more time to consider how to do this and what the practicalities are. We would be delighted—

Chairman PROXMIRE. Wouldn't you agree that there could be a serious problem here?

Mr. MALLOY. There might be, bearing in mind that most of the incidents of tie bids—this is not a listing of collusive bids—it is a list of tie bids. I think this is demonstrative that this is not a collusive situation. That happens normally in the kind of standard items we buy. We buy most of our standard items by formal advertising. The potential in the negotiated—I would be glad to furnish that.

Chairman PROXMIRE. I wish you would give us a report on that. (Material below was supplied by witness.)

With respect to your question concerning the possibility of identical proposals being received and the evils attendant thereto, and upon a further review of the Armed Services Procurement Regulation, we believe that the government's interest is adequately protected thereby. The regulation, ASPR 1-111.2, covers reports of identical or equal bids or proposals and contracting officers are admonished to report any evidence of violations of the anti-trust laws directly to the Attorney General for appropriate action.

In addition, ASPR 1-115, requires generally that in all formally advertised and negotiated procurements (with certain limited exceptions) each bidder or offeror certify that its prices have been arrived at independently and have not been disclosed to any other bidder or offeror. If the prices have been disclosed to other bidders or offerors a full explanation of the circumstances of the disclosure must be made and unless the government determines that such disclosure was not made for the purpose of restricting competition, such bid or offer cannot be considered for award. In the event that this certification is suspected of being false or there is an indication of collusion, the matter is handled in accordance with ASPR 1-111.2.

Further, the negotiation process involves a detailed examination and evaluation by the contracting officer of each element in the proposal and a confrontation in the "negotiation" of each of the significant elements with the contractor to arrive at a mutually acceptable price. Thus, the "adversary nature" of the negotiation is effective protection of the government's interest in the unlikely event of the receipt of tie proposals in a competitively negotiated procurement. The likelihood of identical proposals being received in competitive negotiated procurements is considered so minimal as not to justify the cost of a formal reporting system. Copies of the ASPR regulations are attached.

ARMED SERVICES PROCUREMENT REGULATION, 1-111.2

1-111.2 *Non competitive Practices.*

(a) Unless bids or proposals are genuinely competitive, contract prices tend to be higher than they should be. If the Secretary concerned or his representative considers that any bid received after formal advertising evidences a violation of the antitrust laws, he is required by 10 U.S.C. 2305(d) to refer such bids to the Attorney General for appropriate action. Similarly, evidence of such violations in negotiated procurements should be referred to the Attorney General. Practices which are designed to eliminate competition or restrain trade and which may evidence possible violations of such laws include collusive bidding, follow-the-leader pricing, rotated low bids, uniform estimating systems, sharing of the business, identical bids, etc.

(b) Reports of identical or equal bids or proposals should not be submitted automatically, but only where there is some reason to believe that those bids or proposals may not have been arrived at independently. Such reports should be accompanied by conformed copies of the bid or proposal, other contract documents, and supporting data. The report should set forth:

ARMED SERVICES PROCUREMENT REGULATION, 1-115

INTRODUCTION

Certificate of Independent Price Determination (June 1964):

(a) By submission of this bid or proposal, each bidder or offeror certifies and in the case of a joint bid or proposal, each party thereto certifies as to its own organization, that in connection with this procurement:

(1) the prices in this bid or proposal have been arrived at independently, without consultation, communication, or agreement, for the purpose of restricting competition, as to any matter relating to such prices with any other bidder or offeror or with any competitor;

(2) unless otherwise required by law, the prices which have been quoted in this bid or proposal have not been knowingly disclosed by the bidder or offeror and will not knowingly be disclosed by the bidder or offeror prior to opening, in the case of a bid, or prior to award, in the case of a proposal, directly or indirectly to any other bidder or offeror or to any competitor; and

(3) no attempt has been made or will be made by the bidder or offeror to induce any other person or firm to submit or not to submit a bid or proposal for the purpose of restricting competition.

(b) Each person signing this bid or proposal certifies that:

(1) he is the person in the bidder's or offeror's organization responsible within that organization for the decision as to the prices being bid or offered herein and that he has not participated, and will not participate, in any action contrary to (a) (1) through (a) (3) above; or

(2) (a) he is not the person in the bidder's or offeror's organization responsible within that organization for the decision as to the prices being bid or offered herein but that he has been authorized in writing to act as agent for the persons responsible for such decision in certifying that such persons have not participated, and will not participate, in any action contrary to (a) (1) through (a) (3) above, and as their agent does hereby so certify; and (b) he has not participated, and will not participate, in any action contrary to (a) (1) through (a) (3) above.

(c) This certification is not applicable to a foreign bidder or offeror submitting a bid or proposal for a contract which requires performance or delivery outside the United States, its possessions, and Puerto Rico.

(d) A bid or proposal will not be considered for award where (a) (1), (a) (3), or (b) above has been deleted or modified. Where (a) (2) above has been deleted or modified, the bid or proposal will not be considered for award unless the bidder or offeror furnishes with the bid or proposal a signed statement which sets forth in detail the circumstances of the disclosure and the Secretary, or his designee, determines that such disclosure was not made for the purpose of restricting competition.

(b) The fact that a firm (1) has published price lists, rates, or tariffs covering items being procured by the Government, (2) has informed prospective customers of proposed or pending publication of new or revised price lists for such

items, or (3) has sold the same items to commercial customers at the same prices being offered the Government does not constitute, without more, a disclosure within the meaning of paragraph (a) (2) of the Certificate.

GENERAL PROVISIONS

(c) It is not required that a separate written authorization be given to the signer of the bid or proposal for each procurement involved where the signer makes the certification provided in paragraph (b) (2) of the Certificate, provided that with respect to any blanket authorization given, (1) the procurement to which the Certificate applies is clearly within the scope of such authorization, and (2) the person giving such authorization is the person responsible within the bidder's or offeror's organization or the decision as to the prices being bid or offered at the time the Certificate is made in a particular procurement.

(d) After the execution of an initial certificate and the award of a contract in connection therewith, the contractor need not submit additional certificates in connection with proposals submitted on "work orders" or similar ordering instruments issued pursuant to the terms of that contract, where the Government's requirements cannot be met from another source.

(e) The authority to make the determination described in paragraph (d) of the above certification shall not be delegated to an official below the level of the Head of a Procuring Activity.

(f) When a certification is suspected of being false or there is indication of collusion, the matter shall be processed in accordance with 1-111. For rejection of bids which are suspected of being collusive and for the negotiation of procurements subsequent to such rejection, see 2-404.1 (b) (viii) and 3-215.

Chairman PROXMIRE. Gentlemen, I want to thank you very much for a fine performance, a very reassuring and helpful report. I trust you are going to follow up now with the progress report in the specific areas we suggested.

Mr. MORRIS. We shall, Mr. Chairman.

Chairman PROXMIRE. You are doing an excellent job.

Tomorrow we will reconvene at 10 o'clock to hear Senator Dominick, Congressman Minshall, and our principal witness is Lawson Knott, Administrator of the General Services Administration.

(Whereupon, at 12:45 p.m., the committee adjourned to reconvene at 10 a.m., Wednesday, November 29, 1967.)

ECONOMY IN GOVERNMENT PROCUREMENT AND PROPERTY MANAGEMENT

WEDNESDAY, NOVEMBER 29, 1967

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON ECONOMY IN GOVERNMENT
OF THE JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The subcommittee met, pursuant to recess, at 10 a.m., in room S-407, the Capitol, Hon. William Proxmire (chairman of the subcommittee) presiding.

Present: Senators Proxmire and Percy.

Also present: Ray Ward, economic consultant.

Chairman PROXMIRE. The subcommittee will come to order.

Our first witness this morning is the Honorable Peter Dominick, a U.S. Senator from Colorado. We are very happy to have you here, Senator Dominick. You may proceed in your own way.

STATEMENT OF HON. PETER H. DOMINICK, A U.S. SENATOR FROM THE STATE OF COLORADO

Senator DOMINICK. Thank you, Mr. Chairman and members of the subcommittee. I appreciate the opportunity to appear before you today on this matter of such great importance to the taxpayer and to efficiency in government.

I have been growing concerned, as has your committee, over the increasing percentage of our military procurement which is accomplished without open competition. Certainly, in some instances, national security reasons might justify some such noncompetitive actions, but when the average percentage of noncompetitive procurement reaches 86 percent, and the 100 largest business firms continually get a larger and larger share of our military procurement, there is cause for alarm.

I began delving into this situation last year when one of my constituents—Custom Packaging Co., a small business firm in Aurora, Colo., which developed a shoulder-borne portable, recoilless flame weapon—was given what I felt was very unfair treatment by the Army. After expending its own funds to develop and demonstrate the weapon to the Army—the first weapon of this type that had ever been produced by way of equipment for the Army—Custom also was the low bidder on the invitation for bids for the initial development of the weapon. The Army, however, awarded the development contract to Nortronics, a division of Northrop Aviation, at more than double the price bid by Custom Packaging Co., costing the taxpayer more than \$200,000 above the low bid by my constituent.

I want to interpolate here that our constituent also bid on a fixed-cost basis, and the Northrop bid, which was twice what Custom's was, was on a cost-plus-incentive-fee basis. So that the cost could be just astronomical compared to what my constituent's bid was.

Now looking into other Army procurements, I found a pattern: wherever procurement was open to competition, the price was reduced dramatically.

This was true in the case of the AN/PRC-25 radio set where the unit price dropped from \$2,156.91 each in the first production contract to less than \$600 per unit when exposed to open competition.

It was true in reverse with the AN/GRA-6 control chest set. From May 1961 through June 24, 1964, the Army bought this control chest set under six different contracts at unit costs ranging from \$145.50 to \$200 each. Since June 24, 1964, this equipment has been removed from open competitive procurement and the price has more than doubled. The most recent award announced January 19, 1967, by Commerce Business Daily, in the total amount of \$1,220,665, shows an average unit price of \$418.94 for this same equipment.

There are literally hundreds of these cases which need investigation. With my limited staff, I certainly cannot undertake such a large task, but I hope this can be done by the appropriate committee of the Senate, whether it is this committee or Senator McClellan's Government Operations Committee.

I am also greatly concerned about one practice I have discovered being carried out by the Navy which, if allowed to continue and expand, could completely destroy open competitive procurement in the future. This involves a practice called leader-follower procurement procedure. It is an incredible story.

The Naval Research Laboratory, Washington, D.C., scored a breakthrough in airborne transponder development in late 1964 and early 1965. The Naval Research Lab assigned the nomenclature APX-72 to its transponder, which was more than 95 percent developed "in-house" by the Navy. A transponder is a small electronic device mounted in an aircraft which emits a signal permitting ground stations or other aircraft to identify it as friendly or hostile and can itself similarly interrogate other aircraft. It also is an identification device for radar identification in heavy weather flying.

In April 1965, the Navy awarded a contract in the amount of \$58,000 to Bendix Radio Division, Baltimore, to "polish" or "package" the unit into a "mass-producible" model. The value of the contract with Bendix was increased to \$124,000 when a requirement was added for several more prototypes and to make some minor improvements to meet the military's AIMS program.

Less than a year later, Bendix delivered a model to the Navy which was flight tested and conditionally approved for production, although certain improvements were still needed which the Navy felt could easily be made while preparation for volume production was underway.

Bendix Radio was only one of several major firms working to develop a new, lightweight, flexible transponder. Several of these firms working with other services, had been persuaded to invest their own money into this development on the promise that whichever new

transponder was eventually chosen, all competing firms would have an opportunity to bid on volume production of that transponder.

The Navy persuaded the Department of Defense that the Navy-Bendix transponder was superior to others in development. And in June 1966, Bendix was very quietly given a sole-source production contract for 2,300 APX-72 transponders. "Urgent need" was cited as justification for the sole-source contract and first production units were due for delivery in June 1967. It was thereafter decided by the Navy Department to award Bendix an "extraordinary" type of contract called a leader-follower.

Under this arrangement and without any of the usual notification through the Commerce Business Daily, Bendix's extraordinary contract provided that Bendix was to be given a contract for 8,500 additional units of the APX-72 transponders with the further proviso that of the entire total of 10,800 units, 40 percent would be shared with (or subcontracted to) a "follower" company whom Bendix would take under its wing. The Navy justified this approach on two grounds:

(1) That in the normal course of events Bendix would not have a data package for almost a year. But, by having a Bendix handpicked "follower" to understudy the initial production, at least 6 months' time could be gained in getting a second source into production; and

(2) Being able to hold Bendix responsible for the quality and precision of the "follower's" product, complete interchangeability or "commonality" could be assured.

The absence of a technical data package is open to question because Bendix issued such a technical package to its component subcontractors and to potential "followers" at the time of solicitation.

In its second point, the Navy admitted, in effect, that it did not have the ability to demand or obtain from manufacturers performing Navy contracts equipment "common" with or identical to the same equipment, turned out from identical drawings by another manufacturer.

A further part of the agreement between the Navy and Bendix is still more disturbing. This agreement with Bendix held that to perpetuate the commonality feature on future production, Bendix and its handpicked "follower" would be permitted to share all future production.

I want to emphasize that, Mr. Chairman: "all future production."

This is no small factor when you consider that the APX-72 is destined to be the transponder on all military aircraft in the future and will be bought in a civilian version by the Federal Aviation Administration.

The first notice that anyone had of these proceedings came in May 1967, when the fact was announced in the Commerce Business Daily that Bendix was conducting competition to choose the "follower." Bendix announced that it would require a complex management and technical proposal to be submitted within 10 days. Other requirements listed by Bendix were so restrictive that all small business firms were discouraged from bidding. Bendix also held a bidders' conference and disclosed at that conference that Bendix intended to put one of its teams in the "follower's" plant to keep an eye on production. Furthermore, Bendix would demand detailed cost figures and other similar data. At this point, a number of major firms dropped out, unwilling

to have a competitor given access to so much information which normally is confidential within the company itself. The result was a further limiting of competition.

Bendix was unable to work out a satisfactory contract with the eventually chosen "follower," Wilcox Electric Co., of Kansas City, until November 8, at which time Bendix itself had been able to deliver only 10 units instead of 200 units of the APX-72 as scheduled. Although the Navy has refused to disclose the "follower" price officially, the Navy has said unofficially that the follower price is just under \$2,200 per unit. However, the Navy-Bendix price, which will be higher than the "follower's" price to Bendix, is still under negotiation.

There is obviously no real meaningful competition involved in this procurement, either with regard to price or in the choice of producers, and it is equally obvious that there will be no meaningful competition in future contracts under the Navy's proposed procedure. The current Navy plan to limit production to Bendix and Wilcox Electric Co., in effect, hands a free patent to a private contractor for exclusive production in perpetuity of an item developed not only at taxpayers' expense, but largely by Government personnel.

The finality with which the Navy views this transaction is evident in the response received by the Senate Select Committee on Small Business, on which I serve, from the Honorable Graeme C. Bannerman, Assistant Secretary of the Navy (Installations and Logistics). Mr. Bannerman said, and I quote:

Your comment that small producers of transponders not participating in the current procurement will, to all intents and purposes, be foreclosed from supplying transponders to military departments in the foreseeable future, applies only to this particular transponder.

Since this particular transponder is to be the unit installed in all future military aircraft and the military need has been projected in the first 5 years at 30,000 units and will cost in excess of \$70 million, it seems to me that this entire transaction is open to very serious question, and I would hope that further investigation might be conducted without delay.

Mr. Chairman, I commend you and your committee for the work you are doing in this area and would be pleased to offer you any assistance which I might render.

I do want to say that I have gone into considerable detail on the last Navy contract because it seems to me that it opens up a new method of contracting which is going to almost wholly eliminate competition.

Also, I want to say that I know a great deal of the details on the Custom Packaging case and on this ANPRC 25 radio set, and have made two or three speeches—three I believe it is at this point—on these cases in the record, which I will be happy to furnish to the committee if you would like to have them.

(The material later supplied for the record is in app. 11, p. 560.)

Chairman PROXMIRE. Has the GAO investigated these cases?

Senator DOMINICK. The GAO went into the question of whether the contract was properly given to Northrop, Inc., in the Custom Packaging case, and they came to the conclusion that it was a question of technical evaluation, and since they were not qualified to make a technical evaluation, therefore, they had to accept the Army's word for it.

Chairman PROXMIRE. Well, that certainly is not satisfactory. They have a very large and a very able staff. They have done a fine job in many other respects for this committee and for the Government Operations Committee and others.

Senator DOMINICK. Yes; they have.

This was an interesting pattern, though, Mr. Chairman.

In a number of cases that I speak about in these speeches that I put into the record, on each question, where the contract was awarded to a high bidder, and the low bidder and small businessman was eliminated, it resolved primarily around what the Army procurement people called technical evaluation. This means their evaluation of the competency of the bidder, the competency of the personnel, and the type of proposal which has been made to the Army.

In each case, the GAO has indicated that it does not have the qualified staff in order to make an independent evaluation of this judgment factor, and therefore they have to accept the judgment factor, and since this is the major item in the overall evaluation of the bids, the Army is in a position of being the last resort. You do not really have a review.

Chairman PROXMIRE. What is this—the first case?

Senator DOMINICK. This is the Custom Packaging case that I am talking about. But there are others where the same comments have been made by GAO.

Chairman PROXMIRE. Custom Packaging case—that was the case involving the firm in Aurora, Colo.?

Senator DOMINICK. Right. That is the flamethrower.

Chairman PROXMIRE. Now they did not study the Bendix case?

Senator DOMINICK. As far as I know, we have not had any study of that.

Chairman PROXMIRE. All right. We will recommend that the GAO follow up on it, and do all we can to see they check that out. That would have other elements than the competence or financial responsibility of the bidders. Because there were major firms, you say, which in effect were disqualified because of the very limited requirements, and also because Bendix was free to specify that they would have their own people on the premises of the so-called follower.

Senator DOMINICK. Right.

Chairman PROXMIRE. To follow up everything that went on. We can understand why the major firms would drop out under these circumstances.

Senator DOMINICK. They would not like it, I am sure.

Chairman PROXMIRE. I think that this is most helpful, Senator Dominick, because there is no questioning your point. The policy of the Congress is clearly expressed that competitive bidding should be the means of procurement. The amount of competitive bidding has declined. It has declined in recent years. Between 1961 and 1967 Secretary Morris testified that competitive bidding had gone up somewhat.

The Defense Department takes a pretty broad view of competitive bidding. They include not only advertised competitive bidding, but what they call competitive negotiated procurement.

Senator DOMINICK. Between a preselected group of firms.

Chairman PROXMIRE. That is right. They select the particular firms, and it can be just two firms. Of course, as most of us would recognize, this has very serious limitations.

At any rate, there also is an increasing concentration of procurement with the hundred largest firms. And, it is this kind of specific example which is most helpful. They properly resent it when we just make broad charges they are not doing their job. But, when you can come up with examples of this kind, I think it is most helpful. We will certainly follow this up as completely as we can, both with the Comptroller General and with the Defense Department. The Comptroller General is going to reappear before this committee in a few days; they were the leadoff witness. We will bring this up with them at that time, and notify them at once we want to look into it.

Senator DOMINICK. Thank you very much. I appreciate it.

Chairman PROXMIRE. Is Congressman Minshall here?

We are honored and pleased to have as our next witness the Congressman from the 23d District of Ohio, Representative William Minshall.

**STATEMENT OF HON. WILLIAM E. MINSHALL, A REPRESENTATIVE
IN CONGRESS FROM THE 23D CONGRESSIONAL DISTRICT OF THE
STATE OF OHIO**

Mr. MINSHALL. Mr. Chairman, let me preface my remarks with a word of appreciation for the splendid service you are performing in behalf of the American taxpayer. It is no exaggeration to suggest that the ultimate result of these hearings could be the saving of billions of defense dollars.

My purpose in appearing here today is to very briefly outline the action which has taken place regarding my bill, H.R. 10573, which I introduced last June 7 to strengthen the Truth in Negotiations Act.

After 2 days of testimony, and your own years of experience on this committee, I know you have little need for my reviewing the many compelling reasons why this act must be strengthened. Your distinguished chairman, Senator Proxmire, certainly ranks as an expert. He and I share a mutual concern in the matter, inasmuch as his bill, S. 1913, is identical to mine.

Our legislation would guarantee a full-fledge postaudit program by the Department of Defense of all financial records of defense contractors and subcontractors, the object being to determine whether Defense has been overcharged for materials. Minimal spot checking by the General Accounting Office has uncovered overpricing on defense contracts at the rate of about \$13 million a year, and this figure undoubtedly would be multiplied many times if GAO had the vast army of auditors which the Pentagon possesses to institute a thorough postaudit.

I am pleased to report that the outlook for H.R. 10573 is encouraging. The bill has been referred to the House Armed Services Subcommittee on Special Investigations, of which Congressman Porter Hardy is chairman, and I have been advised that hearings will be held after Congress reconvenes in January.

I shall do all that I can to work vigorously for enactment of this legislation and I hope that I shall do so with the support of the members of this great committee.

There has been, as this committee knows, some positive action taken by the Pentagon in this area. Secretary Nitze, on September 29, issued a memorandum to all military departments announcing that new auditing procedures would be adopted by the Department of Defense. (See p. 409.)

On October 26 I asked the Comptroller General to give me his written opinion of the new Defense regulations. Mr. Staats' reply to me, dated November 3, stated that the regulations being promulgated by DOD substantially accomplish the purpose of the Proxmire-Minshall bills. His letter carried the assurance that GAO would keep a close eye on the manner in which the regulations were carried out.

The Comptroller General did point out, however, that Secretary Nitze's memorandum—and I quote—"is silent on the matter of the agency's right of access to subcontractors' performance records which was specifically provided for in your bill." This, in my opinion, is a serious oversight.

Chairman Mendel Rivers of the House Committee on Armed Services apparently shared my concern. He requested a report from the Defense Department on H.R. 10573. The reply Chairman Rivers received, dated November 6, from the General Counsel of DOD indicated that the Pentagon feels its new contract procurement regulations would substantially fulfill the objectives of H.R. 10573 and that the legislation therefore would not be necessary.

It is important to point out, however, that the November 9 letter from the General Counsel did add that the Defense Department "interposes no objection to its enactment."

Ever since the Truth in Negotiations Act became law, there has been a running debate in the Pentagon as to whether further clarifying legislation was necessary. It seems to me that enactment of the Proxmire-Minshall measure would put an end to that debate for all time.

With your many years' experience in the Congress, and particularly as members of this committee, I do not need to tell you that any governmental regulation is a transient thing at best.

After 13 years in Congress and 9 years as a member of the Department of Defense Appropriations Subcommittee, it has been my observation that regulations not only are subject to oversight and misinterpretation, they also are open to change without notice. They are particularly vulnerable in the advent of a new Secretary of Defense or with any change in administration.

There is great unanimity of agreement that strict postaudit checks on contractor and subcontractor financial records are needed. The GAO has urged this for years and has said that the proposed legislation has much merit. The Department of Defense has admitted the necessity for more strict controls by issuing regulations which conform to much of the language in the bill, and has indicated that it has no intention of opposing its enactment into law. The House Committee on Armed Services is prepared to give the bill a hearing.

I hope and trust that this committee will add its powerful voice to urge enactment of the Proxmire-Minshall legislation.

I thank you, Mr. Chairman.

Chairman PROXMIRE. Thank you, Mr. Minshall. I want to congratulate you on pressing so hard for this legislation. What you have done in the House in advancing it I think is absolutely invaluable and essential. You deserve a great deal of credit for that.

I want to tell you that—I am sure that other members of this committee, and I also, will do all we possibly can to encourage its passage in the Senate, and also, of course, in the House.

Now, you point out that—and I think this is an excellent point—the Comptroller General says—and I think that our interrogation yesterday of the Assistant Secretary of Defense for Logistics, Mr. Morris, confirmed the point—that Secretary Nitze's memorandum is silent on the agency's right of access to subcontractors' performance records, which was specifically provided for in our bill.

NEED FOR POSTAUDIT LEGISLATION

He indicated that, of course, the prime contractor would have the obligation to follow up on this. But I think that this is a special reason why this legislation should be enacted.

Now, in addition to that, even if the Nitze memorandum were revised to provide access to subcontractors on the same kind of basis, still the enactment of legislation, as you say, is most essential. And I think we are essentially aware of it today. In the last couple of days we have been made aware that the Secretary of Defense is going to move on to another job. And it could be that an entirely new administration of the Defense Department would come in. Under these circumstances, regulations of this kind could be changed very promptly.

We also know that there is always opposition. After all, it has taken a long, long time—5 years—to get any action under the Truth in Negotiations Act—any complete action. There is opposition to making this Truth in Negotiations Act effective, and that opposition could work its influence on a new Secretary of Defense. And under these circumstances, the one security that the taxpayer has would be the enactment of a law.

So I think that the points you make here this morning are most welcome, and logical.

I might clarify what I said about the response of the Defense Department. The question was as follows:

"Does this"—referring to the Nitze memorandum—"extend to subcontracts—this Nitze order—or is it only confined to prime contracts?"

Mr. Malloy stated—who was responding for Mr. Morris—

Mr. Chairman, there is a flow-down from the prime contract to the subcontract. In other words, this audit right follows the same line as the law itself. Wherever the law is applicable, and it is applicable at the subcontract level under certain conditions.

And I said where it is not applicable.

MR. MALLOY. It is not applicable under the same conditions that it would not be applicable in a prime contract; namely, if there is adequate price competition, or if the purchase is for catalog items, or for items the price of which is set by law or regulation.

At any rate, I do feel, as you emphasized so well in your statement, that it would be most desirable to have this spelled out in a law, and then, as you say, there can be no question about it.

Mr. MINSHALL. Mr. Chairman, I want to again thank you for your cooperation. As I said in my statement, this legislation could conceivably save the taxpayers billions. I would like to point out since 1965, when our total prime contract awards for defense—they were then in fiscal 1965, \$27.4 billion. In 1966 they went up to \$37.2 billion. And this year, under fiscal 1967, they are \$43.4. And I think they are even going up higher next year. And I think our total military expenditure this year could far exceed what they have already said it would be by up to \$5 billion to \$7 billion.

Chairman PROXMIRE. And then when you recognize the fact that most of this procurement is on a negotiated, not on a competitive basis, the only safeguard for the taxpayer is having current, comprehensive, and accurate records available, and the right of the auditor to have access to these records.

When you recognize that, it seems to me that this kind of legislation on the Truth in Negotiations Act is especially essential. And it is no exaggeration at all in my view to say it will save billions of dollars a year.

Mr. MINSHALL. I am glad you pointed out most of these contracts are negotiated. For the record, in case you do not have it in there already, the formally advertised contracts last year amounted to \$5.8 billion out of the over \$43 billion, or only 13.4 percent of all procurement contracts for the Defense Department.

Chairman PROXMIRE. They have this other category of negotiated competition—negotiated price competition—which includes another substantial percentage. But, still, the overwhelming amount of it is by negotiation without any competition.

Mr. MINSHALL. Thank you very much, Mr. Chairman.

Chairman PROXMIRE. Thank you for a fine presentation.

The Senate is scheduled to have a rollcall vote at 10:30 this morning. If you gentlemen—Mr. Knott and your assistants—would be patient, I think it might be helpful to have a recess. There is the vote right now. As soon as the voting is over, I will be back, and we will reconvene. (At this point in the hearing a short recess was taken.)

Chairman PROXMIRE. The subcommittee will come to order.

Our principal witness this morning is the Honorable Lawson B. Knott, Jr., Administrator of General Services Administration. We are pleased to have you with us again, Mr. Knott, to give us your views on the subject outlined in my letters of November 8 and 20 of this year, which will be included in the record.

(The material to be furnished for the record follows:)

NOVEMBER 8, 1967.

HON. LAWSON B. KNOTT, JR.
Administrator, General Services Administration,
Washington, D.C.

DEAR MR. KNOTT: This letter will confirm previous information given to your staff that the Subcommittee on Economy in Government of the Joint Economic Committee will hold hearings on November 27-30, 1967. You and the associates you may wish to accompany you are scheduled to testify in Room AE-1, The Capitol, Joint Atomic Energy Committee Hearing Room, Wednesday, November

29 at 10:00 A.M. Please forward 100 copies of your prepared statement at least one day prior to your appearance.

In general, the hearings will be a follow-up on the conclusions and recommendations contained in our report of July 1967. There are a number of specific references therein to GSA which will merit special attention at the upcoming hearings:

1. Procurement policies and practices.
 - a. Developments in use of Buy American Act.
 - b. Program for procurement and management of Automatic Data Processing Equipment (ADPE).
 - c. Public utilities. Savings and adequacy of staffing. Extent of G.S.A. participation before regulatory bodies.
 - d. Competitive versus negotiated procurement. Use of principles embodied in Truth in Negotiations Act (P.L. 87-653) by G.S.A.
 - e. Procurement of commercial industrial products and services pursuant to BOB Circular No. A-76, revised.
2. Inventory management.
 - a. Progress in control of short shelf life items.
 - b. Status report on inventory of ADPE.
 - c. Utilization of excess and surplus personal property.
3. Progress in developing a National Supply System.
 - a. DOD/GSA relationships.
 - b. GSA civilian agency relationships.
4. Status of management of real properties pursuant to Budget Circular A-2, revised.

If additional information is required, please contact Mr. Ray Ward, Staff Consultant, Code 173—Ext. 8169.

Sincerely yours,

WILLIAM PROXMIRE.

NOVEMBER 20, 1967.

HON. LAWSON B. KNOTT, Jr.
Administrator, General Services Administration
Washington, D.C.

DEAR MR. KNOTT: Reference is made to your scheduled appearance in my letter of November 8, 1967 advising you of the hearings of the Subcommittee on Economy in Government on November 29, 1967.

With respect to the management of short shelf life items, will you bring us up to date on the programs to use the medical stockpile, including utilization and losses since our last hearing and other pertinent information.

Best regards,

WILLIAM PROXMIRE.

Chairman PROXMIRE. Our hearings have largely been concerned with procurement and property management subjects. The declaration of policy in the act establishing GSA states, section 2:

"It is the intent of the Congress in enacting this legislation to provide for the Government an economical and efficient system for (a) the procurement and supply of personal property and nonpersonnel services, including related functions such as contracting, inspection, storage, issue, specifications, property identification and classification, transportation and traffic management, establishment of pools or systems for transportation of Government personnel and property by motor vehicle within specific areas, management of public utility services, repairing and converting establishment of inventory levels, establishment of forms and procedures, and representation before Federal and State regulatory bodies; (b) the utilization of available property; (c) the disposal of surplus property; and (d) records management."

You, therefore, have much at stake in these hearings, and I know you and your agency have made a large contribution in this broad and enormously important field. Please introduce your associates and proceed.

STATEMENT OF HON. LAWSON B. KNOTT, JR., ADMINISTRATOR, GENERAL SERVICES ADMINISTRATION; ACCOMPANIED BY H. A. ABERSFELLER, COMMISSIONER, FEDERAL SUPPLY SERVICE; HARRY VAN CLEVE, GENERAL COUNSEL; DOUGLAS E. WILLIAMS, COMMISSIONER, TRANSPORTATION AND COMMUNICATIONS SERVICE; WILLARD L. JOHNSON, JR., ASSISTANT ADMINISTRATOR FOR ADMINISTRATION; WILLIAM A. SCHMIDT, COMMISSIONER, PUBLIC BUILDINGS SERVICE; JOHN G. HARLAN, JR., COMMISSIONER, PROPERTY MANAGEMENT AND DISPOSAL SERVICE; AND JOE E. MOODY, DEPUTY ADMINISTRATOR

Mr. KNOTT. Thank you, Mr. Chairman.

Mr. Chairman and members of the subcommittee, it is a pleasure to appear before you again to discuss the programs and activities of the General Services Administration.

I propose today to review briefly programs of particular interest to the subcommittee as evidenced by your letter to me of November 8, 1967, with emphasis on the progress we have made in implementing recommendations included in the report of your subcommittee to the Congress in July 1967.

We watch with interest the almost continuous deliberations by this committee on a wide range of subjects, including revenue sharing and other matters of national interest. We are pleased that we have this opportunity to appear.

I do apologize. I always hate to have a lengthy statement, but to cover the things that you specifically asked us about, I think it would be best if I read the statement. I think I probably can do it in 15 to 20 minutes or less, and then we can respond to questions. Since we do cover a wide area, I have with me the Commissioner of our Federal Supply Service, Mr. Abersfeller, who was with me at our last appearance; our General Counsel, Mr. Harry Van Cleve; our Commissioner of Transportation and Communications Service, Mr. Williams; our Assistant Administrator for Administration, Mr. Johnson; our Commissioner of Public Buildings—while there are no specific items here on public buildings, there may be some interest in that area—Mr. Schmidt is with us. Also, the Commissioner of our Property Management and Disposal Services, Mr. Harlan, is here. Mr. Chairman, this service represents a consolidation of all of our disposal activities, real and personal property, as well as stockpile disposals, in one service. And, my deputy, Mr. Joe Moody.

PROGRESS IN DEVELOPING THE NATIONAL SUPPLY SYSTEM

To proceed with the National Supply System, to which we always like to make at least passing reference, I would like to report that we are continuing our efforts toward full implementation of the national supply system. The cooperation of DOD activities and civilian agencies in this effort continues at the highest level.

Since my last report to you in May, agreement has been reached with the Defense Supply Agency on the transfer to GSA of the

primary management of 65 Federal supply classes. Some 51,000 items in these classes have already been transferred and 15,000 additional items will be transferred by July 1, 1968.

Chairman PROXMIRE. What is the dollar volume?

Mr. ABERSFELLER. The dollar value of the inventories transferred is approximately \$80 million. This figure includes the hand tools transferred in 1963 and 1964, as well as those transferred last July.

Chairman PROXMIRE. What is the status of the inventories?

Mr. ABERSFELLER. We have a continuous inventory system. We use a statistical sampling method of taking inventory, which breaks the merchandise in the warehouse into smaller lots, and we inventory on a continuing basis.

Chairman PROXMIRE. Does this mean a 100-percent physical inventory during a period of a specific time, or does it mean that you sample a certain amount, and how big a sample do you take?

Mr. ABERSFELLER. We sample the lots, Mr. Chairman. And if the sample lot is within tolerance, and we are looking for 95-percent accuracy level—if it is within that tolerance, we take no further inventory. If it is outside that tolerance, for that particular lot, there is a total physical inventory.

Chairman PROXMIRE. If your sample shows a 5-percent error or less, you don't take an inventory?

Mr. ABERSFELLER. That is correct.

Chairman PROXMIRE. How did you arrive at this kind of standard? Isn't this pretty free and easy?

Mr. ABERSFELLER. No, sir. That is based on military standard 105, which is a regular recognized statistical sampling method of application for inventories or other things.

Chairman PROXMIRE. OK. Go ahead.

Mr. KNOTT. We are now negotiating with DOD for the transfer of general mobilization reserve inventories and their management for these classes.

This has been under discussion for a long time, and has not been concluded.

Current plans are for DSA to assume Government-wide support on electronic items on July 1, 1968. The object here is to point out this works both ways. It is not all flowing to GSA, and where the Defense Supply Agency is in a better position to handle an item or is the predominate interest agency, we are working toward their taking over the full responsibility.

Initiation of DSA support of civilian requirements for fuel will begin July 1, 1968, and full implementation will be phased to extend over a 16-month period. Here, we were the small procurers of fuel, whereas the Department of Defense is the large procurer.

Joint efforts of representatives of DOD, VA, PHS, and GSA resulted in increasing uniform specifications for hospital feeding items from 300 last year to 500.

In our testimony last May, we reported that DSA only assumed supply support to selected agencies for certain common use medical and subsistence items because of the lack of commonality of items in these groups stocked by GSA and utilized by civilian agencies.

Chairman PROXMIRE. Why not all of them?

Mr. KNOTT. Well, the principal problem is the lack of commonality, and the problem of DSA taking on items which they do not feel they can afford to get into and handle without detriment to their primary mission, which is military supply support.

Chairman PROXMIRE. How many items are there here? What agencies are there?

Mr. ABERSFELLER. I don't know, Mr. Chairman. We will provide them for the record.

The following subsequently was supplied for the record:

In connection with DOD consideration for DSA support of civilian agencies on medical and non-perishable subsistence items, we understand that 10,800 medical items are centrally managed in DOD by DSA and 3,437 are centrally managed by civilian agencies. Regarding non-perishable subsistence, DSA manages 570 items and the civilian agencies 631.

Chairman PROXMIRE. Do you know what agencies are involved?

Mr. ABERSFELLER. Yes; in the medical and food field, primarily Public Health Service and the Veterans' Administration. There are some other small ones—Federal Prisons is an example. But, the major civilian agency users of medical and subsistence is Public Health Service and the Veterans' Administration.

Chairman PROXMIRE. Proceed.

Mr. KNOTT. As a result, and in an effort to accelerate assumption of these classes of material into the national supply system, we have proposed to officials of the VA that that agency assume civil agency-wide procurement responsibility and that GSA assume the storage and distribution responsibilities for these commodities. The response we have just received from the VA objects to our proposal and suggests as an alternative that the VA be assigned responsibility for both procurement and distribution of medical and subsistence items for the civilian agencies. We will continue to work with officials of the VA to develop an integrated system for implementation by July 1, 1968.

We just received this response yesterday, and, therefore, we have not had an opportunity to discuss with them in more detail the reasons why we feel GSA ought to take on the supply and distribution responsibilities.

Senator PERCY. If they continue to object, who will make a final decision on it?

Mr. KNOTT. The Bureau of the Budget will have to make that judgment in the final analysis and it has been very helpful in the resolution of other controversies of this sort.

BUY AMERICAN ACT

We have recently furnished the Bureau of the Budget procurement and contracting information relating to domestic and foreign procurement for fiscal years 1966, 1967, as well as projections for fiscal year 1968, to assist them in their study regarding the establishment of uniform differentials to be applied to both DOD and civilian agencies.

The information furnished BOB included an analysis of the balance-of-payment savings and budgetary costs of the differential applied by civilian agencies compared to the alternative differential currently applicable to the Department of Defense.

Chairman PROXMIRE. We are very interested in this. Congressman Curtis is especially interested in the great discrepancy of the 50 percent for the Defense Department and 6 percent in much of the rest of the Government.

What does this show in terms of the balance-of-payments saving and other budgetary cost?

Mr. ABERSFELLER. We formed no conclusions, Mr. Chairman, and we simply reflected to the Bureau of the Budget, as an example, that the amount of foreign procurement has increased from fiscal year 1966 to 1967 by 65 percent.

Chairman PROXMIRE. The amount of what?

Mr. ABERSFELLER. Of procurement from foreign sources.

Chairman PROXMIRE. Has increased?

Mr. ABERSFELLER. Yes; has increased.

Chairman PROXMIRE. Despite the Buy American Act.

Mr. ABERSFELLER. With the application of the 6 percent—or 12 percent in the case of a small business or labor-distressed area—it has increased.

Chairman PROXMIRE. You show, then, that as far as the developments at present, there seems to be a decreased budgetary cost inasmuch as we are procuring more from abroad, but an adverse effect on the balance of payments inasmuch as we are procuring more from abroad; is that right?

Mr. ABERSFELLER. Yes, sir.

Chairman PROXMIRE. Does buying from foreign sources complicate procurement? It does decrease costs, I presume.

Mr. ABERSFELLER. Yes, sir.

Chairman PROXMIRE. Does it complicate it in any way?

Mr. ABERSFELLER. Not particularly complicate; no, Mr. Chairman.

Chairman PROXMIRE. What was the volume of foreign procurements by GSA last year?

Mr. ABERSFELLER. \$8 million.

Chairman PROXMIRE. \$8 million out of how much procurement?

Mr. ABERSFELLER. Out of approximately \$900 million.

Chairman PROXMIRE. So it is about 2 percent.

Mr. ABERSFELLER. Actually, in relation to the total contracts we award, it is something less than 1 percent. The \$900 million, Mr. Chairman, deals with the GSA moneys expended. In addition to that, we contract for about \$1,100 million more which other agencies order direct.

Chairman PROXMIRE. Supposing we do not have a Buy American Act. Can you give us any notion as to how much this would increase foreign procurement, and decrease budget costs?

Mr. ABERSFELLER. No, sir.

Chairman PROXMIRE. You do not have any statistics on that? Don't you think that would be helpful for Congress formulating policy in this area?

Mr. ABERSFELLER. Yes, sir; I think it would be. It can be prepared.

Chairman PROXMIRE. Would it be possible for you to compute this.

Mr. ABERSFELLER. Yes, sir; it would not be difficult.

Chairman PROXMIRE. That would be most helpful to us, if you could do that in the future.

Mr. KNOTT. You know, of course, that we have fully supported the objectives of this committee in bringing about uniformity of differentials under the Buy American Act. And the report we made to the Bureau of the Budget is in line with the effort we have consistently made in the period of the last year and a half. We provide them with whatever information we develop in the course of our own experience, which points up the need for uniformity.

Chairman PROXMIRE. This particular committee then, could be especially useful to the Congress in making recommendations on Buy American, inasmuch as we make intensive studies of the balance of payments, we have some members of the committee with great expertise in this area. And, of course, this subcommittee is very concerned in keeping our costs down. These are the two conflicting elements involved here. And, the more information we can develop on this, the more useful our recommendations can be.

One other specific matter of information. Does this include kits that have foreign items in them—this procurement?

Mr. ABERSFELLER. From foreign sources?

Chairman PROXMIRE. Yes.

Mr. ABERSFELLER. It would, if the value of the foreign components of the kits represented the predominant cost of the kit.

Chairman PROXMIRE. You think 1 percent is a pretty fair estimate—of what our foreign procurement is?

Mr. ABERSFELLER. It would be less than 1 percent overall. Actually eight-tenths of 1 percent, Mr. Chairman, overall—of the value of the contracts that GSA contracts for.

Chairman PROXMIRE. Very good. Proceed.

AUTOMATIC DATA PROCESSING PROGRAM

Mr. KNOTT. Next, Mr. Chairman, to the field of automatic data processing.

Since May we have completed the initial round of testing under interim Federal specification W-T-0051a for 800 b.p.i. (bits per inch) tape. As a result four products have now been qualified and Federal supply schedule contracts have been negotiated covering individual purchases under a maximum order limitation of \$25,000. A regulation is now being prepared which will require agencies to submit consolidated computer tape requirements—in excess of the \$25,000 schedule maximum order limitation—to GSA for procurement on a competitive basis. This should be cleared and issued by January 31, 1968.

The new specification and purchase procedures will result in substantial reduction of tape costs. The new specification, for example, permits a maximum of less than one error per reel and by holding to this error rate, additional substantial savings in machine time will be realized.

The ADP resources utilization program continues to be emphasized and expanded. In addition to the 18 ADP sharing exchanges now in operation, four are planned to be operational by the end of fiscal year 1968. These will be located in geographical areas where computer density warrants and now are planned for Anchorage, Baltimore, Cleveland, and Louisville.

Chairman PROXMIRE. That is an amusing sentence.

You mean there is a terrific computer density in Anchorage?

Mr. KNOTT. That is right.

Chairman PROXMIRE. It certainly has nothing to do with the population. It must, of course, have to do with the Defense Establishment.

Mr. KNOTT. Yes, sir.

Chairman PROXMIRE. That startles me.

Mr. KNOTT. In fiscal year 1967, ADP sharing under the program resulted in an estimated cost avoidance of \$28 million, an increase of some \$2 million over the previous year.

Government-owned ADP equipment declared excess to the needs of owning agencies having an acquisition cost of \$80 million was reutilized in fiscal year 1967 by Federal agencies, or donated to State agencies for educational purposes.

ADPE inventory and planned use information required for the ADP management information system has been received by GSA from designated Government agencies in accordance with Bureau of the Budget direction of April 20, 1967, in their Circular A-83, and it is now being assembled, edited, and processed. We expect to issue the printed inventory and 35 related management reports during the third quarter of fiscal year 1968.

Chairman PROXMIRE. Do you have adequate funds and facilities to conduct this program to the optimum?

Mr. KNOTT. Yes; we think we have enough, certainly, to get it moving.

This is a program that will succeed or fail in large measure depending on the extent to which we are able to sell agencies on the benefits that flow from their cooperative efforts. It is not a heavy cost program.

We would like to get further into buying equipment, and we have the initial installment on a revolving fund this year. We will be buying some equipment that we feel ought to be purchased rather than leased.

But we could not, under the present budgetary situation, purchase all of the equipment where economically we would be justified in buying it.

ROLE OF SMALL PRODUCERS IN SUPPLYING ADPE

Chairman PROXMIRE. I understand that small manufacturers have complained that they often sell a component cheaper than the big companies, but are not able to get the business. We have a witness coming in tomorrow to testify on this. I hope that you will have a man here in the audience so that you can be able to comment on his testimony.

Mr. KNOTT. Yes, sir; we will.

Chairman PROXMIRE. Are you aware of this complaint and this problem from the small manufacturers?

Mr. ABERSFELLER. No, sir.

Chairman PROXMIRE. You have not been made aware of it.

Maybe we can perform that service tomorrow.

I have an article here from the Wall Street Journal which says:

Honeywell says U.S. will ease computers. Honeywell said it has been notified in a letter of intent by U.S. Defense Supply Agency of its plan to lease 22 Honey-

well computers valued at \$8.6 million. The computers will process data on Defense Department contracts. They will be used to report on the status of vendor production, quality assurance, invoice control, accounting services and other functions necessary for production and timely delivery of Defense items. The multicomputer system will lease for about \$172,000 a month when the system is fully implemented, Honeywell said. The Government has the option to purchase the equipment at any time.

Do you know if these are for a pooling arrangement?

Mr. ABERSFELLER. I do not.

Chairman PROXMIRE. Does GSA have any part in these DSA transactions?

Mr. ABERSFELLER. Well, we are generally informed. I happen to be uninformed about that particular one. But, we are generally informed of the intent to procure. First the intent to buy or to lease—that notice comes to us first. And then, subsequently, any decision that might be made comes to us. I am not familiar with the case you mentioned, but I do not think it would be pooled within the general Government framework.

Chairman PROXMIRE. This looks like a big and important element, sufficient to warrant a story in the Wall Street Journal, and it is a lot of money.

Mr. ABERSFELLER. I just do not happen to be personally informed, Mr. Chairman. I would like to check with my staff and provide the details for the record.

(The following information was supplied for the record:)

The General Services Administration is responsible for contracting for the Defense Supply Agency requirements for the purchase and/or rental of 22 Honeywell Computer Model 200 Series Systems. On September 15, 1967, the Defense Supply Agency requested GSA to contract for these systems. Representatives of GSA have been meeting with Honeywell, Incorporated, in order to consummate contractual agreement. We expect to complete this by January 15, 1968.

The computers are required by the Defense Supply Agency for use in status of vendor production, quality assurance, invoice control, accounting services, and other functions related to the production and timely delivery of defense items. The multi-computer system will be located and installed during Calendar Year 1968 at various DSA installations located in Detroit, Boston, Chicago, Cleveland, St. Louis, Los Angeles, San Francisco, New York, Philadelphia, Atlanta, and Dallas.

Chairman PROXMIRE. You are confident that GSA has been informed?

Mr. ABERSFELLER. I am not; no.

Chairman PROXMIRE. Are there occasions when they do not inform you?

Mr. ABERSFELLER. Yes, sir.

Chairman PROXMIRE. How can that be? Shouldn't there be intercommunication if you are going to have an efficient operation?

Mr. ABERSFELLER. Yes, sir; it should be. And we have very recently issued a Federal property management regulation on this point, requiring that agencies do this. Until we had done that, there were occasions when we had not been informed.

Chairman PROXMIRE. I would like to ask if it is permissible, Mr. Knott—because you have, as you say, a lot of ground to cover, and Senator Percy and I will be asking you questions on it—if you would mind if Senator Brooke, who has now appeared, could come in and testify, and then we will resume your testimony?

Mr. KNOTT. All right, sir.

Chairman PROXMIRE. Senator Brooke, we are delighted to have you this morning, and welcome you to the committee.

**STATEMENT OF HON. EDWARD W. BROOKE, A U.S. SENATOR FROM
THE STATE OF MASSACHUSETTS**

Senator BROOKE. Thank you, Mr. Chairman, for your courtesy.

Mr. Chairman, Senator Percy, I am appearing today to testify with respect to the serious situation which presently confronts the handtool industry of the United States. This subject received consideration by the Subcommittee on Federal Procurement and Regulation of the Joint Economic Committee during hearings conducted in 1966. It is now vital that the hitherto ignored recommendation of that subcommittee relative to price differentials applicable to handtool purchases by the Government be implemented without further delay.

As you are aware, the purchase of handtools for use by agencies of the U.S. Government is conducted by the General Services Administration, despite the fact that more than 90 percent of such purchases are used by the Department of Defense. Both GSA and the Department of Defense are governed by the provisions of the United States Code, title 41, sections 10a through 10d—the so-called Buy American Act.

GSA is bound in addition by the terms of Executive Order 10582, issued in 1954, which clarifies the vague "reasonable cost" criterion of the Buy American Act by authorizing a price differential of 6 percent in favor of domestic manufacturers (12 percent if small business is involved). However, the Department of Defense has departed from the guidelines set forth in Executive Order 10582, apparently on the theory that such action is necessary to prevent further inroads upon a favorable balance of payments, and has established a 50-percent price differential for its own purchases.

Purchase of handtools by GSA rather than by the Department of Defense has had an extremely negative effect upon the domestic industry. The difference between the 6-percent price differential applied by GSA and the 50-percent price differential applied by the Department of Defense is the crucial factor. Domestic handtool manufacturers who would clearly be able to bid successfully on the basis of the Department of Defense differential find that they are increasingly being underbid by foreign manufacturers as a result of the application of the inadequate GSA differential.

Thus, the awarding of contracts has been, to a large extent, influenced by an administrative decision that the purchase of handtools be the function of GSA rather than the Department of Defense. The negative effects upon domestic industry of this decision are all the more intolerable in light of the fact that the overwhelming percentage of handtool purchases are used by the Department of Defense; yet they are not subject to Department of Defense purchasing procedures.

The effect upon the U.S. handtool industry is inevitable. In 1948, the value of all mechanics hand service tools imported into the United States was approximately \$169,000. But by 1966 the value had increased to approximately \$14 million. And figures for the first 5

months of 1967 reveal that this year's imports are running 13.1 percent ahead of those of last year.

Chairman PROXMIRE. Do you have any statistics, Senator Brooke, on what this represents to the industry—this \$14 million figure?

Senator BROOKE. No; I do not have that figure, but I can get it for you, and I will supply it to the committee, Mr. Chairman.

These inroads, which are primarily the result of activity by Japanese bidders, could have been avoided to a great extent had the purchasing of handtools been conducted on the basis of Department of Defense rather than GSA standards. The divergence of purchasing standards applied by the Department of Defense and GSA affects the domestic handtool industry in a highly discriminatory fashion. Purchases from foreign manufacturers constitute only 1½ percent of total GSA purchases; but, handtool purchases constitute some 57 percent of the GSA foreign purchase total.

Is that the figure you want?

Chairman PROXMIRE. Let me see.

Well, the 57-percent figure gives the percentage of the GSA foreign purchase total. But, what I wanted was the impact of the \$14 million on the industry as a whole.

Senator BROOKE. That percentage upon the entire industry. All right, fine.

(NOTE. Material which covers the Chairman's question was subsequently received from the Service Tools Institute and appears in app. 9, p. 550.)

Obviously the application of GSA purchasing procedures has resulted in severe dislocation within the American handtool industry.

The Bureau of the Budget has the authority to order a change in the application of price differentials to end discrimination against the domestic handtool industry. However, the Bureau has temporized on the subject. Upon being asked by the Federal Procurement and Regulation Subcommittee whether it favored continued application of different price differentials, the Bureau replied as follows:

As a temporary measure, the Bureau of the Budget has supported the existing practice among civilian agencies and the Department of Defense. We believe the existing difference between the practices followed by the Department of Defense and the civilian agencies should be eliminated when problems of trade negotiations and balance of payments are less critical. We believe a change at this time would not be advisable but will be pleased to support appropriate actions toward a more uniform policy as soon as these problems are relieved.

The subcommittee observed in its report that this response did not meet the issue, commenting:

To the extent that GSA takes a different course and makes awards to foreign producers, the Department of Defense Balance-of-Payments program is undermined as is any existing trade agreement.

And the subcommittee recommended:

The subcommittee strongly recommends that the Bureau of the Budget take steps to apply uniform differentials under the Buy American Act for the same items regardless of which Federal agency does the buying for the Government.

As the Federal Procurement and Regulation Subcommittee pointed out, the American balance-of-payments problem will be aggravated rather than relieved by purchasing policies which result in the capture of increasingly large segments of a given industry by foreign manu-

facturers. It is especially true in the case of purchases used primarily by the military that we have an interest in maintaining productive capacity with respect to sources which could be disrupted during an emergency. I am aware of and sympathetic to the Bureau's desire not to take actions which could have an adverse effect upon present attempts to conclude international trade agreements. My request does not represent a desire to defeat the progress and principles of the Kennedy Round. Rather, it is based upon a recognition that the domestic handtool industry has been prejudiced not by an attempt to secure freedom of international trade, but by what is in effect an arbitrary decision to apply one set of Government purchasing standards rather than another.

I believe that alteration of the present policy is especially necessary insofar as the domestic handtool industry is concerned, since this industry suffers to such an extent from present administration of Federal purchasing practices. It would, of course, be cumbersome and impractical to attempt to amend the Buy American Act for the purpose of relieving a particular industry. But, it would be entirely valid for the Bureau of the Budget to recognize the problem which has been created, and to alter the price differential applicable to such industry by administrative order. I have asked the Bureau to take such action in a letter dated November 16, 1967, addressed to the Bureau's Director, the Honorable Charles L. Schultze. I hope that this subcommittee will support this request by an emphatic reiteration of last session's recommendation that uniform price differentials be applied to the same items irrespective of which governmental agency is charged with purchasing responsibility.

Chairman PROXMIRE. Now as I understand it, the difficulty, as you say in the beginning of your statement, is that more than 90 percent of these purchases are used by the Department of Defense.

Senator BROOKE. That is correct.

Chairman PROXMIRE. Yet, the GSA makes the purchase, and applies the 6 and 12 percent differentials, rather than the 50 percent.

Senator BROOKE. That is correct.

Chairman PROXMIRE. That certainly seems to be a very legitimate complaint. One would think, just offhand, that the agency which used the tools would be the one where you would apply the differential.

Mr. Knott, do you have any observations on that?

Mr. KNOTT. It is the procuring agency that applies the rule. And as Senator Brooke has pointed out, the crux of the problem is not which agency does the buying. Unfortunately, there is a difference in the rules being applied by different agencies. It is not the agencies, but it is the rule that causes the problem.

Chairman PROXMIRE. You mean you feel the problem is that you have this discrepancy between what the Defense Department applies, the 50 percent—

Mr. KNOTT. Exactly.

Chairman PROXMIRE (continuing). And the 6 percent applies elsewhere. You should either compromise, take one or the other—

Mr. KNOTT. We have raised this very point with the Bureau of the Budget. If we are buying for Defense, why can't we use the Defense formula?

Chairman PROXMIRE. Senator Brooke raises the point that it is going to be extremely hard to introduce and get legislation passed to apply to the handtool industry. On the other hand, the administration has provided a 50-percent differential as part of our balance-of-payments approach. And, they could just as easily, it would seem to me, provide that in view of the fact that the Defense Department uses 90 percent of these tools, they should be the agency that is recognized as the procurement agency.

Mr. KNOTT. I have no quarrel with that. I have no quarrel with his recommendation. I think his recommendation is fine. And, in fact, to do otherwise is to do just to the contrary to what you read in the preamble to the Federal Property and Administrative Services Act—the declaration of policy there was to establish for the Government an efficient and economical system for centralized procurement. And yet this nonuniform differential tends to dissipate that problem. If you followed the principle that has been suggested here—for the Defense Department to buy its own requirements when it uses 50 percent—then you get back to a system whereby each agency is in the business of buying for itself, and the whole idea of the national supply system, which I have described earlier this morning, where we have turned over to Defense the procurement of fuel and electronics and other commodities which we think they are best able to buy—and they have turned over to us the things that they think we are best able to buy—this would all go down the drain.

Chairman PROXMIRE. Has there been any rationale in principle for this discrepancy; for having the Defense Department apply the 50 percent? We all know that Secretary McNamara is enormously respected and very influential. And, I take it, this was an order of his that was first applied.

Mr. KNOTT. Yes.

Chairman PROXMIRE. Why is it that there is this difference? Is there any justification that you know of—why the Defense Department should have a 50-percent differential, and the rest have so much less?

Mr. KNOTT. No. I can only speculate to this extent. It goes back several years, and much of the implementation of the national supply system that has brought about these changes, whereby GSA, for example, does do all the procuring of handtools, does do all the procuring of paint—these have taken place since that time.

His rule was in effect at that time; ours, the 6-percent rule, was also in effect. The Bureau of the Budget felt that we should not change during the period that the Kennedy round discussions were underway.

Chairman PROXMIRE. I see. So, it is possible now that the Kennedy round discussions are over, that you could have a resolution of this with the 50 percent applying across the board.

Senator BROOKE. By an administrative order.

Mr. KNOTT. Yes; and we have urged that this be done.

Chairman PROXMIRE. And what would this mean in terms of the purchasing? The Defense Department buys what proportion of total procurement?

Mr. KNOTT. Our percentage is relatively small, because we are dealing only in the common-use items.

Chairman PROXMIRE. Would they buy 75, 80, 90 percent?

Mr. ABERSFELLER. Yes; in that range, Mr. Chairman, out of the \$49 billion in the budget for supplies and equipment—

Chairman PROXMIRE. So in terms of increased costs, the difference would not be very great. It would mean that you would eliminate these discriminations that we now have against the handtool industry, and I imagine there may be some other industries that are adversely affected, too.

Mr. KNOTT. There are some others. I think this is one of the more conspicuous ones.

Chairman PROXMIRE. You see, this committee feels guilty on this to some extent, because in the past it has asked that handtool purchasing be transferred to the GSA, which could do a better job, and the industry agreed that this would be the best way to handle it. But since then, the differential developed.

Mr. KNOTT. This is true.

Chairman PROXMIRE. And a great disadvantage to the handtool industry.

Mr. KNOTT. Senator Percy's distinguished predecessor was one of those who consistently urged this transfer.

Senator PERCY. Are they for the most part standard stock items, that are purchased from the commercial market and used by Defense?

Mr. KNOTT. Yes.

Senator PERCY. It seems to me I recall the Senator traveling around Illinois some years ago, with a big bag of parts, taking out a screwdriver, and saying the Defense Department paid \$3.50 for it, and he could buy it at the local hardware store for 19 cents. I wonder if Senator Douglas wasn't one of the powers instrumental in transferring this to GSA so that it would not have to be put through the whole labor of the specialized procurement of Defense, but rather have GSA just negotiate open bids on commercial items and have them available. I think that is probably the rationale that was used. The logic originally was perfectly sound for the transfer.

Chairman PROXMIRE. And the industry strongly supported the transfer.

Senator BROOKE. Yes; and I do not think the industry objects, except for this differential, which is being applied now. Obviously, they are being very seriously injured by it.

Chairman PROXMIRE. Well, Mr. Knott, you say you concur in the Brooke recommendations.

Mr. KNOTT. Yes, sir.

Chairman PROXMIRE. You would recommend that to the Budget Bureau. Would the Budget Bureau be the proper agency for this committee to direct over—

Mr. KNOTT. Yes; that is right. And I believe your committee did that last year, after the Deputy Director of the Bureau of the Budget appeared here.

Chairman PROXMIRE. He is going to appear tomorrow. We will take it up with him tomorrow.

Senator BROOKE. And, of course, I further ask, Mr. Chairman, that this committee reiterate its stand of its last meeting.

Chairman PROXMIRE. You have made a very strong case, Senator Brooke. We will certainly take it up with the Budget Bureau tomorrow,

and do our very best to try and eliminate what is obviously an unintended discrimination against handtools.

Senator BROOKE. Thank you very much, Mr. Chairman.

**STATEMENT OF HON. LAWSON B. KNOTT, JR., ADMINISTRATOR,
GENERAL SERVICES ADMINISTRATION—Resumed**

Senator PERCY. Mr. Chairman, before we go on to public utilities, could I ask one question about computer systems.

Computer systems for any agency or company are almost a status symbol. Everyone has to have his own, and they all like to have the system under their own control. How much authority do you have when a Government agency puts in a request for a system, to scour around to see whether a modified or up-dated system some place else would not serve their purpose, and direct them to use such service, and get it transferred to them or made available to them, rather than them having their own system installed and put in, which might be utilized only a smaller percentage of the time against maximizing 7 days a week, 24-hour-a-day utilization of a system that exists some place else?

Mr. KNOTT. Yes.

This was the whole thrust of some legislation that was enacted a couple of years ago.

The unfortunate thing is that in the course of a last minute compromise, the act ostensibly gave GSA some broad authority for management of computer systems, it dropped its voice, so to speak, in a later section when it reserved to the agencies the final authority for determination as to the type and kind of equipment that it needed to carry on its program mission.

In other words, GSA, as a service agency, is always in the position that it must stand aside when whatever it attempts to perform in the way of a service function can be said to interfere with the mission of the other agency involved.

However, despite this fact, there are ways in which we can approach the problem.

For example, the Comptroller General—within the last 10 days or 2 weeks—has made it eminently clear in a rather lengthy opinion that he believes that GSA's authority for the purchase of—the acquisition of—ADP equipment supersedes the authorities of other agencies, and that they must clear purchases with us. I believe that is the substance of the opinion. (See app. 10, p. 556.)

We believe this reaches a new plateau in GSA assumption of a greater role of management of ADPE.

The ADP sharing exchanges, as I pointed out earlier, have been largely voluntary, but with some pretty good salesmen scattered around the country, this has been a fairly successful effort.

Now, one other device—

Chairman PROXMIRE. I am going to have to interrupt you. You might make a note so you can return to it. Senator Percy and I have to go down and vote again. We will be back in a very few minutes. We apologize.

(At this point in the hearing a short recess was taken.)

Chairman PROXMIRE. Senator Percy is not back. But, why don't you go ahead with your answer to his question—if you can recall.

Mr. KNOTT. All right, sir.

The only additional point I was going to make is this. I had just stated we had been able to accomplish a great deal, by people strategically located, dealing with agencies that had need for equipment, and we had been able to get agencies to cooperate. NASA for example, has, in one recent instance, actually canceled a procurement because we were able to show them where they could get the equipment that was already available through another agency. This type of cooperation is going on.

Another example is that the Federal Communications Commission has entered into an 18-month agreement that will save over half a million dollars for the Navy by providing services to the Navy on FCC equipment, in lieu of new procurement or leasing by the Navy.

These are simply two of a number of examples that could be cited.

The final point I was going to make about indirect means of control is that many of the public buildings that were authorized several years ago, particularly in the larger cities, have reached the point where we are laying out space in them for occupancy. One of the controls that we can properly and do exercise is not only the amount of space that agency is going to occupy per person, but, for example, control over the printing and duplicating shops. We simply will not allow the duplicate assignment of space for printing and duplication plants. In a similar manner, we simply will not allow agencies to have, on different floors in the same building, several different computer operations. We insist that if they will not share, or cannot share the same computers, that they be placed side by side, looking forward to the day when the walls that may exist between them now can come down—because the installation costs themselves are rather extensive.

These are then, indirect controls that we can exercise through our assignment responsibility on space that does give us a control over the utilization.

Chairman PROXMIRE. Now, would you favor repealing that last paragraph or last part of the last which gives the agency the final word on whether or not they can hold on to their own computer?

Mr. KNOTT. Certainly, Mr. Chairman, I believe that it could be stronger than it is now. Perhaps not repeal it, but certainly—

Chairman PROXMIRE. Just that last part.

Mr. KNOTT. We should place the burden on the agency to make a case, which it does not have to do now. The agencies now make determinations to share equipment or to obtain other equipment where sharing will interfere with their program mission.

Chairman PROXMIRE. In your view, this could save some of the \$3 billion annually we spend on computers?

Mr. KNOTT. Yes; I think this would be simply another step along the way toward strengthening the hand of the agency that has been vested with the authority and responsibility to move in this direction.

Chairman PROXMIRE. Would you suggest to us the wording of such an amendment?

Mr. KNOTT. We would be happy to. (See letter below.)

Chairman PROXMIRE. Fine. I think that would be very helpful. We will take it up with the committee and very possibly put it in.

GENERAL SERVICES ADMINISTRATION,
Washington, D.C., December 6, 1967.

HON. WILLIAM PROXMIRE,
Chairman, Joint Economic Committee,
Congress of the United States,
Washington, D.C.

DEAR MR. CHAIRMAN: You will recall that during the course of my testimony before your subcommittee on November 29 you asked, in effect, whether we regarded the authority vested in General Services Administration with respect to ADP by the so-called Brooks bill (P.L. 89-306) as adequate to enable us effectively to discharge our general responsibilities under the bill.

In response I indicated that the limitations on our authority contained in the last provision of the bill (Section 111(g) of the Federal Property and Administrative Services Act of 1949, as amended) detracted from what otherwise would have been a clearer mandate vested by preceding provisions, namely Section 111 (a) and (b).

However, in response to your further question as to whether I would favor repeal of the Section 111(g) limitations on GSA's authority, I indicated preference for amendment of the limiting provisions so as to clarify the respective roles of GSA and the agencies using ADPE with respect to determination of requirements for and selection of equipment on the one hand and the actual procurement of such equipment on the other hand, and so as to more explicitly place the burden of proof on using agencies in any instances where they object to proposed determinations by GSA "specifically affecting them or the automatic data processing equipment or components used by them".

You will recall, also, my testimony to the effect that, generally speaking, we were receiving good cooperation from using agencies in the general field of automatic data processing as a result of which substantial progress had been made in implementing the Brooks bill and significant savings have been realized. This has been made possible, despite the statutory limitations, through consultation and cooperation with other agencies, persuasion, and through indirect controls available to us, such as limiting the amount and location of space we will assign in public buildings for ADPE installations.

I pointed out, also, that a very recent decision by the Comptroller General of the United States (B-151204/B-157587 dated November 21, 1967) holding, in effect, that the Brooks bill vested in GSA exclusive authority to procure all general-purpose ADPE and related supplies and equipment for use by other Federal agencies will importantly strengthen our effectiveness. (NOTE. See p. 556.)

During my testimony, in response to your request, I agreed to prepare and submit to the subcommittee amendatory legislation along the lines indicated above.

Upon further reflection, however, I have concluded that, all factors considered, amendatory legislation at this time would be inadvisable. The overall ADP management improvement task is stupendous and, as recognized during the legislative process on the Brooks bill, must be brought about on a progressive basis.

Regardless of the precise wording of the statute, our success, as the agency charged with central responsibility, will be impacted to a major extent by the degree of cooperation we are successful in generating on the part of the using agencies. In view of the cooperation currently being received from using agencies, the magnitude of the task, accomplishments to date under the existing law, the fact that the law is relatively new and unproven, and the recent Comptroller General's decision, I believe it would be the better part of wisdom to defer any effort to amend the present law to allow us more time to evaluate our potential for its full implementation as presently worded. We will be prepared to report further in this regard to your subcommittee during hearings next year and to make recommendations at that time concerning the need for amendment of the law in the light of experience gained by that date.

Sincerely yours,

LAWSON B. KNOTT, Jr., Administrator.

PUBLIC UTILITIES

Mr. KNOTT. On the subject of public utilities, which was of some interest to the subcommittee last May, and you asked that we report on it again—your report of July 1967, concluded that it is important to economy in Government that GSA have the capability and motivation to carry out its responsibility to protect the Government as a user of utility services. We are in full agreement with that conclusion and our policies and our operation are in accord with it.

Our responsibility under title II of the Federal Property Act is to protect the Government as a user of utility services. Our role is not that of a "people's counsel," representing all rate payers, nor are we assigned responsibility for regulating the overall earnings of public utilities. The task of protecting the Government as a user is our sole statutory concern.

Also, Mr. Chairman, our first effort in protecting the Government as a user of utility services is through our utility management and negotiation activity and, as the subcommittee report puts it, "if necessary, to represent or have the Government represented in rate cases * * *."

If necessary to protect the Government's interest, we will and do initiate or intervene in such proceedings; we represent the Government through our own staff or jointly with other agencies; or we arrange to have the Government represented by delegation of our representation authority to other agencies. We are firmly convinced, however, that management and negotiation efforts should first be exhausted before resorting to litigation.

In the course of the hearings last spring, I advised the subcommittee that our savings for the period fiscal year 1960 through May 15, 1967, were \$11.5 million.

Chairman PROXMIRE. How did you calculate that?

Mr. KNOTT. These were the rates that we were being charged at the time, or the rates that were proposed, and which, through our negotiation, we were able to reduce.

Since that report to you, our effort has produced additional recurring annual savings of some \$481,000, and nonrecurring savings of \$1,322,389, of which \$1.2 million was a refund from the American Telephone & Telegraph Co., resulting from a coordinated effort on the part of our Office of General Counsel and the Office of the Judge Advocate General, Department of the Air Force. This coordinated effort exemplified both our policy of negotiation and our utilization of the total Government staff available without regard to department or agency in the effective protection of the Government's interest as a user of utility services.

We have in the past and will continue to discharge our responsibility in the utility rate area in close cooperation with other agencies, particularly major users such as the Department of Defense, National Aeronautics and Space Agency, and the Atomic Energy Commission.

The subcommittee report also recommended that the BOB investigate the adequacy of GSA's capability and efforts on behalf of the Government as a user of utilities. We have had several informal discussions of this matter with the Bureau and we have advised it of our belief that additions to our utility management staff at the regional

level would be productive of beneficial results. We will continue to explore this matter with the Bureau.

Chairman PROXMIRE. In what way?

Mr. KNOTT. It simply puts people out on the frontline—our staff has been principally a staff located here in Washington. It would give us broader representation, particularly in some regions where we have a larger demand for utilities—for example the west coast, Chicago, and some of the larger regional areas, where there are a number of these transactions going on all the time. It will give us a greater opportunity to get the information at an early date, and get into negotiations at an early date, rather than sometimes rather tardily.

SAVINGS ON TELECOMMUNICATIONS

Chairman PROXMIRE. In your telecommunications network, have you computed how much you save per word, or minute, or other unit of usage?

Mr. KNOTT. Well, our rate now on long-distance telephone calls is down to 73 cents—the average call.

Chairman PROXMIRE. Does that mean our bill has been going down—or have the words increased so much?

Mr. KNOTT. Well, I don't think there are any fewer calls, Senator.

Chairman PROXMIRE. I am sure there are many more. I am just wondering if this works out to a reduction in overall cost, because your rates have been going down, but the number of calls have been increasing. What is the net effect?

Mr. KNOTT. The system now extends to some 435 cities.

The pro rata use of the system is distributed to the agencies.

This means, while we occasionally have to add additional lines, and in that way—

Chairman PROXMIRE. My question is whether or not you have made any computations as to the overall cost now of communications. Whether it has been diminishing or increasing. Do you know?

Mr. KNOTT. Our bill, I think, runs \$32 million a year. Do you have the figures on that, Mr. Williams?

Mr. WILLIAMS. \$38 million. And the going call rate is about 52 million calls per year.

Chairman PROXMIRE. How does that compare with what it has been over the past 4 or 5 years? Has it been going up?

Mr. WILLIAMS. The call rate is coming down.

Chairman PROXMIRE. Yes, but the bill.

Mr. WILLIAMS. The system cost is going up, but not in direct proportion to the increased call volume. We are making gains on the thing—through increased efficiency of the system. We get higher utilization. The cost per call comes down. But the corresponding increase in systems costs I think is the question that you are asking.

Chairman PROXMIRE. We have to make some assumptions about this, and one is that increased communication is desirable, and necessary, in a growing country, and increasingly complex government. And that while the overall cost is going up, on a per-unit basis it is going down, and you are confident the efficiency is increasing all the time; is that correct?

Mr. WILLIAMS. That is correct. This condition is illustrated by comparing the first 4 months of fiscal year 1967 with the first 4 months of fiscal year 1968. During these comparative periods, the record communications system cost was up \$40,000 or 3 percent from the fiscal year 1967 period and the number of words transmitted was also up 106 million or 71 percent. However, the cost per word was down 37 percent from the fiscal year 1967 period. Similarly, the Intercity Voice Communications System cost was up \$800,000 or 6 percent from the fiscal year 1967 period and the number of calls completed was up 4 million or 30 percent but the cost per call was down 18 percent from the fiscal year 1967 period.

Chairman PROXMIRE. Is there any way at all that we can put reasonable limits on this? It seems to me you open it up in a way that makes it so simple, there might be a lot of unnecessary calls.

As I understand it, now you can make unlimited long-distance calls through GSA without charge to an agency pretty much, can't you—and you make a modest initial payment?

Mr. WILLIAMS. No, sir. The agencies pay for the calls that they make.

Chairman PROXMIRE. On a per-call basis?

Mr. WILLIAMS. Yes, sir.

Chairman PROXMIRE. How do you control it?

Mr. WILLIAMS. The only controls which are possible are through administrative means which the agencies themselves must apply.

Mr. JOHNSON. Mr. Chairman—one of the things that forms a brake here, or a control, is that the total cost of the system is equally prorated among its users by statistical sampling. Therefore, each Government agency must pay for that service.

Now, in the administrative practices within an agency, therefore, they control the amount of usage that they have of the system. Now, we continually argue with them about the price, and the administrative officers around town have various means of controlling the usage of the system, to keep their costs from rising. But the more they use it, the more their costs will go up, in terms of volume of calls they make.

Chairman PROXMIRE. How do you do it? A fellow picks up the phone and calls San Francisco. How do they exercise this control?

Mr. WILLIAMS. What was the question, sir?

Chairman PROXMIRE. What I am thinking about is—we have just gotten into this in my own office. I have a man out in Wisconsin who is on a system where you make a certain payment, and then you can call any place in the country. Senators can get on that, too, now.

Mr. KNOTT. Seventy-five Senators receive FTS service from GSA.

Chairman PROXMIRE. And, I take it that you can put people through-out the Government on this kind of thing?

Mr. KNOTT. Yes.

Chairman PROXMIRE. And, my question is how you control excessive use of this, or doesn't it matter how much it is used?

DIFFICULT TO CONTROL USE OF SYSTEM

Mr. KNOTT. I do not think that it is economically feasible to mechanically control use. There are no reasonably priced mechanical con-

trols that can be employed. We explored this thoroughly in the early stages of the system and the cost of mechanical device control or making a ticketed record of calls is more costly than the cost of allowing the mechanically unlimited use. This involves to some extent, of course, a selling campaign to agencies based on the fact that if they overburden the system, and we have to add to the system, then the agencies are going to have to pay. And we try to give cost-cutting tips to agencies on how to limit usage.

Chairman PROXMIRE. Very hard to discipline them, though.

Mr. KNOTT. It is very hard.

Chairman PROXMIRE. If one agency overburdens it, and you have to add to the system, all the agencies share in the additional cost; isn't that right?

Mr. KNOTT. That is true. But you can get to the point with a small regulatory agency where it is not even worthwhile billing them for their share of the use. It is so small in comparison to a large agency.

The Treasury Department is a large user of the system. But, in its Internal Revenue Service primarily—Internal Revenue Service has found that in terms of the payoff, that this has been one of the most tremendous advances that they have made—equal in terms of importance to them to the computer system that they have installed. They have been able to avoid sending a man to see somebody about a delinquent tax account, because they can pick up the phone and call him, talk to him, make an appointment, know that he is there when they go.

The Post Office can arrange by telephone for a whole force that otherwise would come on at a distant point to take over a mail delivery, to delay reporting for 3 hours, when they know mail is going to be delayed for 3 hours.

Chairman PROXMIRE. Can there be conference calls that eliminate the need for travel?

Mr. KNOTT. Agencies vary on this point. I do not think I have used conference calls three times in the time the system has been in use. Civil Service Commission has used it fairly extensively for this purpose. And, it has cut down on travel. Veterans' Administration finds it most helpful in meeting emergency situations in connection with patient care, and so on.

Chairman PROXMIRE. It seems that there is an opportunity here for an agency like yours, which is right in the center of it, to perhaps—if you could do so—to make some inquiries, and then perhaps pass on some of the cost-saving techniques that some agencies have found through using this communications system.

Mr. KNOTT. We have done that. And, we point out to them—

Chairman PROXMIRE. You have done that?

Mr. KNOTT. Yes. In fact, we have considered the possibility that we might even give them a reduced rate—a reduction in their rate if they use the system between 8 and 10 in the morning, and between 4 and 6 in the afternoon, rather than the other hours, which are heavy-load hours. We are constantly exploring inducements that we can offer to them.

Now, of course, if you add to this communications system cost the cost of terminal equipment, we think we have made real substantial savings there. And we started this in GSA: we conducted courses

among the agencies. Nearly a thousand people in Government have received instruction in the things they can do to cut out the costly devices that would otherwise be sold to them when they set up a new office. Buzzers and call directors and that type of thing.

We have saved well over a million dollars per year in terminal equipment.

Chairman PROXMIRE. All right. Go ahead.

COMPETITIVE VERSUS NEGOTIATED PROCUREMENTS, TRUTH IN NEGOTIATIONS ACT

Mr. KNOTT. To get to the competitive versus negotiated procurements Truth in Negotiations Act—although the requirements of the Truth in Negotiations Act of 1962 (Public Law 87-653) are applicable by its terms only to those agencies subject to the Armed Services Procurement Act, GSA, as a matter of procurement policy, has incorporated the provisions of the act in the Federal procurement regulations thereby making the statutory procedures mandatory on all Government agencies in the executive branch.

Chairman PROXMIRE. That is good.

Mr. KNOTT. Both our Federal Supply Service and Public Buildings Service are implementing directly the cost or pricing data provisions of the regulations. As a result of a GAO report of July 1967 which noted some instances where construction contracts entered into after June 1964 did not contain the prescribed defective pricing data clause, the Public Buildings Service issued clarifying instructions to contracting officers for guidance and such contracts will hereafter contain this clause.

In negotiations with architects, for example, where the fee exceeds \$100,000, we get into dollar details and apply the regulation to those negotiations.

GSA HAD 76 PERCENT ADVERTISED SUPPLY PROCUREMENT IN 1967

The regulations emphasize that procurements shall be made by formal advertising whenever such method is feasible or practicable even though the circumstances present would otherwise satisfy the statutory requirements for negotiations. We are firm in continuing this policy. In fiscal year 1967, 76 percent of GSA supply procurement dollars were expended under publicly advertised, competitive bidding procedures. This includes awards made to small business firms under restricted advertising procedures but does not include orders placed by other agencies under term contracts and Federal supply schedule contracts.

Chairman PROXMIRE. How does this compare? Is this more competitive advertised bidding than before?

Mr. KNOTT. It runs about the same. It has not improved a great deal. We have a considerable amount of supplies still under the Federal supply schedules, and those are difficult to handle in that form.

On small business, while we continue to try to emphasize that, mergers have not helped us a great deal on that. There has been

a changing structure of small business, so that your percentage has remained about the same.

Chairman PROXMIRE. Well, I hope you will keep emphasizing this, because, of course, it is one method of procurement which really complies with congressional policy. Your purchases are by and large more amenable to competitive bidding than the Defense Departments—much more. After all, they only have 13 or 14 percent—you have 76 percent—advertised competitive bidding.

Mr. KNOTT. Right.

Chairman PROXMIRE. It is hard to ask you to criticize the Defense Department—but at the same time, is there anything you are doing in your procurement processes which they could do which would enhance and increase their proportion of advertised competitive bidding?

Would you think about that?

Mr. KNOTT. Mr. Abersfeller was with the Quartermaster Corps a good many years and works day in and day out with Defense.

Chairman PROXMIRE. We are after them all the time. Frankly, they are hard put to come up with many constructive proposals in this area.

Mr. ABERSFELLER. Mr. Chairman, I am not privy to all the information incident to the negotiations that Defense makes. But it seems to me in the large procurements that constitute most of their negotiations we would be hard put to do it any other way than they are now doing.

The basic problem is one of the absence of specifications.

Chairman PROXMIRE. How about breaking out some of their component parts?

Mr. ABERSFELLER. This is possible, Mr. Chairman; but one of the real risks that you take is that it might cost more over the long term if you do this, in the sense that you then do not have a single contractor to look to regarding the performance of a given product. This could take the form of Government-furnished material as an example, and you could provide on a separate breakdown for the procurement of components, and provide that to an assembler or a contractor. But one of the real risks you take, then, is the contractor, should there be a deficiency in the end product, would simply point to the fact that you forced him to take these components which you had provided from other sources.

Chairman PROXMIRE. Do you buy handtools by advertising?

Mr. ABERSFELLER. Yes.

Chairman PROXMIRE. And did the Defense Department do this when they had the responsibility?

Mr. ABERSFELLER. Yes; in the same instances. They do, however, I understand, buy some handtools under negotiation where the handtools were provisioned with an end item, radar trailer, for example. They then had the supplier of the radar trailer, for example, provide the handtools.

Chairman PROXMIRE. I hope you will think about this, and if you can, in the course of going over the record in the next few days, come up with whatever you can in the way of suggestions as to what we can do to help the Defense Department get more into the advertised competitive bidding. They admit there is a saving of 25 percent when they can procure on competitive basis.

Mr. ABERSFELLER. Yes, sir.

PROCUREMENT OF INDUSTRIAL PRODUCTS AND SERVICES PURSUANT
TO BOB CIRCULAR A-76 (SEE APP. 13, P. 611)

Mr. KNOTT. Bureau of the Budget Circular A-76, revised, has to do with the question of buying, or relying on private enterprise system to provide the services and products which are needed by the Government. The inventory by GSA of the commercial and industrial type of products and services which could be procured through private sources rather than produced or performed in-house by GSA has recently been completed. Thirteen activities meriting analysis and study were identified in the inventory. Four studies have been completed and the remaining nine studies are scheduled for completion by June 30, 1968.

The four completed studies are—

- (1) Cleaning of public buildings;
- (2) Maintenance and repair of Government-owned buildings;
- (3) Operation of interagency motor pools; and
- (4) Repair of office machines.

Studies of the first two activities justify distribution of the work between Government and commercial contractors based on a cost comparison for each building. The third study indicates that continued operation of interagency motor pools by the Government is more economical than operation of the pools under commercial contracts. The study of the fourth activity—office machine repairs—justifies the continuation of the operation of facilities located in Denver, Colo., and Washington, D.C., by the Government on the basis of cost and local shortages of qualified repair technicians and facilities. In all other geographical areas office machine repairs are being performed by commercial concerns.

Chairman PROXMIRE. You do not use prison labor?

Mr. KNOTT. We have arrangements with the prison industries, yes, sir: for certain products. Do you have some examples?

Mr. ABERSFELLER. Yes; we buy paintbrushes and several items from the prisons—furniture.

Mr. KNOTT. Some of the rehabilitation of furniture is done by them.

On short-shelf-life items—I am pleased that we were able to clear a report on your bill, I believe, just yesterday.

Chairman PROXMIRE. Good. That is mighty welcome.

Mr. KNOTT. The report is with the committee now.

Chairman PROXMIRE. Fine.

(Note: Bill is S. 1717. See also p. 309.)

CONTROL OF SHORT-SHELF-LIFE ITEMS

Mr. KNOTT. We advised you in May that 186 items valued at \$42.5 million were subject to rotation by December 1968. We now understand—

That \$9.9 million of these items have been transferred to other Federal agencies for utilization or will be transferred prior to expiration of shelf life;

An additional \$5.4 million of items have been discontinued as stockpile items and will be declared excess by December 1968; also, \$3.3 million in biologicals and antibiotics have been determined by

the Food and Drug Administration to be unfit for human use and will be destroyed;

The remaining \$23.9 million of shelf items have useful life established through December 1969; reinspection and testing at that time should result in extension of usable shelf life.

Chairman PROXMIRE. This \$3.3 million that were destroyed—how does this compare—is this a better record than you had in the past?

Mr. KNOTT. Yes.

Chairman PROXMIRE. Considerably better?

Mr. KNOTT. Considerably better. I think we had a figure, at one time, that ran as high as \$24 million.

Chairman PROXMIRE. That was the reason I put the bill in.

Did the life of these items expire, or was there some other cause?

Mr. KNOTT. The larger volume, or the improvement?

Chairman PROXMIRE. I am talking about the \$3.3 million, this particular item.

Mr. KNOTT. This particular item. Yes, these simply were determined to be unfit for human use. We have been attempting to redistribute these before the shelf-life time expired. But, we just did not make it on this \$3.3 million.

Public Health Service has reported that excess materials valued at approximately \$10.1 million were utilized by VA and DOD from May 1965 to September 30, 1967.

We also reported to you last May that, with respect to the problem of short-shelf-life items in the civil defense medical stockpile, an inter-agency committee composed of representatives of GSA, DOD, PHS, and VA had developed a plan to assure utilization of stockpile materials prior to expiration of their shelf life. During the final clearance of this plan it developed that existing stockpile facilities were unable to handle the redistribution of small quantities of stock.

As a result we are investigating the feasibility of bringing required stocks into the existing Federal Supply Service distribution system in bulk for subsequent redistribution to the smaller users. Under this plan bulk distribution to large users direct from the stockpile storage points would continue to be made. We expect to have the feasibility of this approach decided by February 1, 1968, and if no further problems develop we expect to implement the plan no later than June 30, 1968.

Until this plan is completely developed and implemented, we will continue to utilize short-shelf-life medical stockpile items under the interim arrangements we discussed in May 1967.

DHEW also advises that the Office of Emergency Planning's Task Force on Emergency Health Preparedness has, to the extent possible, selected all military specification or Federal specification items for inclusion in the current program involving community and packaged disaster hospitals.

This should facilitate greater utilization of expiring shelf-life items in this program in future years. As I indicated in May, this same task force has developed a plan whereunder a 30-day inventory of certain of these items will be located at and rotated by community hospitals. The goal is to distribute 1,800 units consisting of 30-day supplies for 200-bed capacity hospitals over the next 5 years.

Chairman PROXMIRE. Congratulations. I am glad you are making this kind of progress. It is very encouraging.

Senator PERCY. Mr. Chairman, may I interrupt?

I regret I have a 12 o'clock meeting.

May I just simply say—I know this agency is one of the less glamorous ones. The glamor agencies are the ones that spend all the money. It is never headlines when you save money or procure frugally. But my own personal experience in manufacturing over the years, being on the other end of GSA, has shown that their procurement practices have measured up to the highest standards of the highest and most efficient corporations in this country. In fact, sometimes we thought they were too efficient, too tough.

Now that I am at this end, where we have to raise the money, I certainly can appreciate everything that your people do to instill a sense of efficiency, honesty, and decency, and the highest standards of procurement.

I think the Government and certainly as one Senator I am so grateful for the dedication of the men that you have in your service, and for yourself. As a tenant in the Federal Building of Chicago, I can again testify to the efficiency of your operations out there.

Mr. KNOTT. Thank you, Senator. With your background, that is very meaningful.

Senator PERCY. Thank you, sir.

EXCESS PERSONAL PROPERTY

Mr. KNOTT. General Services Administration continues to promote the utilization of all types of excess personal property throughout the Government in lieu of new procurement and in support of the President's cost-reduction program.

During my testimony at the hearing on May 16, 1967, I stated that while the quantity of available excess personal property decreased significantly in 1966 due to the military buildup in Southeast Asia, the quantity of such property transferred for further Federal use remained high at 585,497 line items costing \$617.1 million. I can now report that in 1967 excess personal property transferred to Federal agencies totaled 642,951 line items costing \$643.5 million, an increase of \$26.4 million over 1966. This increase, in utilization in 1967, was accomplished in spite of a 23.3-percent decrease in the amount of excess personal property available as compared to the previous year. In 1967, excess property available for utilization totaled \$2.3 billion, at Government acquisition cost, contrasted with the availability of excess property costing \$3 billion in 1966.

For the first 3 months of fiscal year 1968 the decline in excess personal property generations was reversed slightly, with property costing \$653 million becoming available. Federal transfers for the 3-month period, however, increased significantly, totaling \$199 million at acquisition cost.

The type of excess personal property being generated continues to include an increasing proportion of special technical equipment with limited utilization potential, such as electronic communications equipment, weapons systems material, and instruments and laboratory equipment.

GSA has continued to place special emphasis on the utilization of excess inventory in the possession of Government contractors. In May

1967, we reported that in fiscal year 1966 transfers of contractor inventory totaled \$117.5 million at Government acquisition cost. This reduction from \$140.4 in 1965 was due to the declining volume of property available for transfer. The decline in volume of excess contractor inventory continued into 1967, and transfers for the year were reduced slightly from 1966 to property totaling \$115.9 million. For the first 3 months of 1968 generations of excess contractor inventory continued to decrease. Volume was \$49.6 million of excess generations. Transfers, however, are increasing substantially, totaling property costing \$31.4 million.

Chairman PROXMIRE. How is the cost of contractor inventory known to you?

Mr. KNOTT. This is a reported cost. It is not a cost that we——

Chairman PROXMIRE. It is their estimate?

Mr. KNOTT. It is their estimate; yes.

Chairman PROXMIRE. How does this cost compare to your costs?

Mr. KNOTT. On acquisition costs?

Chairman PROXMIRE. What I am talking about is whether or not you could select a fair sample of these items from four or five of your regions, and compare the costs with your costs and let us know.

Mr. KNOTT. That is an interesting thought. I would like to try that. I do not think we have made any such comparison. But I would like to——

Chairman PROXMIRE. Could you do that for us?

Mr. KNOTT. Yes.

Chairman PROXMIRE. Fine.

(NOTE. Report will be made in 2 or 3 months.)

Mr. KNOTT. Surplus personal property costing \$285.9 million was donated by GSA for education, public health, civil defense, and public airport purposes in 1967, a decrease of \$143.3 million compared to 1966. This significant decline was due to the overall drop in the availability of property coupled with our highly successful effort to effect the reuse of excess personal property by Federal agencies. This trend has continued for the first 3 months of 1968, when donations of surplus personal property totaled \$64.6 million, at Government acquisition cost. During fiscal year 1967, property having an original cost to the Government of \$99.7 million has been reconditioned or repaired. This represents an increase of 10 percent over the previous year. The cost of reconditioning and repairing was \$15.6 million, which is less than 20 percent of the overall original cost. Approximately 95 percent of this work is being accomplished by over 2,000 small business concerns.

Chairman PROXMIRE. How much was the saving to the Government in the utilization of excess personal property last year?

Mr. KNOTT. \$643.5 million.

Chairman PROXMIRE. \$643.5 million. Where did most of the property come from?

Mr. KNOTT. Most of it from Defense.

Chairman PROXMIRE. What would it have brought by sale?

Mr. KNOTT. Our recovery on personal property runs across the board generally around 12 to 18 percent, in that area. That is on personal property.

Chairman PROXMIRE. Twelve to 18 percent of the cost?

Mr. KNOTT. Of the cost; yes.

Chairman PROXMIRE. When you sell it?

Mr. KNOTT. That is right.

Chairman PROXMIRE. Then you really saved how much? Can you make an estimate? So this would reduce—

Mr. KNOTT. About \$547 million.

Chairman PROXMIRE. If the Defense Department embarks upon a greatly expanded exchange-sale program, how much property will be removed from the excess category?

Mr. KNOTT. It is a little bit early to tell, because they have only recently embarked on a tighter program. We have recently issued a new regulation on exchange-sale which has not worked all one way. That is, we have not simply added to the list of items that would be subject to exchange-sale. We have actually taken some of the exchange-sale column and put them over into the donation column.

But, we continue to include, in the exchange-sale area, items such as vehicles and typewriters and that type of thing, which are in frequent use, and continue to be needed, so that they don't become available to the donation program.

I would imagine that it is going to result, however, in cutting down on the donation program. It is hard to estimate how much.

Chairman PROXMIRE. Does this mean that your utilization program will be denied this property through the technicality of definition of excess and exchange-sale?

Mr. KNOTT. I think that is a fair statement; yes, sir.

Chairman PROXMIRE. Do you favor changing the law so utilization will take precedence over exchange-sale?

Mr. KNOTT. I do not think so.

Chairman PROXMIRE. You do not?

Mr. KNOTT. No.

Chairman PROXMIRE. What does it cost GSA to prepare for sale and sell surplus personal property? DOD reports that it takes about 80 percent of the proceeds—79 percent.

Mr. KNOTT. Is that for sale, or is that for their utilization and sale?

Chairman PROXMIRE. For sale—

Mr. KNOTT. Only?

Chairman PROXMIRE. What does it cost GSA to prepare for sale and sell. DOD reports it takes 79 percent of the proceeds to do this.

Mr. KNOTT. I was asking whether their statement covered utilization and sale, or sale only. Certainly our costs for sale do not run 80 percent.

Chairman PROXMIRE. Preparation and sale.

Mr. KNOTT. It runs approximately 30 percent on sales.

Chairman PROXMIRE. Do you recommend that surplus real property not be donated to non-tax-supported donees?

Mr. KNOTT. Not be donated; yes.

Chairman PROXMIRE. Would you apply a kind of Morse formula? You know, Senator Morse has—

Mr. KNOTT. I know it well; yes, sir. Yes; I think that the Government should recover for property that it no longer needs. There are enough exceptions to the law now, specifically providing for discount for public health and education, airports, and other recognized public.

uses. The efforts to expand to other areas is fruitless in that there is simply not that much property to go around.

Chairman PROXMIRE. Well, it sounded as if most of the disposal of property was to nonprofit—as I read your report—was to these nonprofit sources from which there was no return.

Mr. KNOTT. Yes, sir; that is right.

Senator PROXMIRE. How much has there been donated to non-tax-supported donees since your act was passed in 1949? Do you have any figures on that?

Mr. KNOTT. I do not think I have any summaries regarding donations as between tax-supported and non-tax-supported levels.

But, it is a figure that we could compile and furnish. We would like to do it.

(The following was later furnished for the record:)

Donations of Real and Personal Property F.Y. 1958–F.Y. 1967 inclusive.
(Records are not available prior to F.Y. 1958.)

Real property:

Numbered: 1,470

Acquisition cost: \$960,000,000

Personal property:

Acquisition cost: \$3,660,000,000

Records are not available from which to determine donations between “tax-supported” and “non-tax-supported” institutions.

Chairman PROXMIRE. Does that take us up to real property?

EXCESS REAL PROPERTY

Mr. KNOTT. Yes, sir. As I indicated in my last report to the committee, I had hoped that the recently revised Bureau of the Budget Circular A–2 of April 5, 1967, with its new provisions, requiring the holding agencies to make a detailed annual report of their real property to the BOB, would give added impetus to the identification and reporting of excess real property not required to meet program objectives. (Text of Circular A–2 appears in hearings, 1967, pt. 1, p. 234.)

Although the expected increase in the reporting of excess real property has not yet materialized, it is still too early to make a judgment on the effectiveness of the circular. The first reports from the holding agencies to the BOB are only now being submitted under the revised Circular A–2, and the review and critique of those reports by the BOB may serve to further the excess program.

We continue to provide for the further Federal utilization of real property wherever feasible. During fiscal year 1967, 59 excess real properties were transferred to other Federal agencies for continued use. An additional 18 properties have been transferred to other Federal agencies during the period from July 1 to October 31 of this fiscal year.

Exchanges of excess property for other privately owned lands needed by Federal agencies are fostered by GSA in an effort to reduce the amount of appropriated funds needed for new acquisition. Nine such exchanges were accomplished during fiscal year 1967.

Chairman PROXMIRE. What did this amount to in terms of dollars, roughly?

Mr. KNOTT. We would be glad to supply that. Just one quick passing example. We had 115 acres of land near Portland, Oreg.—a Federal Communications field office. That was exchanged for city property adjoining the Federal building, which houses the Bonneville Power Administration in Portland. This was land that was needed, not only for motor pool operations, but for the future expansion of the building. We are trying to use properties where we can effect these exchanges rather than make other dispositions.

(The following information was later furnished for the record:)

Value of nine real property exchanges during fiscal year 1967—\$3.4 million.

We have exchanged properties outside of forest preserves for privately owned properties within the boundaries of the preserves that the Department—the Forest Service—wanted to acquire. This has also been true with respect to lands administered by the Department of the Interior, National Park Service.

We continue to stress the disposal of surplus property by sale in order to—

- (1) Return its full cash value to the Treasury;
- (2) Reduce maintenance costs; and
- (3) Return property to the local tax tolls and to the civilian economy as a source of jobs and payrolls in local communities.

During the fiscal year 1967 GSA sold a total of 406 real properties valued at \$39½ million. Prices obtained from the sale of this surplus real property totaled \$46 million. In the first 4 months of the current fiscal year, sales have totaled \$30.2 million.

The preceding fiscal year disposals totaled \$125 million, for an all-time high. But, our annual sales levels depend on the mix of properties, rather than the number of properties, and the value of the available properties.

A large portion of the surplus property disposed of each year is conveyed at price discounts for public non-Federal uses. Under existing procedures, prior to public sale, State and local governmental agencies and eligible nonprofit organizations are given notice by the GSA of the possible availability of surplus real property for disposal for health, education, park and recreation, historic monument, wildlife conservation, and public airport purposes, without charge or at price discounts, and afforded the opportunity of submitting a plan for the acquisition and use of the property. During the first 4 months of fiscal year 1968, 51 surplus real properties have been conveyed for public uses. Federal investments in these properties amounted to \$79 million.

Under the Land and Water Conservation Fund Act (Public Law 88-587, approved September 3, 1964) a fund was established to assist in providing moneys for the planning, acquisition, and development of lands for park and other outdoor recreation uses, including matching grants-in-aid to States for these purposes. Receipts from surplus real property sales are deposited in and form the bulk of the fund.

Turning to another subject, during fiscal year 1967, in a number of large cities, contracts for the maintenance, repair, and overhaul of electric typewriters and certain other office machines were awarded to local companies. Previously, only services by manufacturers had been made available by GSA for Government-wide use. The results of this shift in contractual base have demonstrated sufficient savings to

warrant use of local contractors in other geographic areas, and this is planned for next year.

Mr. Chairman, it has been a pleasure to give you this summary. If you have any further questions, we would be happy to spend with you whatever time you like.

Chairman PROXMIRE. I think we have asked questions right along. I am just about through with my questioning.

I would like to point out what seems to be a very substantial improvement in your identical bid procurement. I notice that you had 8 million—nearly \$9 million in 1962, identical procurement, \$3 million in 1963, just under \$3 million in 1964, \$3.8 million in 1965, and you were down to \$1.3 million in 1966—a steady improvement.

Now, I am still somewhat shocked and concerned with the percentage of identical bid procurement if this statistic is right; it indicates it had been 22.5 percent in 1962. It declined to 5.4 percent. As I recall, when we were questioning the Defense Department about it, the identical bid procurement was below—way below 1 percent. An identical bid was very exceptional and unusual that they had identical bids.

I raised the point on their so-called negotiated competition, that would have a different kind of a collusion that they had to be very wary of, and be much more likely, and much more tempting. There are all kinds of ways two or three selected suppliers can get together.

But this percentage—Mr. Ward tells me—I had asked him before, and we were not able to figure this out. But now he says he thinks this is perhaps the total amount of all agencies' identical bidding, only 5 percent is from GSA. This would include all agencies, Federal, State, and local. Federal agencies are 64 percent, Department of Defense is a large percentage of that. And GSA is a relatively small percentage.

But you have improved in that respect as well as in so many others. We are very grateful to you.

Congressman Widnall, a member of this committee, has a series of questions, some eight questions he would like to have you answer. I won't ask you these at the moment, orally, but I would appreciate it if you could give us your answers for the record.

Mr. KNOTT. I shall be happy to.

(The information to be supplied for the record follows:)

GENERAL SERVICES ADMINISTRATION,
Washington, D.C., December 18, 1967.

HON. WILLIAM PROXMIRE,
Chairman, Joint Economic Committee,
Congress of the United States,
Washington, D.C.

DEAR MR. CHAIRMAN: This is in reply to your letter of December 12, 1967, which requested our response to a series of eight questions for inclusion in the recent hearings of the Subcommittee on Economy in Government.

The requested answers are appended hereto.

Sincerely yours,

LAWSON B. KNOTT, Jr.,
Administrator.

1. *Question:* Numerous bids offering foreign made hand tools must be further considered for award after application of the present Buy-America criteria used by GSA. Are any delays encountered in the final disposition of such bids and awards involving foreign source products?

Answer: In determining whether a low responsive bidder is responsible and capable of performing on a proposed award of a substantial contract, a financial

report is obtained on the bidder, and a plant facilities inspection is made on the manufacturing source, whether foreign or domestic. Usually, more time is required for such inspection in foreign countries. The additional time varies from a few days to several weeks, depending on the circumstances and whether qualified Government personnel are available in such countries, or commercial firms must be employed to perform the inspection.

2. *Question:* It is understood that GSA buys approximately 15 million dollars worth of tool kits annually for military users and that growing numbers of foreign made tools are supplied as components of those needs. As components of a kit such tools are excluded from provisions of the Buy-America Act. Does GSA have means for determining the dollar value of such foreign components?

Answer: Procurement of tool kits by GSA is subject to the Buy American Act. Substantially all kits purchased have been certified as domestic products. Under the Buy American Act, as implemented by Executive Order 10582, the kit is considered of foreign origin, if the cost of foreign products used constitutes 50 percent or more the cost of all the products used in such kits. We do not have any valid measure of the value of components of foreign origin within this limit.

3. *Question:* Does GSA have the necessary qualified people to understand both software and hardware in a total computer system to be able to write the technical specifications which will be used for requests for quota when seeking bids from computer manufacturers and peripheral manufacturers? (If the answer is "yes") : Then is there any reason or justification for having to ask a computer manufacturer to write the specification for the government?

Answer: GSA does not have qualified specialists who understand both software and hardware to the extent necessary to permit the development of technical specifications which, strictly speaking, would relate to the development and preparation of finite equipment system specifications. Generally, requests for proposals contain data system specifications which are required to be developed by using agencies in such a manner so that they ensure free competition among equipment manufacturers. In accordance with BOB policy guidance as contained in their Circular No. A-54, these specifications delineate the objectives which the system is intended to accomplish; indicate the data processing requirements in terms of data input and output, volumes of data, frequencies, and timing.

4. *Question:* Can you break apart a computer system in order to put individual pieces out for bid? In other words, can you put out for bid, for example, an IBM system which would include the break out of the main frame, the central processor memory, the line printers, the card reader, the card punch, the high capacity storage memories and the other peripheral equipment? If not, why not? If yes, has the Government done this; and is it standard practice to do so?

Answer: It is possible to break apart a computer system in order to put individual pieces out for bid provided adequate resources are available. However, at this time, neither the practicality nor the economic advantages that may obtain as a result of such a technique have been determined. Further study and evaluation to determine the relative efficiency and economy, including a careful study of alternative courses of action, is required. It is not a standard practice to segregate the various elements of a computer system and to put out individual pieces for bid, although we understand that in certain limited cases involving research and development, this technique has been used.

5. (a) *Question:* Do you have the necessary qualified people to assemble a total system?

Answer: No. GSA does not have the engineering staff necessary to assemble individual components, make modifications, and perform other work required to do this. GSA does not have an inventory of such qualified personnel within the Federal Government to be able to form a judgment on this as it relates to other agencies.

(b) *Question:* Is the government assembling its own computers or do we buy an entire system from one manufacturer?

Answer: As indicated in the answer to Question 5(a) above, we generally do not assemble a total system, but buy an entire system.

6. *Question:* Do you know whether any independent peripheral equipment is in any system purchased by the government from a major computer manufacturer?

Answer: We understand that there are systems supplied by major computer manufacturers which contain peripheral equipment purchased from another manufacturer.

7. *Question:* Would there be a significant saving to the government if both the independent peripheral manufacturers and the computer manufacturers were permitted to bid on any part of any total computer system required by the United States Government?

Answer: As stated earlier in reply to Question 4, this matter requires further study and evaluation.

8. *Question:* If a computer system is sold to the government by a manufacturer who does not make all the peripheral equipment which goes into the system, does the GSA have the prices paid by the systems manufacturers for each individual periphery and the main frame? (If "yes") In other words, is there any reason why the government should be paying more for the peripheral part than the cost to the systems manufacturer.

Answer: No.

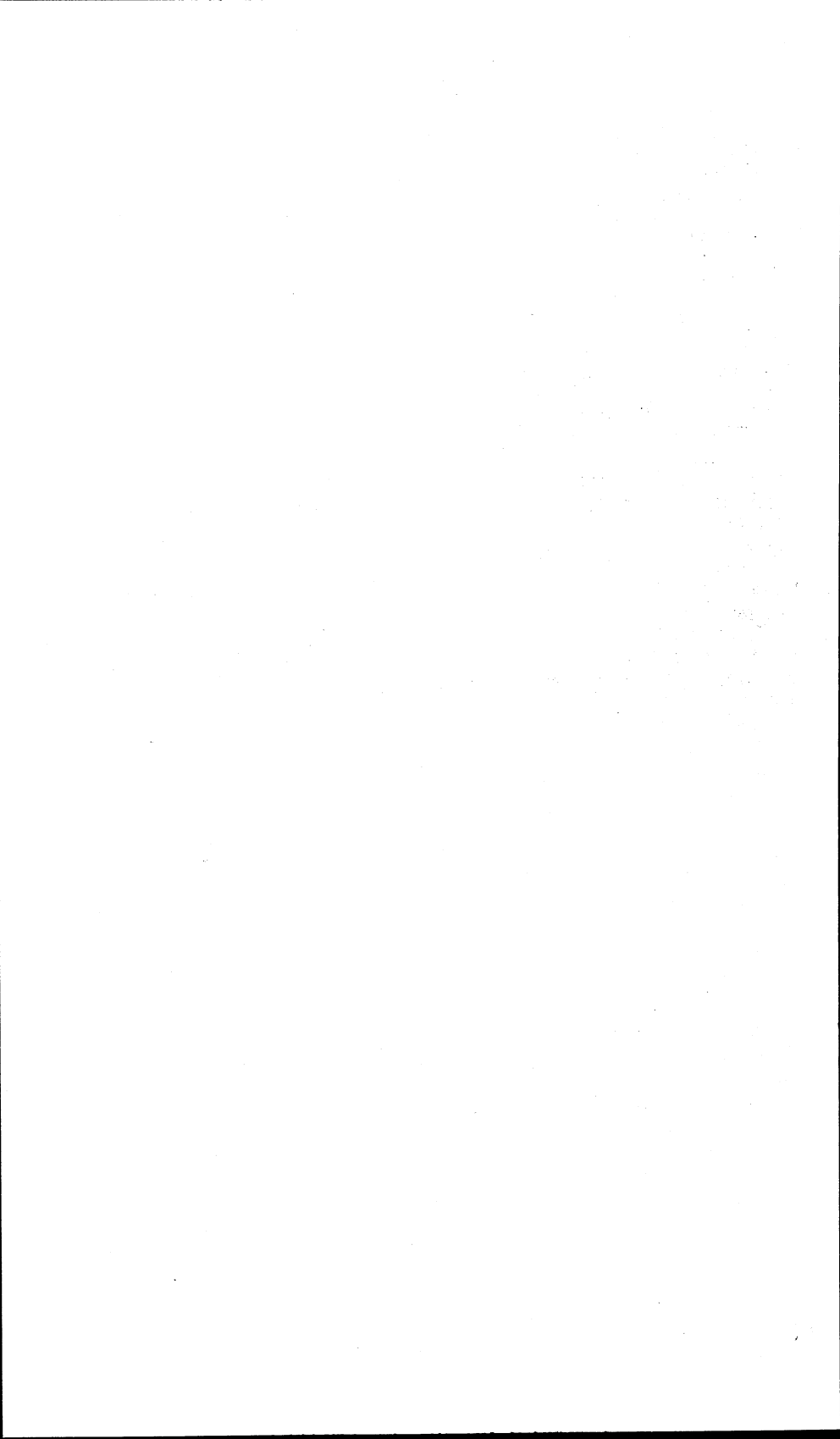
Chairman PROXMIRE. We want to thank you once again for a very competent and reassuring performance. I want to echo the eloquent words of Senator Percy. We are certainly very grateful to you.

Tomorrow we will conclude our testimony from our scheduled witnesses and welcome the return of the Comptroller General.

The witnesses will be Lewis R. Caveney, of the Bryant Computer Products, and Philip S. Hughes, Deputy Director, Bureau of the Budget.

We will convene here at 10 o'clock in the morning.

(Whereupon, at 12:15 the subcommittee was recessed, to reconvene at 10 a.m., Thursday, November 30, 1967.)



ECONOMY IN GOVERNMENT PROCUREMENT AND PROPERTY MANAGEMENT

THURSDAY, NOVEMBER 30, 1967

**CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON ECONOMY IN GOVERNMENT
OF THE JOINT ECONOMIC COMMITTEE,
*Washington, D.C.***

The subcommittee met, pursuant to recess, at 10 a.m., in room S-407, the Capitol, Hon. William Proxmire (chairman of the subcommittee) presiding.

Present: Senator Proxmire; and Representatives Griffiths and Rumsfeld.

Also present: Ray Ward, economic consultant.

Chairman PROXMIRE. The subcommittee will come to order.

Our first witness this morning is Mr. Lewis R. Caveney, representing the Bryant Computer Products. I should add that Congressman Widnall, a member of this committee, Congresswoman Griffiths, and others have expressed an interest in the views of Mr. Caveney.

Since we spend \$3 billion per year for purchase and lease of automatic data processing equipment, this is an important subject. I understand that you will give us a brief of your statement, Mr. Caveney, and we will insert the entire statement in the record without objection. It is quite a long statement. I understand you may abbreviate it.

**STATEMENT OF LEWIS R. CAENEY, ASSISTANT TO THE VICE
PRESIDENT, BRYANT COMPUTER PRODUCTS, DIVISION OF EX-
CELL-O CORP., WALLED LAKE, MICH.**

Mr. CAENEY. Mr. Chairman, I am Mr. Lewis R. Caveney and I appear here as assistant to the vice president of Bryant Computer Products, a division of Ex-Cell-O Corp., located at 850 Ladd Road, Walled Lake, Mich.

These hearings are extremely significant not only to my company but to all of the 50 major so-called independent manufacturers of computer peripherals. In fact, Mr. Chairman, I appear here today not only as a representative of my company, but as an unofficial voice for the independent manufacturers of computer peripherals nearly all of whom suffer from the problems I wish to bring to this committee's attention.

Our division is involved in research, development, and manufacturing of data handling equipment which are those memory devices required of total computer systems. Our division manufactures memory storage drums, memory storage disk files, and the controllers necessary to interface a memory device with a computer. We are an independent peripheral manufacturer in that we, including the total corporation we are a part of, do not build computers nor total computer systems but only specialize in the data handling equipment, or more frequently called, the memory devices for total computer systems.

Mr. Chairman, the problem that confronts the independent peripheral manufacturer is the continuous position by the executive branch of Government of maintaining an objective of freezing out the small independent peripheral manufacturers from selling directly to the Government as part of large EDP systems such as the large controversial Air Force phase II contract. If this practice is allowed to continue it will decrease the national economy in that it will decrease the growth of independents and the direct result will be a stagnation of technology and a decrease in employment and in some cases independents will be forced to go out of business with the end result being less competition.

The independents consist of over 50 major manufacturers of peripheral equipment consisting of divisions of large corporations who do not build computers or total computer systems and separate firms whose entire objective of profit is derived from peripheral manufacturing, thus, several thousands of citizens of the United States receive income direct from such independents and indirectly several hundreds of thousands more U.S. citizens are employed to support those employees of independents with consumer goods and service, therefore, the independents have quite an effect on the national economy and should not be deprived of their basic right to bid on a part of an EDP system in an attempt to receive their share of the Government buying power—after all, part of the Government's buying power is derived from independents in the form of taxes. The national economy with all its variables will without any doubt decrease if the Federal Government does not cease its current policy in acquisition of total computer systems, and I do not mean a token effort, but an open policy to allow independents to bid on any part of any total EDP system requirement.

Former President of the United States Harry S. Truman said in his White House letter dated February 19, 1948, when he signed into law H.R. 1366, which granted unprecedented freedom to the executive branch from specific procurement restrictions during peacetime, that this bill had a hidden danger. This freedom, he said, was

given to permit the flexibility and latitude needed in national defense activities. The basic need, however, remains to assure favorable price and adequate service to the Government. To the degree that restrictions have been diminished, therefore, responsibility upon the executive branch of Government, which includes the Defense Establishment, has been increased. The danger, he said, is the natural desire for flexibility and speed in procurement will lead to excessive placement of contracts by negotiation and undue reliance upon large concerns, and this he said must not occur—it has and is.

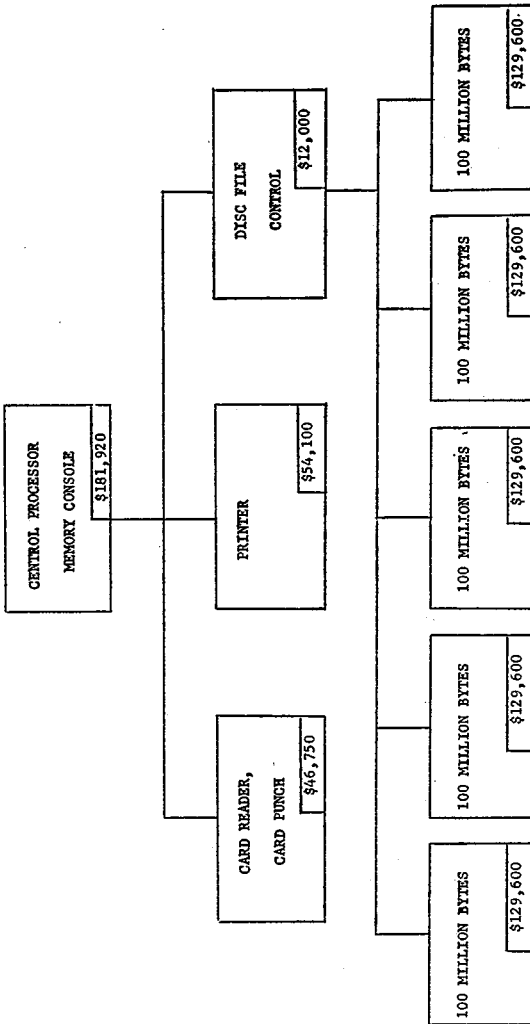
The U.S. Government must become aware of the cost savings to the Government through increased competition in Government procurement of peripheral equipment for computer systems but this can never be accomplished unless all manufacturers, both independent peripheral manufacturers and computer manufacturers, are permitted to bid on any part of a large computer system required of the Federal Government.

The major computer firms offer the Government complete computer systems involving main frames, peripheries, software and maintenance for many different sizes, types, and ranges of applications. They sell equipment that is GSA listed, or at least in their announced product line; and, generally, peripherals or other types of input/output equipment manufactured by independents are very seldom made available to the Government by the computer manufacturer unless under severe duress or under threat of losing a major order or unless a particular input/output device, periphery or feature that is nonstandard, is added to their otherwise published line of equipment for a particular procurement or due to the competition in the market.

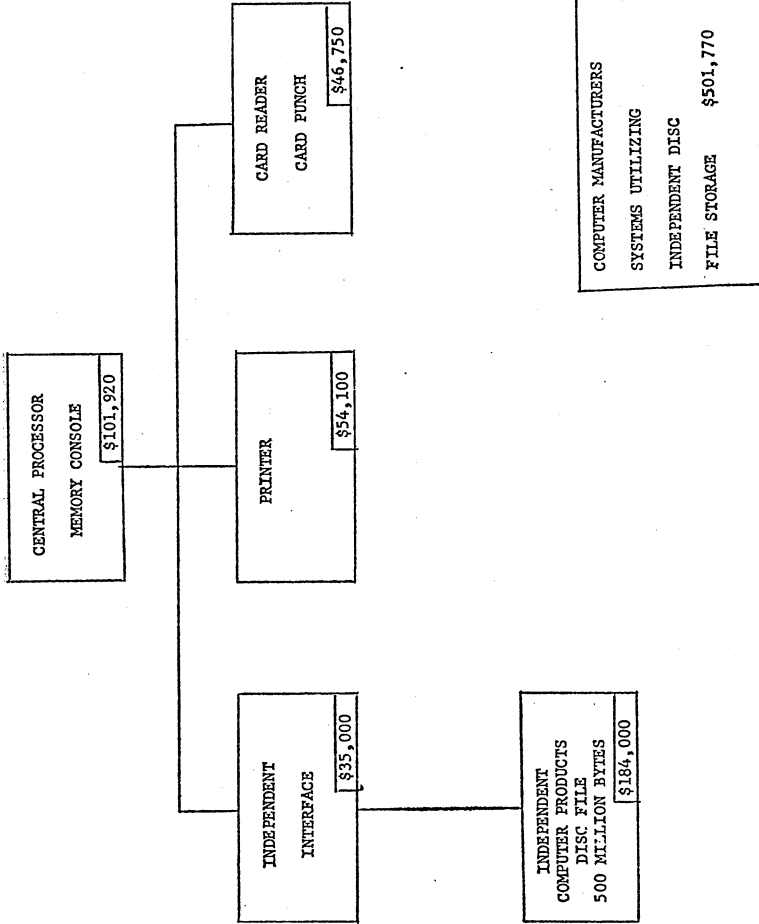
This practice raises the cost of procurement to the Government, provides less than an ideal solution to many problems for which the EDP system is intended to alleviate, since non-product-line peripherals are often not made available to the Government for many excuses, such as the difficulty of interfacing, maintenance and providing software for the nonproprietary periphery or nonstandard input/output device not carried in the computer manufacturer's price book, and tends to stifle competition which can be provided by the independent input/output and periphery manufacturer who often has superior equipment designed to do a specific job with such equipment readily available.

For example, Mr. Chairman, to illustrate this cost factor, I have prepared two illustrations, marked pages 6 and 7, which indicate the difference that could be saved if an independent had been allowed to bid and had won, from this illustration, the contract to furnish the memory and memory controller for the total computer system required of the Federal Government.

(The charts referred to follow:)



COMPUTER MANUFACTURERS
SYSTEM UTILIZING THEIR OWN
DISC SYSTEMS \$942,770



Mr. CAVENEY. It must be noted the five memory units of the computer manufacturer equal only one unit of the independent, and both meeting the specifications assigned with the only difference being price. GAO, I am certain, can substantiate the prices stated in the illustration and the fact it takes five memory devices at a unit price of \$129,600 plus another \$12,000 for a controller, with these being manufactured by a computer manufacturer, whereas one independent firm's memory would equal these same five units, but at a price of \$184,000 and \$35,000 for the controller, with the savings being \$441,000, if the Government had purchased the memory equipments individually and had not purchased a total computer system from the computer manufacturer. These figures are just initial cost savings.

Further, if five memories take about 400 square feet of space and the one memory takes only about 64 square feet it can be readily seen another dollar savings in floorspace is achieved. I have been informed by GSA officials this runs well over \$100 per square foot.

Further, you take the five equipments, and count individual parts, it is easily understandable that to support these five units with spare parts and maintenance personnel, the one unit requires about 75 percent less, and again, a savings is accomplished.

Further, operating manpower increases with the five units and thus the overall cost savings for this example is well over half a million dollars and if you multiply this by just 100 such cases you are at a savings of \$50 million. These figures do not include downtime—that time equipments are down due to failure, and this cost runs extremely high at a rate per hour. A total breakdown of each peripheral, plus the other variables including, but not limited to, spare parts, maintenance, floorspace, and manpower involved in a total computer system, the savings would be astronomical just for one—repeat, one—total computer system.

The GAO can clearly substantiate the fact that the Government, in a considerable amount of procurements, procures peripheral equipment, manufactured by independents, unknowingly, but via a computer manufacturer with such peripheral equipment being purchased at a price higher than if the Government had purchased each of the equipments required of the total computer system directly from independent peripheral manufacturers and computer manufacturers, and the Government plugging the system together.

Regarding the need of the technology put forth and available from independent peripheral manufacturers is exemplified by the article taken from the Electronic News, November 13, 1967, issue, under the title "Computer Trend, 1967," with the pertinent data quoted verbatim.

"Marriage counseling will soon become big business in the computer industry."

"But the computer industry 'marriage counselor' will not be called on to solve difficulties of estranged men and women. Instead he will work on the problems of wedding noncompatible peripheral equipment to the main frame system."

To capitalize on this potential business, Datametrics Corp., North Hollywood, Calif., is changing from a general customhouse to a specialist in marrying non-compatible pieces of hardware for computer application.

Dr. Melvin P. Peisakoff, group director of computing systems, planning and operations at North American Rockwell Corp.'s Space & Systems group, observed, "I think this would be a good business to get into." He feels the emergence of the marriage counselor will increase competition and give the user a better cost performance from his peripheral equipment.

When the main frame manufacturer knows that the user can turn to another supplier of peripherals for hardware which will be used with his main system he will price and engineer things better," Dr. Poisakoff said.

It was indicated the marriage counselor will also offer an avenue to the outside supplier of peripherals which might otherwise be blocked by the difficulty of engineering a unit to meet the various specifics of the many main frames.

One factor encouraging the counselor is the reluctance of the major systems manufacturer to expend time and money on wedding non-compatible hardware to this computer.

The major systems manufacturer would prefer to unite his peripherals with his main frame, saving lots of time and effort and adding dollars to corporate coffers.

The big hangup comes when the user says, "But your peripheral does not answer my needs and so I'd rather have what's-his-name's peripheral."

MARKET CREATED

Since the main frame producer would rather expend his money on getting his own hardware out the door, a market has been created for such people as Datametrics, Philip A. Ingalls, manager of applications, said.

Mr. Ingalls said the biggest interface area is in communications—remote computers and remote terminal sites. He said this market has been created by the non-compatibility of common carriers' data links with computer hardware.

While major computer manufacturers are reluctant to talk about the problem, Mr. Ingalls contends they have problems marrying some systems to peripherals.

In particular, Datametrics is aiming at a market of possibly 10-of-a-kind marriages. This might include a user who wants an extra-large desk file which the producer of the main frame does not have.

INTERFACE PACKAGES

The Data Products Sales group has developed interface packages to meet the problem of uniting one of the company's peripherals with any standard computing system.

Mr. Drake feels the need for counseling will continue to increase because "the user is becoming more sophisticated about his peripheral needs."

He contends that a few years ago the user might accept what the main frame producer might say completely, but now the user is prepared to look around and decide for himself.

The major main frame producers don't like to talk about this aspect of the peripheral story.

Chairman PROXMIRE. Marriage counseling is going to become big business in the computer industry.

Mr. CAVENEY. Yes, sir; it is. Since you made that statement—

Chairman PROXMIRE. I do not want to get into that now.

Mr. CAVENEY. It should be noted that the group director of Computing Systems at North American Rockwell Standard Corp.'s space and systems group, who is not in the commercial computer business, made comments that are enlightening to both the Government and, of course, the peripheral manufacturers.

The individuals I have talked with in the executive branch of Government maintain the computer system know-how is lacking in the executive branch of Government and, therefore, they must go to industry for expertness in this field which is the same old outdated excuse they have been using for over 5 years for placing total EDP procurement with just computer manufacturers. Mr. Chairman, this was a true statement years ago but the executive branch of Government is considered by industry to have the best caliber personnel available who are knowledgeable and understand the total computer disciplines, and, therefore, the weak excuses offered appear to be offered by stagnant individuals reluctant to shift into an area requiring change.

The laxity by certain Government procurement facilities to write their own specifications stimulate the lockout of independents as the Government calls on a major computer manufacturer to write the specifications for the Government and naturally the specifications are written to the manufacturer's equipment. The Government places these specifications in a request for quote and then invokes that portion of Armed Services Procurement Regulations (ASPR) which will not allow any deviations and the manufacturer who wrote the specification is assured that he will receive the award because all the other bidders cannot meet the specification without deviation.

If the Government would pull key personnel under one group and cease the overlapping of functions not only would proper specifications be written but the budget could be reduced and such funds and personnel transferred to those functions of Government which handle the internal problems of the United States, such as poverty.

The eight major computer equipment manufacturers in this country cannot and do not provide in every proprietary periphery or input-output device the best device to do the job that is available on the market in their product line in most cases. This would be the same as saying this or that manufacturer is batting out a score of 100 percent.

Experience shows this does not happen; but there are many healthy independent periphery manufacturers who often offer superior equipment, but unless this equipment is made standard product line with the OEM (original equipment manufacturer) supplying the Government, the Government generally cannot purchase this equipment from them unless considerable time and expense is expended by outright insistence of the procurement authority to have a specific nonstandard component included in his system.

The U.S. Navy, specifically, the U.S. Navy Weather Facility, at Monterey, Calif., has recognized the fact that it isn't true that the best total computer system can be procured from any specific computer manufacturer. They realize they will not receive the best peripherals to do the best job for the application required at the lowest possible cost. The U.S. Navy procurement method resulted in savings which the GAO can substantiate which clearly points to a significant savings to the U.S. Navy when the equipment required of the total computer system was procured from independent and computer manufacturers.

This type of procurement made by the U.S. Navy I have defined as procurement of a total computer system by the "black box concept" and/or "modular concept" which is giving the independents and the computer manufacturers the right to bid on any part of an EDP system required of the Government of the United States. The Government's practice of freezing out the small independent peripheral maker from selling directly to the Government as part of large EDP systems is not new and as the practice is continued to be maintained by the Government the cost to the taxpayer is increasing year by year at an accelerated pace, since the number of available peripheral devices is increasing at a rapid rate and is expected to continue to do so through the 1970's.

The types of devices manufactured by independent peripheral people are modems, line printers, magnetic tape machines, magnetic drums, disk files, plotters, displays, tape punches and readers, et cetera. Over

50 companies are involved in the specialization in research, design, development, and manufacture of peripheral devices for computer systems that are compatible to almost any digital computer system in the Government operation. Some of these companies have achieved product line status with the major computer manufacturers. However, a great majority do not enjoy this very special and privileged relationship and are threatened with loss of their business in the future unless a change is made to Government procurement practices involving procurement of complete computer systems and equipment from only the computer manufacturer.

This freeze by the Federal Government is stimulated by the lack of control over appropriated funds received from Congress. Some elements of the Department of Defense and the U.S. Office of Education receive appropriated funds and in turn give them out to major universities for special computer requirements and little if any control over the funds are maintained. As an example, one element of the Department of Defense granted funds to a major State university and an independent was asked to assist on the memory application which he did for some 8 to 9 months and all communications indicated he would receive the memory contract and then silence from the university. After pressure was applied, it was learned the computer manufacturer who received the computer contract knew he would not receive the memory contract so he literally gave a new memory device to the program professor and the comment received from those in the university who were solely responsible for the program stated that they did not bother to ask the independent to requote in that they felt he could not compete with such an offer from the computer manufacturer. What is felt and what is proper procurement ethics are two entirely different practices and too many times the term "felt" and not adhering to any procurement ethics is the rule rather than the exception in today's Government procurement philosophy.

The Department of Defense element involved when confronted became very antagonistic and the procurement method by the university was condoned until the independent confronted them with the possibility of taking the incident to Congress and letting Congress decide if the proper control of appropriated funds had been adhered to and if proper procurement policies were being maintained. They very rapidly changed their "holier than thou" attitude. The element within the U.S. Department of Education grants funds piecemeal in a majority of cases and does not communicate funding information properly and certain universities with computer programs which are to be paid by appropriated funds cannot procure from independents because all funds are not available nor is any specific PERT time scale made available when such funds will be allowed and therefore must turn to a major computer manufacturer who will permit little if nothing down in respect to funds for 12 to 24 months or until Government funds are actually available for such programs at that university to spend and independents just are not that rich nor are the majority of computer manufacturers.

Another stimulant to lockout of independents by the Federal Government is allowing free service to be accepted by the Federal Government from large computer manufacturers which even the computer

manufacturers themselves are making large overtones about as stated in the November 22, 1967, issue of the Wall Street Journal with the following statements quoted verbatim:

IBM's competitors don't want to comment publicly on the current Government investigation (neither does IBM, nor the Justice Department), but executives of three IBM rivals privately confess that they consider Government intervention to stimulate competition in the industry long overdue. At the very least, one rival would like to see the Government require IBM to charge customers for services it now provides free.

At least one IBM rival company, however, believes the computer business would become far more competitive if Federal trustbusters ordered IBM to quit providing certain free services to its customers—including preparation of computer programs and visits from IBM systems analysts who show customers how to adapt a computer system to their own needs. Competitors complain that they can't match the services that IBM provides for no charge beyond the lease or purchase price of its machines. If IBM had to charge extra for such services, one of its strongest selling points would be eliminated, some industry sources believe.

Further stimulants to the freeze of independents and even computer manufacturers by the Federal Government is expressed in procurement ethics of the U.S. Air Force as stated by the November 22, 1967, issue of the Wall Street Journal with the following statements quoted verbatim:

Some IBM competitors say that Government buying practices over the years also helped IBM gain dominance. The head of one rival computer maker claims that Federal "procurement specifications are written around IBM machines," a charge that Government purchasing men deny.

This computer executive also maintains that Air Force purchasing officers "want aerospace firms to stick to IBM machines" and, in some cases, have refused to allow aerospace companies to buy from other manufacturers on the ground that costly new computer programs would have to be prepared for non-IBM machines.

All the independent peripheral manufacturer is asking is to have an equal opportunity, on a competitive basis, to be considered for Government business on his own merits of price, delivery, maintenance, logistic support, reliability, reputation and performance.

Today this is no sure road to success since the major manufacturers are all dedicated to building their own peripheral equipment and, in effect, freezing out the independent manufacturer from this growing and important segment of the computer business which is right in the free enterprise system but to have the Federal Government literally lock out independents is not right. The main frame is becoming less and less the major cost item in the average computer system. The difference in performance between computer systems of the future may well rest in the efficiency and reliability of the input/output devices.

For the Government to obtain the most of its taxpayer's dollar in the electronic data processing field the Government must immediately recognize the fallacy in their current procurement methods involving the purchase of total computer systems from one manufacturer. The degree of sophistication of some Government users is increasing and today some scientific branches of the Government are actually purchasing computer systems and equipment, with hardware and software often coming from different sources, with even maintenance being supplied by a third party.

Some large industrial users are going this same route and the trend is definitely toward the acquisition in major computer user organiza-

tions of hardware-oriented people to make the purchasing decisions on the basis of merit of the individual equipment or service, whether it be manufactured by computer maker or from an independent supplier.

The Ford Motor Co. has also recognized this fallacy and has employed our former assistant manager of systems who has stated the prime objective of his position is to bring to Ford Motor Co. the hardware knowledge and understanding of computer systems and to assist in implementing the best peripherals and augment the many total computer systems they now have with better peripherals which will assist in decreasing computer systems leasing costs, initial computer system cost, maintenance cost, floor space, manpower, and new buildings which were forecasted for computer facilities which now can be used for more important functions with all this leading to a tremendous dollar savings.

Mr. Chairman, we are faced with a situation in which one minute the Government says it wants competition and the next it practices a lockout of manufacturers.

Yet, if Government would follow just competitive practices both the Government and the taxpayer would benefit. The Government would be able to obtain superior equipment at lower cost through increased competition, and could serve to advance technology in the computer industry by preventing the ultimate destruction of many peripheral makers that today cannot foresee competing with major computer firms if the current lockout situation is allowed to continue in Government procurement.

The ultimate solution to this problem is a Federal standardization in the industry of interfaces between peripheral equipment and the computer proper. This is not something that obviously can be done overnight and should be a main objective of the Government now for future procurement of fourth generation of computing equipment.

Strong indicators clearly indicate Federal standardization would help to direct these companies to establish common interface equipment to allow the Government a free choice of input/output and peripheral equipment with assured compatability between the devices and systems. This can and should be a subject for Government control of the computer interface, at least involving computer equipment furnished the U.S. Government.

At the present time, however, an immediate solution is available that will allow the Government to purchase virtually any peripheral device and yet be assured plug-in compatability can be achieved at reasonable cost without resorting to special negotiations between the Government, the independent peripheral supplier, and the manufacturer of the computer.

This solution rests in the creation by each computer manufacturer for machines offered to the Government, a general purpose peripheral adapter. This device is not a controller, but provides the required timing, controlled data, and interface circuit specifications necessary to connect the peripheral device to the computer manufacturer's line of computers. It is anticipated that there would probably be a general purpose adapter for each series or type of computers from a given manufacturer.

The object of the general purpose peripheral adapter would be that for each manufacturer this unit would be clearly specified and listed

by GSA, such as other computer equipment now listed. The Government and the independent peripheral manufacturer then is assured that the specifications, input/output data, and control requirements of the peripheral interface are frozen or standardized and not subject to change at the whim or design of the computer manufacturer to intentionally or not thwart attempts of end users, such as the Government, from buying from second sources often less expensive and superior performing peripheral equipment; and equipment not available from the computer manufacturer.

One company has done this. The Honeywell Corp. has designed, built, and is marketing such a peripheral adapter. This unit allows the 200 series Honeywell computers to transmit data to and receive data from a wide variety of peripheral equipment not included in the standard series 200 product line. It is not in itself a complete peripheral controller which would be supplied by the independent peripheral manufacturer, however, it does contain all the common features required to communicate with the 200 line computers without the peripheral manufacturer or the Government necessarily becoming involved in the internal bussing and control operations of the computer proper.

Availability of this type of device gives the Government freedom in purchasing computer peripheral devices not manufactured or sold by Honeywell. The general purpose peripheral adapter offered by Honeywell appears to be unique in the computer industry and is something that should be required, in our opinion, of all computer manufacturers doing business with the U.S. Government.

Bryant Computer Products is currently offering several large industrial organizations series 4000 Bryant disc file systems attaching to a Honeywell 200 through their adapter. The XLO-1000 Controller, manufactured by Bryant, is compatible with the Honeywell peripheral adapted with a minimum of effort, as it would to any similar general-purpose adapters made available by other computer manufacturers.

We feel strongly, in conclusion, that the Government is not and cannot efficiently, at lowest cost, purchase complete computer systems for all types and classifications of applications as complete systems from any of the major computer manufacturers. This is due to the diversification of requirements for performance, cost, and for input/output of peripheral equipment which is becoming more highly specialized and more important to the average computer installation every day than is the capability of the main frame itself.

Computer systems cost is increasingly going into the electro-mechanical peripheral equipment area, and the trend is expected to continue upward for many years. In order for the Government to be able to purchase the best of these peripheral devices and to assemble systems with a minimum of difficulty, at the lowest possible price, a common interface is essential in the fourth generation computers now on the drawing boards. However, we feel there is no necessity to delay these benefits, nor to further tolerate the stifling of competition and the possible demise of very capable independent peripheral companies and their technology, by waiting for the advent of the fourth generation and a common Federal interface.

The general-purpose peripheral adapter is a device that can be designed and made available for any computer series by any manufac-

turer at this time. We need Government support by direction from the executive branch of Government to the General Services Administration to require computer manufacturers doing business with the Government to provide published information on standard peripheral adapters at this time.

Strong indicators exist which seem to substantiate the fact the executive branch condones, either knowingly or unknowingly, unethical practices of the Federal procurement elements to freeze independent peripheral manufacturers from submitting proposals to (1) commercial segments who have been given appropriated funding from the U.S. Government for computer system procurements and (2) directly from Federal procurement segments themselves.

Unless our words are heard the independent peripheral manufacturer will eventually decrease and become annihilated from the market which will decrease employment, stagnate technology, decrease competition, and increase cost to the taxpayer. Action must be taken to correct this problem as time is something the independent peripheral manufacturers just do not have.

I thank you, Mr. Chairman.

Chairman PROXMIRE. Thank you, Mr. Caveney. That is a very impressive statement.

Mr. Caveney, what experience have you had in Government procurement?

Mr. CAVENEY. Mr. Chairman, I was a former Marine Corps officer. I graduated from the Marine Corps Supply School, fourth out of a class of 33. And I spent my last 4 years with the Armed Forces special weapons project of AEC in the repair and manufacturing of nuclear weaponry.

I left the service and acquired a degree, majored in accounting, and contract law, and I have since been with my current company, where I am not only assistant to the vice president, but manager of all contracting and foreign licensing. So I am well versed in procurements of the Federal Government on both sides of the fence.

Chairman PROXMIRE. You acted in your capacity as a military officer as a procurement official—you bought for the Federal Government?

Mr. CAVENEY. I bought for the Government from commercial sources.

Chairman PROXMIRE. What did you buy? What was your area?

Mr. CAVENEY. Handtools—anything from toothpicks on up through minor computer periphery.

Chairman PROXMIRE. You did buy computer—

Mr. CAVENEY. Yes. But it was done by higher authority, I was a junior officer, and we would sit down in concert with the colonel and we would take parts of the contract. He would make the ultimate decision.

Chairman PROXMIRE. Who were the 50 independent peripheral companies you are talking about?

Mr. CAVENEY. Just to name a few—a list can be passed to the committee members, which Mr. Ward has several copies of—it will show the 50 major ones with some being as large as Packard Hewlett, a large corporation.

(See app. 6, p. 530.)

Chairman PROXMIRE. That is a peripheral manufacturer?

Mr. CAVENEY. Yes. One of their divisions makes peripherals.

Chairman PROXMIRE. How do you discriminate between a peripheral—and what do you call the other ones?

Mr. CAVENEY. They are computer manufacturers. Independent peripheral manufacturers do not make computers, nor do they make total computer systems.

Chairman PROXMIRE. But you make computer parts?

Mr. CAVENEY. No. Mr. Chairman, the word "parts" is the wrong word—excuse me.

Chairman PROXMIRE. That is all right. I am glad to get corrected.

Mr. CAVENEY. As the GSA brought up yesterday, which was not correct, you take a light bulb, and if you laid the brass base out, the filament, and the glass top, they have no purpose whatsoever until they are put together, and then and not until then do they have the intended purpose of being inserted into a socket, and you push the switch on and off, and the light comes on. Now, that is an assembly which has an end use, which can be sold as an identifiable item.

Now, I have heard this same type of statement, of assembly part, used to either distract people in Government from the fact that they are trying to maintain that a peripheral is in fact a part.

Chairman PROXMIRE. My question is to determine the difference—what superficially rational basis, if you do not say it is rational—I think you make a strong case—the Government has for not procuring from you and insisting on procuring from the computer manufacturers.

What do you do? What is it—what does the peripheral producer do, what does he provide?

Mr. CAVENEY. He makes a specialized unit that is required in a total computer system—the memory, the memory system, the printers, et cetera.

Chairman PROXMIRE. He makes all of these specialized, or some of these?

Mr. CAVENEY. He makes all of them, not just a few of them.

Chairman PROXMIRE. And the computer manufacturer would make them all, or would at least procure them all and put them together?

Mr. CAVENEY. Yes.

Chairman PROXMIRE. I raised this specific point yesterday, and I think we have raised it before; GSA, as I recall—and Mr. Knott confirmed this was their position—in contradistinction to what you say, the Government, they feel, does not have the qualified personnel to do the job of assembling the various components into an overall computer, and that to do this, and to assume this responsibility is something the Government is willing to pay for, because they feel private industry can do it better.

Mr. CAVENEY. The U.S. Navy has done it. It is not a very difficult thing. It is just like plugging your lamp into the wall—it is so simple today. We have an Ex-Cell-O 1,000 controller, and with minor insertions of the electronic cards, we can plug into just about any major computer system.

Chairman PROXMIRE. Well, don't these people in private industry who assume this management responsibility for getting the parts from

the so-called peripheral producers, and then assembling them—aren't they very well paid?

Mr. CAVENEY. They certainly are highly paid.

Chairman PROXMIRE. They are not?

Mr. CAVENEY. They are highly paid.

Chairman PROXMIRE. Well, can the Government meet this kind of competition for personnel? We have pretty strict limits on what we can pay?

Mr. CAVENEY. I have talked to several people at your Elite Command, such as the Naval Electronics Systems Command, the Army Command, Rome Air Development—and the people there, to me, are the finest caliber individuals that you could find, they are second to none in the United States in the computer industry. With this top talent, I do not see why the Government cannot plug computer systems together.

Chairman PROXMIRE. You say the Navy has already done it?

Mr. CAVENEY. The Navy has already done it.

Chairman PROXMIRE. And they have been successful in doing it, and made a saving in doing it?

Mr. CAVENEY. Yes; Mr. Chairman. In fact, they came back for the third, fourth, fifth, sixth, and seventh memory and memory systems, right now, from us.

Chairman PROXMIRE. You see no reason why the rest of the Government—space, Air Force, Army, and so forth—cannot do the same thing?

Mr. CAVENEY. No, sir.

Chairman PROXMIRE. Does the Navy do this comprehensively?

Mr. CAVENEY. No—this is the only time I have ever heard, in my experience with my company, that we have ever been a true prime to the Government. Normally when we are a prime, it is when a total computer system has been purchased by the Government, and then certain peripherals fail—memories. Then they come to us for high capacity, and then they put the memory that was in out, and they move ours in. The only other time is when we sell spare parts direct to the Government.

Chairman PROXMIRE. Secretary Morris said in his testimony when price competition is introduced there is a saving on the order of 25 percent. What would you estimate to be the saving to the Government if the peripheral manufacturers were permitted to bid on computer systems?

Mr. CAVENEY. Well over 25 percent, as exemplified by my illustration. There alone it was over half-million dollars. The highest price was \$900,000, roughly, the lowest was \$500,000, with a saving of \$400,000 in that one incident.

Chairman PROXMIRE. How many computer manufacturers are there?

Mr. CAVENEY. There is IBM and 70 others.

Chairman PROXMIRE. IBM pretty much dominates the field?

Mr. CAVENEY. Yes.

Chairman PROXMIRE. What proportion of Government procurement would you say they get in the area of computers?

Mr. CAVENEY. Well, I really cannot answer that.

Chairman PROXMIRE. But you think it is enough so that they are the dominant force; is there a degree of price leadership?

Mr. CAVENEY. We really do not follow the computer industry—I mean the total computer industry—because we feel they have dominance in the field.

Chairman PROXMIRE. When the Government procures a computer, do they by and large do this on an advertised competitive bidding basis for the computer manufacturers, or do they do it on some negotiated basis?

Mr. CAVENEY. Well, there again—

Chairman PROXMIRE. I know it varies. But, what is the rule?

Mr. CAVENEY. We are normally subcontractors. We receive the proposal down on big programs from a prime, such as RCA, and then we have to convince him to put our equipment into the system. We do not know the method, because it is a rule—and I have never read it in the regulations—but the rule is that the Government cannot talk to the subcontractor, only the prime can. And I have always felt this has been wrong as the whole truth by the Government is not known.

Chairman PROXMIRE. You do not know, then, what the system procurement is?

Mr. CAVENEY. No, we do not.

Chairman PROXMIRE. Finally, you referred to the need for a kind of computer marriage counselor, and a knowledge that the function would be to bring the peripheral manufacturers together?

Mr. CAVENEY. Well, I brought that up because of the statements made indicating the end users today realize independent peripheral manufacturers can supply the equipment to do the application at a cost savings which no longer can be overlooked.

Chairman PROXMIRE. This is a wedding counselor rather than a marriage counselor. It is not having trouble among the peripheral manufacturers, it is just arranging the procurement.

Mr. CAVENEY. No. This is because the end user today—banks, industry, small businesses—have become more knowledgeable of computer systems, and they are saying now to the computer manufacturer “Look, we do not like some of your peripherals, we want Joe’s over here, who makes a peripheral that meets our requirements better and it is cheaper.” They will say “You can’t have that, we don’t sell that.” They say “Well, I will get this marriage counselor, he will interface it.” And this is what the market trend is right now.

Time sharing has brought this out.

Chairman PROXMIRE. Would the Government procurement official act as a marriage counselor in this sense? Would he bring the peripheral manufacturers together for the Government into a complete computer system?

Mr. CAVENEY. Yes, sir. The Navy is doing it.

Chairman PROXMIRE. OK.

Mrs. Griffiths?

Representative GRIFFITHS. Thank you very much. I am especially pleased to have you here, Mr. Caveney. As you are aware, the president of the parent company is my constituent. And I am delighted to welcome you here.

Particularly I am happy to see a former purchaser, too, for the Government.

I would like to ask you this:

Let us assume for all practical purposes IBM is drawing the specifications for the purpose of computer systems, and they know before they start that they are going to be the qualified bidder.

What real advantage would there be to them in buying a cheaper peripheral system than—for any purpose?

Mr. CAVENEY. You mean the Government buys a cheaper peripheral.

Representative GRIFFITHS. No; for IBM. If they know they are going to be the qualified bidder, there is no advantage to them to buy a cheaper peripheral system?

Mr. CAVENEY. No; because the specification including the engineering numbers, the technical numbers, are stated around their equipment, and then when the Government invokes the clause whereby no deviations can be taken to the spec, in my opinion it is sort of unknown collusion.

Representative GRIFFITHS. Of course, it is. The result of it is that IBM makes more money on a higher price periphery system than they would make if they had a cheaper, better one—or anybody else that is drawing the specifications and knows he is the qualified bidder to start with.

Mr. CAVENEY. That is right.

Representative GRIFFITHS. May I ask you this. What would you think would be the result in my bill, to ask that the contractor show the price he has paid to every sub, be invoked just in computer systems? Just the first tier of subcontractors. What do you think the result would be?

Mr. CAVENEY. Well, I don't know what the result would be. I know what it should be. The bill should go through.

Representative GRIFFITHS. Good. But what do you think it would be in the matter of savings for the Government?

Mr. CAVENEY. Well, I would estimate just roughly it should amount to—in inventory time alone—would run around a half a billion dollars.

Representative GRIFFITHS. We are just talking about one set of purchases—just IBM systems or just computer systems—and asking only for the first tier of subs to supply the information. And do you really think it would take much manpower to keep track of that?

Mr. CAVENEY. No, I do not.

Representative GRIFFITHS. In the first place, they are not making a sensible buy when they do not know the price—the cost of building up—

Mr. CAVENEY. As an example, just our small division—we have over roughly 90,000 items what we call smart parts, and we only have a staff of four people that do all the purchasing and maintain inventory control on data processing equipment.

Representative GRIFFITHS. I do hope, Mr. Chairman, you are hearing this and supporting my bill.

Chairman PROXMIRE. Yes, indeed.

Representative GRIFFITHS. I would like to ask you, also, if you are selling now any parts to a prime—I mean any periphery system to a prime contractor for the Government?

Mr. CAVENEY. Oh, yes, Mrs. Griffiths.

Representative GRIFFITHS. Do you know what markup they take on it?

Mr. CAVENEY. No, I do not. However, I do feel that GAO has access to this.

Representative GRIFFITHS. And they could give us that answer?

Mr. CAVENEY. I am 100-percent confident they could, because of the fact they have access to Government contracts.

Representative GRIFFITHS. Mr. Chairman, will you ask one member of the staff to find out from GAO the markup on a periphery system in a computer?

Chairman PROXMIRE. Yes, indeed.

Representative GRIFFITHS. And let's put it in the record at this point.

Chairman PROXMIRE. Is there a representative from GAO here today who might know offhand? If not, we will certainly find it out and put it in the record. We will do that, Mrs. Griffiths.

Representative GRIFFITHS. Thank you, Mr. Chairman.

(NOTE.—GAO is currently formulating an answer to the preceding question and at the time these hearings went to press had not completed the study.)

Representative GRIFFITHS. I have just come from the Ways and Means hearing on the tax bill, in which the Secretary of the Treasury is asking us to defend the dollar. I personally feel that if the Secretary of Defense were to look at the mission of defending the country, it would not really be necessary to ask the Secretary of the Treasury to defend the dollar. Here is the place to take the money. And the savings you have already shown us, and the savings that we have already shown in this hearing, if these are made, we are in no problem.

The real truth is that the Defense Department is overpaying on almost every item that they purchase, because they do not know the price of anything—they do not know the cost of making anything—at least that is my judgment—as one ex-purchaser to another.

Mr. Ward would like to know, is it possible for one control point to keep an inventory of 4 million items and match requirements against it?

Mr. CAVENEY. Is it possible to do this?

Representative GRIFFITHS. Yes.

Mr. CAVENEY. Yes; I would say that I could handle 4 million line items and control them, and have a positive inventory.

Representative GRIFFITHS. Thank you very much.

Chairman PROXMIRE. Thank you, Mrs. Griffiths.

I would like to ask, before Mr. Caveney leaves, whether GSA representatives wanted to make a statement clarifying their position on this problem. I may have phrased the question differently to them yesterday, and I want to be sure I am fair to them. Mr. Abersfeller, in this case, is there an opportunity for these particular manufacturers to sell to the Government directly?

Mr. ABERSFELLER. Mr. Chairman, I think that opportunity exists. I talked to Mr. Caveney last night. He is coming in to see me on Friday, to explore this further.

Chairman PROXMIRE. What I wanted to clarify particularly was the impression that I got yesterday that you felt that the Federal Government was not in a good position to buy component parts, or in this case component systems, perhaps, because of the lack of the capacity to put these together.

Mr. ABERSFELLER. Well, it depends so much on the component part. There is in my view at least a lack of capacity, when we are talking about the total Government. Some agencies may have the capability of doing it. At the moment I think there is a lack of capacity to put it together. But if as Mr. Caveney says it is a matter of plugging it in, it is not the kind of technical problem I understood it to be.

Chairman PROXMIRE. Do you want to follow that up, Mr. Abersfeller? Go right ahead.

Mr. ABERSFELLER. I was just going to say one of the first things we must do is that we must get the product on the Federal Supply Schedule. Mr. Caveney has referred to talking to a lot of people. But unfortunately we have not had the opportunity of discussing this matter with him to establish a contract with his company for the products which they make. We do have contracts with 40 accessorial and periphery manufacturers now. But we do not have any with his company, nor to my knowledge—I do not have the list of the 50 companies—but, certainly, that is the first effort we must make. We hope to do that Friday.

Chairman PROXMIRE. You say you are buying from 40 peripheral manufacturers similar to Mr. Caveney's and you feel that there is not any significant or serious obstacle in the way of procurement?

Mr. ABERSFELLER. Not at the moment. I feel there is no particular obstacle at the moment in putting this item on the schedule.

Chairman PROXMIRE. Mr. Caveney?

Mr. CAVENEY. Let's clarify one thing here now. GSA is not giving the total picture.

I am talking about the big procurements, like the Buick program, the Bull's Eye program, the Air Force phase II contract, which GSA has no control over whatsoever.

Chairman PROXMIRE. You are talking about defense?

Mr. CAVENEY. Yes. This is where the dollars are located.

Chairman PROXMIRE. Will you add to the Navy program—the GSA in their procurement—

Mr. CAVENEY. We hold the highest esteem for GSA. In fact, we like the Brooks bill, but we feel it does not have enough teeth. And we feel the GSA is doing a tremendous job for everybody, not just one side of the coin. We feel that the Brooks bill has not got the proper teeth in their area of procurement of EDP equipment.

Representative GRIFFITHS. Mr. Chairman, may I ask the GSA?

If you could buy a part, one of these peripheral systems, to update a system, a computer system, do you have the knowledge and the authority to do it—in place of tossing that out and buying a whole new system?

Mr. ABERSFELLER. We have the authority to do it. I do not know whether we have the knowledge. It would depend on the peripheral equipment. We would have to examine it in some depth. But I would like to clarify something Mr. Caveney has mentioned. Apparently he does not know that we do have to do with the procurement the Defense Department makes. We are now negotiating the Air Force phase II, and not the Defense Department. So I do want to clear it up. GSA, under the Brooks bill, and under a recent decision of the Comptroller General has the exclusive authority in the executive branch of the Government to buy general purpose ADP.

(See Comptroller General decision, app. 10, p. 556.)

Chairman PROXMIRE. GSA would have the authority to buy automatic data processing and computers generally for the Defense Department?

Mr. ABERSFELLER. That is correct.

Chairman PROXMIRE. So you do assume the responsibility for this difficulty that Mr. Caveney refers to?

Mr. ABERSFELLER. Indeed. And we do hope we will work this out and put it in schedule. In furtherance of Mrs. Griffiths' point—we would hope that by using the revolving fund, provided for by the Brooks bill, and by using the information provided under our management information system, be able, in the future, to identify those pieces of equipment which otherwise might not be used and update them as she suggested by the addition of more high speed peripheral equipment.

Representative GRIFFITHS. Why don't you call up the Navy and ask to borrow their people? They will lend them.

Mr. ABERSFELLER. I am not too sure at the moment any people are necessary. I simply do not know how complicated this matter is at the moment.

Mr. CAVENEY. Mr. Chairman—

Chairman PROXMIRE. Mr. Caveney.

Mr. CAVENEY. Now, the statement here—granted he might have the prerogative of these big systems. But then I have a question. If this is true, I would like to know why the Government then sends all the RFQ's to the computer manufacturer and why we must go through the computer manufacturer, not direct to the Government.

Chairman PROXMIRE. Why is that, Mr. Abersfeller?

Mr. ABERSFELLER. Only because Mr. Caveney's firm is not on the Federal Supply Schedule. Generally only those firms who are on the schedule are invited to bid.

Representative GRIFFITHS. Are those people on the schedule the people who make or assemble the total computer system? Are those the only people on the schedule?

Mr. ABERSFELLER. At the moment, other than the 40 accessorial and periphery manufacturers—the other people on the schedule are the original equipment manufacturers.

Mr. CAVENEY. Then I have a followup question. If this is true, how can we get requests for quotes from CDC, Defense, Lytton Industries, RCA—

Chairman PROXMIRE. You say you are on the schedule?

Mr. CAVENEY. We are not on their schedule. But we get RFQ's on the programs via the computer manufacturer.

Chairman PROXMIRE. It sounds to me—and again I do not want to be abrupt—it sounds to me, Mr. Caveney, as if you can get together with Mr. Abersfeller and solve the problem. I am sure you are not interested simply in yourself. You say you are testifying for other peripheral manufacturers, you want to see that justice is done generally, and that the Federal Government saves money.

Mr. CAVENEY. That is correct.

Chairman PROXMIRE. So I think this is a broader question than simply satisfying Mr. Caveney his particular company's problem.

What steps are taken, Mr. Abersfeller, to see that the Defense Department has as comprehensive and full a listing of qualified suppliers

in the computer area, peripheral computer area, as there is? Isn't there a responsibility to make sure that the Federal Government knows virtually all of the manufacturers? After all, if there are 50, this is not an infinite number.

Mr. ABERSFELLER. The steps that are taken generally start with the request that a firm be placed on the Federal Supply Schedule.

Chairman PROXMIRE. And that is initiated by the firm?

Mr. ABERSFELLER. Yes, sir. Or sometimes on our part. In this particular case, I talked to Mr. Caveney last night—he did not call me. I asked him to come down to see whether or not we could not negotiate on the schedule—because after it came up yesterday, I checked with my staff and found that the firm had been in some time ago to discuss it, but we had not completed a negotiation, nor had an application been sent in. As soon as he comes in, I am fully convinced—presuming we can arrive at price—and from what he says, we sure can, because it is less costly—that we will be able to place his products on the schedule. It does not seem to be any problem.

I have looked at the list of the 50 manufacturers, and if my recollection serves me properly, Mr. Chairman, some of these people are on contract now with us. But certainly his firm is not.

Chairman PROXMIRE. Why would it not be a good idea to get in touch—write each one of these firms?

Mr. ABERSFELLER. It is an excellent idea, and we shall do so.

Mr. CAVENEY. Mr. Chairman—

Chairman PROXMIRE. Mrs. Griffiths wanted to say something.

Representative GRIFFITHS. Do you know the price that the total manufacturer of computer systems pays any of these peripheral people?

Mr. ABERSFELLER. I do not.

Representative GRIFFITHS. Why not?

Mr. ABERSFELLER. Well, this goes back to the Truth in Negotiations Act. If the product is sold commercially in substantial quantities there is no requirement—in fact there is an exception from the cost and pricing data requirements.

Representative GRIFFITHS. And the Defense Department, the GSA have fought getting it. That is why you have not got it.

Let me point out to you that what you are now doing in the Truth in Negotiation Act is after the purchase has been made, you are looking at a breakdown of costs that shows you labor and overhead and so forth and so on.

Supposing one of these peripheral manufacturers items is marked up 100 percent—and in my judgment, I think you are going to find it is pretty close to it. How can you justify that in a breakdown of costs? Where are they putting that cost?

Mr. ABERSFELLER. If the information were made available to you, then obviously it could not be justified. We are having some difficulty—

Representative GRIFFITHS. Why don't you demand it be available?

Mr. ABERSFELLER. To be very candid about it, there are occasions where we have demanded it and it has been refused.

Representative GRIFFITHS. If you support my bill, you will never be refused again. They are going to supply it.

Mr. ABERSFELLER. I am referring now to the current legislation that exists in the Truth in Negotiations Act where there is a requirement to provide cost and pricing data under certain circumstances and there have been recent occasions where companies have refused to provide the information.

Representative GRIFFITHS. I am sure they have. And they have also called up from the west coast, particularly the aircraft manufacturers, and objected seriously to supplying any such information, and the Defense Department has gone right along with them.

The best testimony we have ever had is that four people in a private industry can keep track of the price of 90,000 parts. The testimony of the Army yesterday, of the Defense Department yesterday, was that it would take 10,000 people to keep track of these things.

Now, anybody who knows anything knows that is silly.

Chairman PROXMIRE. Furthermore, isn't it true that to put the big computer manufacturers into the mood to reveal this information, you have to have more competition. As I understand it now, they have the whip hand, and they can refuse it, because they do not have to bid, and the Government may be in a position where they are pretty desperate. There are a few of them, and some of them are very big, and the competition is not as good as it ought to be.

On the other hand, if you can break the components out and provide more opportunity for the so-called peripherals, so that you can put these things together, you might be in a stronger position to insist that they give this information, or lose a very valuable sale to the Government.

Mr. ABERSFELLER. It certainly is a possibility. But unfortunately in some cases, as you point out, Mr. Chairman, these are first-of-a-kind types, but they are also in the commercial line of a particular company, and apparently the company has other commercial customers standing in line—yet the Government needs this particular computer desperately, and it is the only one that is known that can do the particular job. The companies do in fact have the whip hand and the Government then has no alternative but to procure the equipment.

Chairman PROXMIRE. Thank you very very much. I appreciate this. Mr. Caveney, you have been a most valuable witness.

Representative GRIFFITHS. I want to say one more thing.

I would like to point out that during these hearings—and I want to thank the chairman for holding them, because I think we have saved the country money—during these hearings the Defense Department has acted as if Congressman Pike, who reveals some astonishingly high prices on some shelf items, had found the only four or five such items that were overpriced that are purchased by the Defense Department. Now, today we hear that the GSA, after having heard the testimony yesterday, has decided it is possible they could buy some of this stuff differently and save some money. This committee ought to sit here all the time, going over these purchases. We would probably save more money for the Government than any other thing that could be done.

But the horrible thing is that—and any taxpayer must know—that it is like opening a catalog and just pushing your finger down like that, and you find out that the item you have is being overpriced—the Government is paying too much money. We are not going through this item by item.

Mr. CAVENEY. Mr. Chairman, in this regard—not speaking as a member of my company, but as a citizen of the United States—I am involved in what you call spare parts documentation. I sit and listen and advise the Government on what they should buy in the form of spare parts. Then they will turn around and buy it anyway, the ones I feel they should not buy, because they cannot do anything with it, except let it set on a shelf and acquire dust. And they are either procured because they are following some hidden regulation or the prime contractor wants to get as many spare parts on the list as he can, which is obvious, because of handling charges and a small profit. And this area of spare parts in itself is one of the largest wastes in Government.

Representative GRIFFITHS. Of course, it is.

Chairman PROXMIRE. Very good.

Once again, thank you so much, Mr. Caveney, for a very stimulating and useful, and, as Mrs. Griffiths has said so well, information that will help us save a substantial amount of money.

Our second witness is the Honorable Phillip S. Hughes, Deputy Director of the Bureau of the Budget. A letter of November 8 of this year which covers the subjects upon which we asked Mr. Hughes' testimony will be incorporated in the record at this point.

(The document to be furnished for the record follows:)

NOVEMBER 8, 1967.

HON. CHARLES L. SCHULTZE,
Director, Bureau of the Budget,
Washington, D.C.

DEAR CHARLIE: Your staff has been informally advised that the Subcommittee on Economy in Government of the Joint Economic Committee will hold follow-up or review hearings on the recommendations and conclusions contained in this report of July, 1967. This letter confirms that the hearings will be held from November 27-30, 1967, Room AE-1, The Capitol, Joint Atomic Energy Committee Hearing Room, and you and your associates are scheduled to appear on November 30, 10:00 A.M.

Please forward 100 copies of your prepared statement at least one day prior to the date of your appearance. If any additional information is desired please call Mr. Ray Ward, Staff Consultant, Code 173, Ext. 8169.

There are four main topics which we wish to cover in some detail during hearings:

1. Development in compliance with the "Truth-in-Negotiations Act" by the DoD and other agencies, including BoB participation.

2. Improvements in supply management in the U.S. and abroad. This will include procurement practices—Buy American, competitive versus negotiation, development of a National Supply System, procurement and management of Automatic Data Processing Equipment, etc.

3. Adequacy of management of Government-owned equipment furnished to contractors.

4. Progress in implementing Budget Bureau Circular No. A-76, revised, concerning the furnishing of material and services for Government use. An analysis of amendments included in A-76 revised would be helpful.

A status report on real property management under Circular A-2, revised is desirable. We also wish a statement on "the adequacy of the GSA's capability and efforts in behalf of the Government as a user of utilities," as recommended on page 16 of the July, 1967 report.

Sincerely yours,

WILLIAM PROXMIRE,
U.S. Senator.

Chairman PROXMIRE. Your statement is quite short, Mr. Hughes, so we may wish to ask questions as you proceed. Please introduce your associates for the record.

**STATEMENT OF HON. PHILLIP S. HUGHES, DEPUTY DIRECTOR OF
THE BUREAU OF THE BUDGET; ACCOMPANIED BY TIM RUSSELL,
OFFICE OF EXECUTIVE MANAGEMENT; JOE CUNNINGHAM, GOV-
ERNMENT MANAGEMENT DIVISION**

Mr. HUGHES. Mr. Chairman, with me, on my right, is Mr. Tim Russell, of our Office of Executive Management, who is concerned with Circular A-76, "Competition With Business." On my left, Mr. Joe Cunningham, Assistant Director of our Government Management Division, who is concerned with ADP matters.

Chairman PROXMIRE. All right.

Mr. HUGHES. Mr. Chairman and members of the committee, we welcome the opportunity afforded by your November 8, 1967, request to appear and discuss six areas in which the subcommittee expressed a particular interest and concern. They are:

1. Developments in compliance with the "Truth in Negotiations Act."
2. Improvements in supply management.
3. Adequacy of management of Government-owned equipment furnished to contractors.
4. Budget Bureau Circular No. A-76, Revised, concerning Government competition with business.
5. A status report on real property management under Budget Bureau Circular No. A-2, Revised.
6. The adequacy of the General Services Administration capability and efforts in behalf of the Government as a user of utilities.

Our general budget and management improvement interests make all of these areas of interest and concern to us, and in several we have very specific responsibilities. In this statement, which we hope will be of help to the committee, we have attempted to supplement rather than duplicate the testimony of other witnesses who have appeared earlier and discussed some of these subjects at length.

DEVELOPMENTS CONCERNING TRUTH IN NEGOTIATIONS ACT

During the hearings last May, the subcommittee requested that we give particular attention to a General Accounting Office report to the Congress critical of the way the Department of Defense was administering Public Law 87-653, the Truth in Negotiations Act.

The law, which is implemented in the Armed Services Procurement Regulations, requires contractors to certify to the accuracy, currency, and completeness of cost data which they furnish to the Government during the negotiation of a cost-reimbursable-type contract. In its report to the Congress, GAO cited a number of contracts in which, in its view, there was inadequate cost data to support compliance with the act.

Looking into the matter, we found and reported to the subcommittee by letter of July 19, 1967, that DOD had initiated actions to improve its management in this area of contracting, and that in these efforts a close working relationship had been established between the staffs of GAO and DOD. The committee has heard extensive testimony on this in the last 3 days.

The outcome of the DOD-GAO work has been the development of various changes in the Armed Services Procurement Regulations. Generally these new provisions are designed to revise current criteria for determining when adequate price competition exists, to clarify and strengthen the procedure for identification and retention of cost and pricing data in the contract files, and to broaden the scope of post-audit coverage of cost data. In addition, a comprehensive personnel training program has been developed for those involved with the administration of Public Law 87-653.

We believe this joint GAO-Defense effort is the approach most likely to assure well-conceived regulations and procedures, which are the basis for improvements in procurement operations. Ultimate success will necessarily depend upon the effectiveness of internal administration within DOD, requiring proper selection and training of personnel; competent supervision and leadership; maintaining a high capability among procurement people at the working level; and constant testing and refinement of regulations and practices as operational experience is gained. DOD has taken steps to improve internal administration in all these respects. We believe DOD's actions indicate that it is fully aware of the importance of administrative improvements in meeting the objective of obtaining adequate documentation of cost data to clarify the backup records in contract actions.

In summary, our investigation and our discussions with officials of GAO and the Department of Defense since the May hearings indicate that substantial progress has been made. A period of operational testing will be necessary to assure that desired results are being achieved. During this operational period, we are confident that continued cooperation and exchange of views between GAO and the Department of Defense will contribute to further improvements. The Bureau of the Budget will maintain its interest in the matter and be of whatever help it can in overcoming the problems cited by the GAO.

Chairman PROXMIRE. Do you have anything specific in mind in this regard?

What occurs to me is that today is precisely 5 years after the Truth in Negotiations Act was passed. It is 20 years after Public Law 413, the Armed Services Procurement Act, was enacted. We have spent some \$370 billion by negotiation in procurement. The loopholes or the failure to administer effectively the Truth in Negotiations Act have been most conspicuous.

So I think this report is reassuring, very helpful.

I certainly do not blame you, Mr. Hughes. You have not been there for 20 years. At least I do not think you have—not in your present position of responsibility.

Mr. HUGHES. That is right.

Chairman PROXMIRE. But I do hope that you can demand regular and detailed reports, and have a system of followup, so you are sure that the Truth in Negotiations Act is being fully implemented, and there is a full awareness in every respect of the costs of the contractors in negotiations—because this is the only real safeguard for the Government and for the taxpayer.

Mr. HUGHES. Mr. Chairman, our handle in these matters is the budget process, quite obviously. We plan with respect to the 1969

budget, as well as future budgets, to use this tool, this handle, if you will, to follow closely the actions by Defense to carry out the act. And, we will, as I have indicated here, maintain our interest and concern with it, and do what we can to see it is carried out.

Chairman PROXMIRE. One of the things that interested me was to find out how fully trained the procurement officials are, whether or not they have been tested and comprehensively tested so they understand the provisions of the law which requires the Truth in Negotiations Act to be fulfilled, and whether the auditing has been fully executed which is provided by the Nitze order—that kind of thing. And, it seems to me, if the Budget Bureau does not do this on a systematic basis—you have the staff and responsibility—it is unlikely to be done at all by anyone.

This committee has so many responsibilities, and so do the Government Operations Committees of the House and Senate—that we may spasmodically and occasionally get into this. But we have to rely on your steady and constant surveillance.

Mr. HUGHES. We will certainly try and do our part, Mr. Chairman. I think the GAO has given ample evidence of its own interest and continuing concern and will also be very important in following through on this.

Chairman PROXMIRE. OK. Go ahead.

IMPROVEMENTS IN SUPPLY MANAGEMENT

Mr. HUGHES. As we noted in our statement last May, the creation of a national supply system has continued to progress even though the Nation's military requirements have placed increasing demands on supply operations. As scheduled on July 1, 1967, GSA assumed Government-wide support responsibility for 52 Federal supply classes, which brings to 65 the total supply classes for which GSA will provide primary management. GSA also is considering assumption of responsibility for additional classes.

The assumption by Defense Supply Agency of Government-wide support responsibility for fuel has been delayed because of staff limitation in connection with fiscal year 1968 appropriations. The initiation of the first phase of its Government-wide responsibility for fuel, which was scheduled for January 1968, is now scheduled for July 1, 1968. This is also the date scheduled for DSA to assume Government-wide support for electronics which will be phased in over a 12-month period. We will work with the agencies concerned to effect the transfer of resources as required to carry out these plans.

The utilization of long supply items was strengthened by new GSA regulations which include guidelines for determining when items in long supply should be made available for utilization by other agencies in lieu of new procurement.

Chairman PROXMIRE. What was the date of that? You can supply it for the record.

Mr. HUGHES. I will, Mr. Chairman. I am sorry I do not have it. (The information to be furnished for the record follows:)

FEDERAL PROPERTY MANAGEMENT REGULATIONS

(amendment E-38, September 1967)

SUBPART 101-27.3—MAXIMIZING USE OF INVENTORIES

§ 101-27.300 *Scope.*

This subpart prescribes policy and procedures to assure maximum use of inventories based upon recognized economic limitations.

§ 101-27.301 *Definitions.*

As used in this Subpart 101-27.3, the following terms have the meanings set forth below:

(a) "Long supply" means that increment of inventory which exceeds the stock level criteria established by the inventory manager, but excludes quantities to be declared excess.

(b) "Centrally managed item" means an item of supply or equipment which forms part of an inventory of an agency performing a mission of storage and distribution to other Government activities (e.g., GSA and DSA).

(c) "Agency managed item" means an item which is procured and forms a part of a controlled inventory of an agency and its activities for issue internally for its own use and is other than a centrally managed item.

(d) "Economic retention limit" means the maximum stock quantity on hand of an item which may be held without incurring greater costs for carrying the stock than for the costs of its disposal and resulting loss of investment.

§ 101-27.302 *Applicability.*

The provisions of this subpart are applicable to all civil executive agencies.

§ 101-27.303 *Reducing long supply.*

Through effective interagency matching of material and requirements before the material becomes excess, unnecessary procurements and investment losses can be reduced. Timely action is required to reduce inventories to their normal stock levels by curtailing procurement and by utilizing and redistributing long supply. In this connection, requirements for agency managed items should be obtained, from long supply inventories offered by agencies in lieu of procurement, from commercial sources. Since supply requirements usually fluctuate over a period of time, a long supply quantity which is 10 percent or less of the total stock of the item is considered marginal and need not be reduced.

§ 101-27.303-1 *Cancellation or transfer.*

When the long supply of an item, including quantities due in from procurement, is greater than 10 percent of the total stock of that item, the inventory manager, or other appropriate official, shall cancel or curtail any outstanding requisitions or procurements on which award has not been made for such items, and may also cancel contracts for such items (if penalty charges would not be incurred) or transfer the long supply, if economical, to other offices within the agency in accordance with agency utilization procedures. In such cases, acquisition of long supply items shall not be made from other sources such as requirements contracts.

§ 101-27.303-2 *Redistribution.*

If the long supply is still greater than 10 percent of the total stock of an item despite efforts to cancel or transfer the long supply as provided in § 101-27.303-1, the inventory manager shall:

(a) Offer centrally managed items to the agency managing the item for return and credit in accordance with the procedures established by that agency; and

(b) Offer agency managed items to other agencies which manage the same item. Reimbursement shall be arranged by the agencies effecting the inventory transfer. The responsibility of locating agencies or activities requiring these items shall rest with the agency holding the long supply. However, agencies may receive a list of Government activities using particular Federal stock numbers by writing to:

General Services Administration, Federal Supply Service, Standardization Division—FMS, Washington, D.C. 20406.

§ 101-27.304 *Criteria for economic retention limits.*

If, after taking action as provided in § 101-27.303-2, the quantity of an item in long supply is still greater than 10 percent of the total stock for the item, the inventory manager shall establish an economic retention limit for the item in accordance with the provisions of this § 101-27.304. The economic retention limit shall be used to determine which portion of the inventory may be economically retained and which portion should be disposed of as excess.

§ 101-27.304-1 *Establishment of economic retention limit.*

An economic retention limit must be established for inventories so that the Government will not incur any more than the minimum necessary costs to provide stock of an item at the time it is required. Generally, it would be more economical to dispose of stock in excess of the limit and procure stock again at a future time when the need is more proximate rather than incur the cumulative carrying costs.

(a) The agency managing a centrally managed or agency managed item shall establish an economic retention limit so that the total cumulative cost of carrying a stock of the item (including interest on the capital that is tied up in the accumulated carrying costs) will be no greater than the reacquisition cost of the stock (including the procurement or order cost). Consideration should be given to any significant net return that might be realized from present disposal of the stock. Where no information has been issued, the net return from disposal is assumed to be zero. Guidelines for setting stock retention limits are provided in the following table and explanatory remarks that follow:

Annual carrying costs as a percentage of item reacquisition costs	Economic retention limit in years of supply		
	Net return on disposal as a percentage of item reacquisition costs		
	0	10	20
10.....	8½	7½	6½
15.....	6	5½	4½
20.....	4¾	4¾	3¾
25.....	3¾	3½	3

NOTE: The entries in the tables were calculated by determining how long an item must be carried in inventory before the total cumulative carrying costs (including interest on the additional funds that would be tied up in the accumulated annual carrying costs) would exceed the acquisition costs of the stock at that time (reacquisition costs). For example, assuming no net return from disposal, the accumulated carrying costs computed at the rate of 15 percent per year on the reacquisition cost of the stock and compounded annually at 4½ percent (GSA's recommended rate of interest on Government investments) would be:

Years	Compounded carrying cost as a percentage of reacquisition costs	Accumulated costs as a percentage of reacquisition costs
1.....	15.7	15.7
2.....	16.4	32.1
3.....	17.1	49.2
4.....	17.9	67.1
5.....	18.7	85.8
6.....	19.5	105.3

At 15 percent a year, accumulated carrying costs would be equivalent to the reacquisition costs after 6 years. Six years is, therefore, the economic retention limit for items with a 15 percent annual carrying cost rate. Where an activity has not yet established an estimate of its carrying cost, an annual rate of 10 percent may be used as an interim rate thereby resulting in an economic retention limit of 8½ years when the net return on disposal is zero. The elements

of carrying (holding) cost are given in the GSA Handbook, The Economic Order Quantity Principle and Applications. The handbook is identified under Federal Stock Number 7610-543-6765 in the GSA Stock Catalog, Part I, and may be ordered in the same manner as other items in the catalog.

(b) The economic retention limit at a user stocking activity can best be determined by the item manager (for centrally managed or agency managed items) on the basis of overall Government requirements and planned procurement. Since stocks in long supply at a user stocking activity are less likely to find utilization outlets, the retention limit at these activities should be relatively small. Generally the economic retention limit at a user stocking activity should be computed in the same manner as in paragraph (a) of this section and then reduced by 70 percent.

§ 101-27.304-2 *Factor affecting the economic retention limit.*

(a) The economic retention limit may be increased where:

(1) The item is of special manufacture and relates to an end item of equipment which is expected to be in use beyond the economic retention time limit; or

(2) Costs incident to holding an additional quantity are insignificant and obsolescence and deterioration of an item are unlikely.

(b) The economic retention limit should be reduced under the following conditions:

(1) The related end item of equipment is being phased out or an interchangeable item is available; or

(2) The item has limited storage life, is likely to become obsolete, or the age and condition of the item does not justify the full retention limit.

§ 101-27.305 *Disposition of long supply.*

Where efforts to reduce the inventory below the economic retention limit have been unsuccessful, appropriate disposition should be effected in accordance with Subpart 101-43.3 of this chapter. Any remaining inventory which is within the economic retention limit shall be retained. However, the item shall be reviewed at least annually and efforts made to reduce the long supply inventory in accordance with § 101-27.303.

Mr. HUGHES. This will enable civilian agencies to effect savings like those the Department of Defense has achieved through its facility at Battle Creek, Mich. However, a fully coordinated system will not develop as rapidly as we had hoped because of different procedures and different degrees of mechanization of supply records among the civilian agencies.

Chairman PROXMIRE. I understand the GAO has told us they do not think full use has been made of the DLSC at Battle Creek in this respect. (See app. 1, p. 397.)

Mr. HUGHES. I am not familiar with the comment. I thought that there was general agreement between GAO and the Department of Defense on the progress that was being made. I am not familiar with the comment you mentioned.

Chairman PROXMIRE. You go ahead. We will come back to that.

Mr. HUGHES. All right, sir.

With respect to short-shelf-life items of supply, we have responded favorably to the requests for our views on S. 1717 and H.R. 645 which were introduced by Chairman Proxmire and Mrs. Griffiths to insure utilization of medical materials and supplies before they reach the end of their useful life. We believe this legislation, together with the actions which the GSA and the Department of Defense have reported to you, should provide the means to reduce to a minimum losses from the deterioration of stocks which have limited shelf life. (See p. 270.)

MANAGEMENT AND ACQUISITION OF AUTOMATIC DATA PROCESSING EQUIPMENT

In June of this year, the House Government Operations Subcommittee held extensive hearings on the management of automatic data processing equipment. At that time, we reported on the progress being made in the implementation of Public Law 89-306 which provided for a coordinated, Government-wide approach toward improving the procurement and utilization of this equipment.

A basic requirement for strengthening this program has been the need for more comprehensive and current information which would enable us to manage our inventory more effectively.

COMPLETE INVENTORY OF ADPE NEEDED

Chairman PROXMIRE. Does this mean we do not have an inventory of this valuable equipment?

Mr. HUGHES. We have not to date had a complete inventory of equipment in the Government. This is a massive problem, Mr. Chairman, which Mr. Cunningham can talk to more effectively than I, in simply defining what is a computer, what is automatic data processing equipment, and where the lines are drawn between various types of equipment.

Chairman PROXMIRE. So, we do not know what we have.

Mr. CUNNINGHAM. That is not correct, sir. We do have an inventory of computers in the Federal Government; but, it is an inventory of total computer systems. The new information system which has been set up—and the inputs to it are now being processed—is an inventory by component, for each computer. This new inventory is to be maintained on a perpetual basis. It will give us a basis for planning actions, et cetera. We have had, until now, an inventory of the total number of computers, and their total operating cost. We have not had the specifics of the ingredients which made up the various computer systems. We have not had it broken down into detail so you could tell how many various components there are.

It is a brandnew system and with its newness, we are having some difficulty. But, I would hope, within a month or so, we will be operating on a permanent basis.

INVENTORY TO BE COMPLETED IN A MONTH

Chairman PROXMIRE. So you will have an inventory in a month?

Mr. CUNNINGHAM. Oh, yes. As a matter of fact, we have portions of it now.

Mr. HUGHES. I think as somewhat of an aside, Mr. Chairman, some of the problems here, and some of the problems that Mr. Caveney and Mrs. Griffiths were talking about, relate to the question of what is a computer, what the components are, and how complex does the equipment have to get to be counted. And, for these reasons, a numerical count by itself, without the kinds of classifications to which Mr. Cunningham referred, is not real useful. This relates, I think, to Mr. Caveney's problem of which kinds of components can simply be plugged together and which have to be wired together in highly com-

plex and technical fashion in order for them to function as a part of a complete whole.

This information system will provide the basic information necessary in our efforts to improve our contracting and procurement processes, increase the utilization of existing equipment, and extend the redistribution of excess equipment. It will also enable us to evaluate more closely the impact of our Government-wide policies, including those relating to the purchase versus lease of equipment.

GOVERNMENT OWNS ABOUT 50 PERCENT OF INSTALLED COMPUTERS

In this latter connection, the Government now owns outright about 50 percent of the more than 3,000 computers currently installed, compared to only about 21 percent in 1963.

We have also revised our applicable circular, A-54, to improve Government-wide policies on the acquisition of computers. June 1967 amendments to the circular specifically require Federal agencies to give full consideration to the sharing of computers installed within the Federal Government as well as to the use of excess equipment before taking any action to procure additional computers on the open market.

Conversely, agencies are prohibited from retaining displaced equipment for other purposes unless properly justified. Also, we have specified that the cost of money will be taken into account when considering the question of whether computers should be purchased or leased. Finally, we have clarified and reaffirmed the application of these policies to Government cost-reimbursement-type contractors.

AUTHORITIES OF BOB AND GSA

Chairman PROXMIRE. Can you take a minute to indicate to us the distinction between the Bureau of the Budget authority and the GSA authority over computers?

Mr. HUGHES. Essentially, Mr. Chairman—and again I would like to ask Mr. Cunningham to comment further—essentially the Bureau of the Budget is concerned with the division of responsibility as between the agency, the General Services Administration, the Bureau of Standards, and the Bureau of the Budget, all of which have roles in this. The Bureau of the Budget, with a general policy guidance responsibility, the General Services Administration, with a procurement responsibility in the computer area—and the Bureau of Standards, with a technical responsibility in terms of standards, programing and software, and the engineering of computer systems as the Government is involved in them.

Chairman PROXMIRE. Thank you.

PROGRESS IN COMPUTER STANDARDIZATION

Mr. HUGHES. Steady progress continues in the effort to achieve a greater measure of standardization among computers and related software. We expect to announce very soon the adoption of Federal standards for a coded character set and for magnetic tape and punched paper tape. These standards, initially approved for voluntary use by the USA Standards Institute, represent a significant step toward

eliminating costly and inefficient conversion processes, and pave the way for action in other areas where standards are needed.

STANDARDS FOR DATA ELEMENTS AND CODES

Complementing the work to develop computer and software standards is the program just recently established by BOB Circular No. A-86, to develop standards for data elements and codes that are commonly used by Federal agencies. The differences that currently exist in these data prevent their reliable exchange and summarization without engaging in difficult and expensive translation procedures. Through a Government-wide cooperative effort, we hope to minimize these difficulties by bringing about a greater degree of consistency in the way common data is described and coded.

BUY AMERICAN PRACTICES

We have again reviewed the effects of procurement under the Buy American Act by the DOD and civilian agencies. Our review indicates that the balance-of-payments savings gained from using the 50-percent differential in civilian agencies instead of 6-12 percent, would almost surely be more than offset by retaliation from foreign governments.

While the procurement practices of some foreign governments leave much to be desired, foreign government procurement in the United States far exceeds U.S. Government procurement of foreign goods. Millions of dollars of goods now purchased from the United States could be purchased domestically or elsewhere by foreign governments if there were an escalation of restrictive Government procurement practice.

Furthermore, a movement now, toward a more restrictive buy American policy would tend to disrupt our efforts in the Organization for Economic Cooperation and Development to harmonize Government procurement procedure and limit unfair discrimination to the fullest extent possible, and generally to abandon any prospect of improving the conditions of Government procurement. Clearly, it is in the U.S. interest to continue this effort to open up, through more open competition, a potentially large foreign market for American manufacturers. On the other hand, we do not believe the position of the U.S. balance of payments which caused the DOD to introduce a temporary 50-percent differential in favor of U.S. products in its procurement yet permits a change in that policy.

Chairman PROXMIRE. Yesterday we had testimony by Senator Edward Brooke, very able testimony, in which he complained about the discrimination against handtools. He pointed out 90 percent of the handtools are used by the Defense Department, but because they are procured by GSA, the differential in favor of buying domestically, instead of from a foreign source, is only 6 percent, or, with small business, 12 percent; whereas, if you could recognize the procurement by the Defense Department, the differential would be 50 percent. And, it seemed to us a very, very logical argument. The questioning yesterday seemed to suggest that this was something that the Budget, Bu-

reau of the Budget, would be in the best position to help resolve. What would be your comment on that? (See app. 9, p. 550.)

Mr. HUGHES. Well, certainly, Mr. Chairman, first an initial comment should be an acknowledgment that the situation is difficult—with two different differentials. I don't see any use in trying to evade that rather fundamental point.

MESS DUE TO SEPARATE DOD POLICY

Chairman PROXMIRE. This is a mess that the administration created by enabling the Defense Department to issue this directive providing for a 50-percent differential, and with a very real concern about our balance of payments, and perhaps it was good judgment on the part of Secretary McNamara who initiated it.

Mr. HUGHES. Secretary McNamara's action was part of a general defense related effort to reduce the impact of our very extensive defense and particularly oversea defense activities on our balance-of-payments problem. The 50-percent action was taken in that context. It seems to me it makes sense in that context.

The fact that GSA procurement of handtools, for example, for defense purposes results in a different kind of Buy American standard being applied should be evaluated almost case by case, and perhaps industry by industry, in terms of the effect of that practice on the particular industry.

I have had some opportunity to see Senator Brooke's testimony, and I think I can understand his concern with the handtool industry particularly. But I think it is somewhat relevant to look at the figures for handtool procurement in total—I am speaking of GSA procurement—something of the magnitude of \$107 million worth of handtools were procured by GSA, and of that total, under \$5 million represented foreign procurement.

The point I am making here, Senator, is that—

INCREASE OF HANDTOOL IMPORTS FROM 1948-1966 FROM \$169,000 TO \$14 MILLION

Chairman PROXMIRE. Let me read what Senator Brooke said:

In 1948, the value of all mechanics hand service tools imported into the United States was \$169,000. By 1966 the value increased to \$14 million.

This indicates an enormous increase in import. And you are saying \$5 million of this was the Defense Department procurement?

Mr. HUGHES. Was GSA procurement for Government-wide use?

Chairman PROXMIRE. So that it does represent a very large proportion of all of the import, and it does represent roughly—a little less than 5 percent of the handtool procurement; is that correct?

Mr. HUGHES. About 5 percent, roughly—somewhat less than 5 percent of the Government's handtool procurement.

I think the portion of the total handtool procurement may be somewhat less. The figures which we have indicate that total handtool imports for all purposes might be more in the magnitude of perhaps \$50 million than the smaller figure which Senator Brooke cited, but I cannot certify to that figure. (See app. 9, p. 553.)

The significant points are:

First of all, the Federal Government's procurement of handtools from foreign sources is still a very small proportion of the total procurement. And second, I think we need to keep in mind the rather fundamental fact that the United States sells much more to foreign governments than this Government buys overseas. Therefore, we run a significant risk of losing more than we gain, although not necessarily in the handtool area.

Chairman PROXMIRE. I think we are more or less inclined to favor free trade. But we have to look at the very grim short-term problem, especially in terms of the British devaluation, and the persistent adverse balance of payments. We have had this 50-percent differential for a long time.

How much actual retaliation have we suffered during this period?

Mr. HUGHES. I do not know, Mr. Chairman. Certainly, the volume of foreign procurement here remains high, both in terms of foreign government procurement and as reflected in the fact that our exports far exceed our imports—

Chairman PROXMIRE. We have had it several years.

Mr. HUGHES. Oh, yes; several years. It was introduced and so labeled in the Armed Services Procurement Regulation as a temporary measure in recognition of a balance-of-payments problem.

Chairman PROXMIRE. Which is as bad now as it has been.

Mr. HUGHES. That is correct.

Chairman PROXMIRE. And, more critical this month than it probably has been at any time.

Mr. HUGHES. It certainly is a difficult period. And, it seemed to us, certainly no time to back away from the 50 percent on the defense side. On the other hand—

Chairman PROXMIRE. Under these circumstances, you see, a handtool industry, which does seem to suffer this discrimination—what criteria or standard can you apply if you do not permit them to have the 50-percent differential, when the overwhelming amount of the procurement is by or for defense?

Mr. HUGHES. The criterion is applicable to the procuring agency which in this instance is GSA. I think, again, in appraising the impact of the differential, it is important to look at the figures I have cited, to look at the figures reflecting the growth of the handtool industry in general, and to look at the continued small portion of imports in relation to total domestic use of handtools.

I think it is fair to estimate, also, that of the \$4.8 million of foreign procurement by GSA out of this total of roughly \$108 million, some substantial proportion would probably stay foreign, even with a 50-percent differential.

So that the margin here, that we are talking about, between these two differentials insofar as the handtool industry is affected, is something under the \$4.8. I do not know what the figure is.

Chairman PROXMIRE. Under the \$4.8 million.

Mr. HUGHES. \$4.8 million is procured foreign under the 6 to 12 differential. Even if that differential were increased to 50 percent, there would continue to be significant foreign procurement.

Chairman PROXMIRE. Could you do this—as a courtesy to the committee—could you get all the data that you can get on the handtool industry for us?

Mr. HUGHES. Surely.

Chairman PROXMIRE. And, could you then perhaps talk with Senator Brooke about this situation, because he has this very, very deep concern. And indicate to us the basis for this particular treatment of handtools as compared with other industries, which must have a similar problem, and which must be in a position of taking advantage of the situation.

Mr. HUGHES. Yes, sir. I think the dictaphone industry is another similar situation. We will do that, Mr. Chairman. And we will reflect in the data and the comments we give to you the results of our conversations with the Senator.

Chairman PROXMIRE. Very good.

(The information subsequently furnished is in app. 9, p. 550.)

THE MANAGEMENT OF GOVERNMENT EQUIPMENT FURNISHED TO CONTRACTORS

Mr. HUGHES. Another matter on which the subcommittee requested our comments is controls over Government property in the possession of Defense contractors. This relates to a request in the subcommittee report of May 1966 that GAO cooperate with DOD to develop an adequate contractor inventory accounting system and to review any unauthorized use of such property by contractors. Comptroller General Staats testified last May that a study had not been concluded and there was still further work to be done in cooperation with DOD. The final report on the study has now been published and GAO and DOD have both testified at length on the findings. (See app. 4 (a) and (b), pp. 411, 463.)

As you have learned, the cooperative study has produced a number of revisions in the Armed Services Procurement Regulations which are planned to be made effective in the very near future and which should tighten up existing controls considerably. These new measures will be tried out in actual working application for long enough to test whether further refinements will be needed. In any event, there seems to be no disagreement either as to legislative intent, or as to the feasibility of maintaining adequate physical and financial control of Government property, whether under contract or Federal custody. (See app. 4(a), pp. 231, 455, for DOD comments on GAO recommendations.)

Chairman PROXMIRE. This concerned the committee very greatly, as you know, from the testimony of the GAO, and from the questioning of all members of the committee.

INDIVIDUAL USE RECORDS FOR CONTRACTOR-HELD MACHINES

Do you feel that individual use records should be kept on contractor-held machines, so the Government can be fairly reimbursed?

Mr. HUGHES. It seems to me, Mr. Chairman, as a generalization; yes. It seems to me so. (See DMO 8555.1, p. 212.)

BASIS FOR EQUIPMENT CHARGES TO CONTRACTORS

Chairman PROXMIRE. The other alternative is, instead of this, you might charge the contractor for the time the machines are in his custody, the notion being there might be a tendency for the contractor to hoard these machines. After all, if he has them and is not using them, and he is charged, he might be more willing to make them available for disposal.

Mr. HUGHES. It seems to me, Mr. Chairman, that there should be selectively kept use records of equipment which is in the hands of contractors. We have not discussed this directly with Defense, or with GAO, but there is a point—and I think this is the essence of the remaining disagreement if that is the right term, between GAO and DOD—there is a point at which it ceases to pay to keep track of use, either on a use basis, or to charge, as the case might be, for the equipment.

Chairman PROXMIRE. That would be a pretty inexpensive piece of equipment.

Mr. HUGHES. Yes; an inexpensive item, or perhaps, in some instances a one-shot piece of equipment—one shot in terms of Government purpose.

Chairman PROXMIRE. But, certainly, most of the Government's \$11 billion—whatever it is—\$11 billion investment should be covered. That is, 95 percent of it should be covered.

Mr. HUGHES. It seems to us that the Government should know what the contractor is doing with its equipment.

NEED FOR GOVERNMENT TO SUPPLY EQUIPMENT

Representative GRIFFITHS. May I ask this? What real excuse is there now for the Government supplying equipment to many of these manufacturers?

Now, I would like to point out that I feel in a situation where the Government is the sole purchaser from a plant, then the Government should own the equipment, and the plant. It is nonsense to do anything else. Although the Defense Department records are replete with situations where they have permitted a sole producer for the Government to buy the plant, buy the equipment, and charge them for it.

Now, to me this is too silly to talk about. But why should we continue to be in the business of purchasing equipment, or supplying equipment to manufacturers at this point?

DOD NOT ALONE IN FURNISHING EQUIPMENT

Mr. HUGHES. Well, it seems to me there are some instances, Mrs. Griffiths, in which we might wish to do that.

Defense is, incidentally, not the only one in the business. An instance which occurs to me relates to AEC, where there are Government-owned, contractor-operated establishments.

THOMPSON RAMO WOOLDRIDGE

Representative GRIFFITHS. In those you just have to, in my opinion. The worst abuse of this that ever occurred, in my opinion, was when

General Schriever let Thompson Ramo Wooldridge build a great big office and testing lab. I think they had \$160,000 of their own money in it. The Government was the only purchaser. The total cost was \$19 million, And, after the Government had paid for it, Thompson-Ramo-Wooldridge kindly sold it back to them for \$26 million.

Now, it is possible that the Air Force does not understand money. But I think almost anybody would be smarter than that.

NEED FOR EQUITABLE CONCERN FOR COMPETITORS

However, I have talked about this before. But it seems to me that if you are going to have the equipment, and you are going to let the contractor use it on the Government property, then you are absolutely bound to keep track of it—because you are in reality subsidizing that man against his competitors. It is not only that the Government is losing money. It simply is not fair to his competitors, for the Government to be supplying the equipment.

Mr. HUGHES. If he is in a competitive enterprise, then, I think, we get away from the use and into the charge business.

LACK OF ADEQUATE USE RECORDS

Representative GRIFFITHS. But you see we have not been doing that. Nobody even knew there was any Government property around, until I asked that question about 2 or 3 years ago, and then we became quite interested. And there are billions of dollars' worth that is being used, and nobody is paying for it at all.

Mr. HUGHES. From the GAO reports, some are used for essentially private purposes.

Representative GRIFFITHS. Of course.

COMMERCIAL USE OF GOVERNMENT EQUIPMENT

Chairman PROXMIRE. It also indicates that the records are so inadequate, or so inadequately watched and observed that there is an enormous amount of private use for which no rent is ever paid. And even repeated instances of warnings—and each year they use it more and more for private use. These examples, according to Mr. Staats, were not exceptional, they were not picked to demonstrate the worst situations—they were typical. Firms would buy—get millions of dollars worth of equipment free from the Government, and use them most of the time on private commercial work.

IMPACT ON STATE AND LOCAL TAXES

Mr. Curtis raised a very appropriate if somewhat secondary problem of what does this do to the local and State governments, which rely on a property tax, and cannot tax this property. After all, \$11 billion is not just a small amount—it is an enormous amount. But it can result in great penalty for them.

Congressman Rumsfeld?

FAVORABLE POSITION OF CONTRACTOR WITH GOVERNMENT EQUIPMENT

Representative RUMSFELD. Mrs. Griffiths mentioned the problem of enabling one company in the private sector to compete favorably through a subsidy, against another company.

There is another aspect to this about which I have been concerned. I would be interested in your comment on it.

I serve on the Science and Astronautics Committee, also, and we have gotten into space program contracting over a period of years.

I worry not only that a company might be subsidized, but about this second aspect to it.

When a new contract is going to be let, the advantage of the company that has Government equipment in the submitting of a bid, of a response to a request for proposals, seems to me to be considerable, not only from the standpoint of the fact that they might be able to submit a lower price in their bid, but beyond that, there seems to be a tendency on the part of Government agencies in negotiating these contracts to say "Well, this company has the equipment, it is there physically, it does not have to be moved, it does not have to be repurchased, it does not have to be built from the bottom up for someone else, so give them the contract. And, this puts a tremendous advantage in the hands of the company that has the equipment that can be either used the way it is, or updated or changed slightly to help meet the request that is being let.

Frequently, the time element is important. The people who need whatever they are asking to be done may need it now. And so you can add a 2 or 3 or 4 or 8 or 10-month advantage sometimes, because the equipment is there.

Now, I am no procurement officer—and thank goodness—there is no job I would like less. But they have to have discretion, and they are human, and when they do have discretion, as they properly need some, they are going to be affected by all these items I have mentioned. And what happens is the executive branch of the Federal Government starts with a company, and then it builds, and it feeds on itself and its advantage. And I have seen it happen in NASA. I serve on the Government Operations Committee also, and I have been exposed to other instances there where I sense that it happens. I am not aware of a hearing held in the Congress on this subject. I have never seen a comprehensive review of it. I have never even had an opportunity to discuss it in any great depth with people, for example, in a position such as yourself, or in GAO, who are not on the firing line with respect to the letting of the contract. But I am convinced it is happening, that it is serious, and that it is creating some unfortunate imbalances in the private sector.

What are you doing about it, or do you even agree that there is a problem?

Mr. HUGHES. Certainly there is a problem, and I think there are several aspects of the problem that are somewhat separable. Some of them I think we are doing something about in a sense. Some of them are very difficult to do something about—once you get beyond the procurement, the contracting point.

First, there is the inherent advantage of the man who is on the

scene—whether he has any equipment or whatever—he is there, and he is in business, he has an advantage whether he is doing business with the Government or with private industry or what-have-you.

Mr. RUMSFELD. Yes. But, this is Government equipment we are talking about.

Mr. HUGHES. First, whether he has any Government equipment or not, if the man is on the scene and in business and known, and, so on, he is ahead. That is a very hard thing to deal with.

Now, with respect to the Government equipment—it seems to me the essential thing here is that the value of the equipment be properly factored into the bidding process. If one man has access to Government equipment and the other does not, the contracting officer has a responsibility to, in judgment terms, and in financial terms, appraise the situation. People are human, and I am sure it is not done accurately in all instances. However, I am sure, in most instances, at least an effort is made.

Mr. RUMSFELD. But there is no way you can factor in the time element. There is absolutely no way. If this procurement officer is told "We need this in a certain amount of time"—

Mr. HUGHES. This is an on-the-scene problem. The Government equipment is incidental. If the man is there with his own equipment on the scene, he is also way ahead.

Mr. RUMSFELD. That advantage is a part of the private enterprise system. I am not trying to conquer that mountain at the moment. I am talking about the one involving the taxpayer's equipment.

Mr. HUGHES. We struggle with this first problem. I would like to point out—and this is part of the small business problem, this is part of the problem Mr. Caveney was talking about this morning. IBM is on the scene. It will do it fast and—give or take reasonable margins—the end product will be pretty good. And the temptation is great, say I, as a nonprocurement officer—and I am glad I am not one, too—the temptation is great for the procurement officer to settle for IBM, and not to look further into the highways and byways of the particular procurement area.

I think it helped my understanding of Mr. Caveney's problem a little bit, in discussing it with my colleagues, to visualize the problem as somewhat similar to that of the homeowner who wants some hi-fi, and he has a choice to make as to whether he is going to buy a range of components, and either put them together himself, or get somebody to put them together, or whether he will buy a Fisher, or other final product, all fixed up in appropriate furniture fashion.

Chairman PROXMIRE. The Government ought to have more competence than the typical homeowner.

Mr. HUGHES. I think that is right. But, computers are vastly more complicated than hi-fi also. I think Mr. Abersfeller's point was that in some circumstances we can put these together ourselves, and some of these other separate components can be put together more efficiently under contract. And, in still other instances, perhaps, we must pay RCA or IBM to do it. But, the discrimination among these choices is difficult, and I make no case that we are doing it entirely right at the present time.

WHAT CRITERIA ON GOVERNMENT FURNISHING EQUIPMENT?

Chairman PROXMIRE. Could I ask—Mrs. Griffiths uncovered a very important and fundamental point we have not raised so far.

What criteria do you use when you approve the decision made in Government to provide equipment to a contractor? How do you determine that you should go out and buy a million dollar or \$6 million piece of equipment?

Mr. HUGHES. Well, first of all the basic decision would be made in the administering agency.

Chairman PROXMIRE. Do you have review of it?

Mr. HUGHES. We would review it in a budgetary sense. GSA, if it is ADP equipment—GSA would review it as the central procurement agency, and we would be responsible for arbitrating—

Chairman PROXMIRE. As a matter of policy, what would be the basis to determine whether you would buy this or whether you would not?

Mr. HUGHES. It would be a combination of cost and performance.

Representative GRIFFITHS. When the contracting officer makes this determination, he is sold a bill of goods. This is the only time that this firm will ever use the equipment—"We have no use for a piece of equipment like this. Therefore, we would appreciate it if you would buy it."

Now, if you are already producing an item and you are asked to double the amount that you are producing, you can sell this bill, too. You can say, "We cannot get this very fast. Do you have some stored someplace?"

And they will say "Yes, we do."

"OK, if you just bring in your pieces of equipment, and we will do it."

GOVERNMENT PROCUREMENT POLICY

One of the things that is wrong with the Government procurement policy is that they date back to Valley Forge. They have not been changed much, either. You still do what you once did. And in World War I, I understand when they went to the toolmakers, and asked them to change the plants over and make guns, they were told "Well, we do not need that to make these items. Could you supply it?" And they received in that war the most beautiful facility clause that ever was—it was just great—and one large company in Detroit refused ever to change it in World War II, and they got away with it. They went on the World War I facility clause.

Now, the Government ought to have sense enough to know now these arguments are not true. There isn't really anything so tremendously different about a Cincinnati grinder or a lathe or a milling machine. You just put on different jigs and fixtures—that is all you really need to buy for it, if you are going to buy them something.

So that the whole thing should be reviewed on why you do this.

Now, one of the questions we have never raised here is how many times has the Government removed the equipment from a sub's plant at the request of the primes, and put the sub out of business. And I know that they do it. I live in a town where practically any kid could become a patternmaker or a tool and diemaker. They are competent. They are the most skilled labor in the world. A big eastern contractor

came to a plant in my district one time and said, "This item has never been made, we have tried and tried, we cannot make it. Will you try?" Two men ran that plant, with a very small number of employees. They knew that those men were some of the most skilled workmen in America. They made the item. But they put in \$325,000 of their own money. When they had completed it, the big contractor came out, looked over the whole thing, said, "This is great, just wonderful." They sent out their engineers, watched it made, and then the contractor said, "However, we do not need you to make it now." And the Navy inspector picked up their machines, and sent them straight to storage. They broke them.

But I think somebody ought to look into this, too. Because I do not think this is any isolated case. The subs are taking a terrible beating; and the Government is taking a terrible beating, and some of the competitors of some of the primes are taking a terrible beating—because the Government is not looking over this stuff.

CRITERIA FOR FURNISHING EQUIPMENT

Chairman PROXMIRE. Now, your criteria, you say, are cost and performance. I presume that one very important factor would be the availability of the particular item that you want to procure. In other words, if you are having difficulty getting jet blades or getting some kind of equipment—well, jet blades is not a very good example—but some kind of exotic equipment that is new, perhaps, a refinement on a helicopter—and there are no sources around—under these circumstances I can understand why you would have to make all kinds of concessions perhaps to the only manufacturer available, and he might argue "We are not going to have any use for this kind of machine"—under those circumstances perhaps you would think it would be lower cost to buy the machine and so forth. But I should think that would be a very rare exception.

Under normal circumstance, with the vast productive resources we have, and the great versatility of American production, you would think that you would be in a position to procure without actually going into the market and setting the manufacturer up with plant and equipment.

Mr. HUGHES. I certainly agree with you, Senator. I am sure that most of the things that the Government procures in terms of volume and probably cost, are common items available from several sources at any given moment. Time may be a factor, however.

Chairman PROXMIRE. Even if they are only available from one source, I should think you would still be in a position to bargain for them to purchase their own equipment.

Mr. HUGHES. I would think so.

Chairman PROXMIRE. So that in view of the elements other than strict cost and performance, in view of the competitive element, in view of the inequity in terms of taxes and so forth, in view of the difficulty of keeping records and that kind of thing—apparent difficulty—I would think that you would very carefully reconsider this policy which seems to be so widespread, in view of the enormous amount committed—I think Mr. Morris said \$14 billion—between \$11 billion and

\$14 billion—review this and consider, as Mrs. Griffiths suggests, that it would be the rare and really exceptional case where you would actually buy equipment.

Mr. HUGHES. Buy equipment for a Government contractor to use? Chairman PROXMIRE. That is right.

Mr. HUGHES. It would seem to me that with the exception of an exotic situation like the AEC situation and some others—the need for Government purchase of equipment for contractor use should be diminishing. And, it seems to me, it is in the interest of the Government to diminish it.

Chairman PROXMIRE. If you have any records of that, that would be very helpful and useful to us. Could you get that for us? We would like to have that in the record—to find out how much the Government is buying in each of the last 5 or 6 years.

Mr. HUGHES. The trend in contractor-used Government equipment? I will see what we can do.

(For information requested, see app. 9, pp. 553, 554.)

Chairman PROXMIRE. Very good. Thank you.

COMPETITION WITH BUSINESS—CIRCULAR No. A-76

Mr. HUGHES. During the May 1967 hearings of this subcommittee, we indicated that we were then working on a revision of A-76 to reflect a number of clarifying changes recommended by the agencies. On August 30, 1967, a revised circular was issued along with a brief analysis of the changes made. With your concurrence, we would like to insert these documents in the record, together with our memorandum transmitting the revised circular to the heads of the executive departments and establishments. (See app. 13, p. 611.)

In revising the circular we had the benefit of views and suggestions from the executive agencies, the Comptroller General, and the report of this subcommittee in July 1967. In general, the changes made in the circular are for the purpose of clarifying provisions of the earlier circular and lessening the burden of work by the agencies in implementing its provisions. For example, we clarified the requirements for cost comparisons; for computation of depreciation; and for the treatment of costs that would tend to be the same for both Government and industry.

POLICY STATEMENT

There are a number of points on which the subcommittee expressed a specific interest in its July 1967 report, and we would like to comment briefly upon each of these, starting with the policy statement contained in the circular in respect to Government procurement from commercial sources.

After a great deal of consideration, we decided not to change the basic policy statement in the earlier circular. Instead, we emphasized in the transmittal memorandum the continuity of basic policy with the following statement:

There is no change in the Government's general policy of relying upon the private enterprise system to supply its needs, except where it is in the national interest for the Government to provide directly the products and services it uses.

After carefully considering the policy statements in the earlier issuances in 1955, 1957, 1959, and 1966, we believe the basic statement of policy on competition with private enterprise was, in fact has been, essentially the same through the years since the first bulletin was issued about 12 years ago.

STATE AND LOCAL TAXES

The subcommittee report also made reference to the possible inclusion in Government costs of estimated amounts for State and local taxes. The revised circular makes no change in respect to this item, but we are continuing our exploration of it. Large and growing grant-in-aid programs, and rising interest in the subject of Federal sharing of revenues with State and local governments, both indicate a need to study further the policy of excluding State and local taxes from cost comparisons. We know, however, that estimating these taxes will be difficult, and that in many, perhaps most instances, the effect of inclusion or exclusion will be small.

Mr. RUMSFELD. That last sentence bothers me.

You say it will be difficult to estimate, I cannot see, myself, why it is any more difficult than any number of other estimates which you are making. And I would be interested to know why you say the effect would be small. It is a rather substantial sum.

Mr. HUGHES. Let me try and comment—first on the difficulty of estimation. True, we can estimate anything—the question is the difficulty of estimating reasonably accurately.

The problem stems in part from the large number of local jurisdictions and consequent differences in tax practice, tax rates, and so on, and in part also from identifying through the contractor, subcontractor, and so on where the taxes actually are being paid or forgone, as the case may be.

Now, with respect to the effect of inclusion or exclusion, we are exploring this further. But except for utilities—and that is an important exception, obviously—the best data which we have seen and analyzed suggests that State and local taxes in general are less than 1 percent of costs in manufacturing, distribution or service industries.

Now, utilities are different, because of their generally large real estate holdings.

In the case of utilities, the data we have suggests that State and local taxes may approximate perhaps 5, 6 percent of total costs, in which event they may well be significant in a particular cost comparison.

Mr. RUMSFELD. Is this part of the 10 percent?

Mr. HUGHES. The 10 percent is a margin, sort of, and was, as originally contemplated, considered to include an allowance for this and other elements of potential error or oversight in the estimating process.

In addition, it was also intended to be an "edge" for private industry in making these sorts of decisions.

Let me add just one other point.

The 10 percent is not intended to be 10 percent and only 10 percent. It is rather a kind of ground rule or baseline.

Representative RUMSFELD. It came out of the air?

Mr. HUGHES. Yes, sir. It has no technical—

Representative RUMSFELD. There is no computation?

Mr. HUGHES. There is no economic basis for it. It is an order of magnitude figure to be used as a kind of rule of thumb or a baseline in appraising a particular situation.

Representative RUMSFELD. In Circular A-76 you exclude specifically the Federal taxes from individual stockholders. It says:

Including all other Federal tax revenues except social security taxes received from corporations or other business entities, but not from individual stockholders from a product or services obtained through commercial charges.

That again weights it in favor of government—just like the exclusion of State and local taxes weights it in favor of government.

Here again you would have to estimate it. But, you have company records, you have national averages.

I worry that the items you are not estimating all seem to push it in favor of government, away from the private sector.

Mr. HUGHES. Certainly the ones you have mentioned do. The 10 percent or comparable allowance was intended to compensate, perhaps to overcompensate for that.

Representative RUMSFELD. You feel that way?

Mr. HUGHES. Yes.

Representative RUMSFELD. You feel the 10 percent overcompensates?

Mr. HUGHES. Yes—from what appraising we have done of the estimates, of the specific situations that we have been exposed to. It seems to me that 10 percent is not an unreasonable guideline.

Now, as I point out here later, there are some factors which weigh against the Government doing the work directly. And, these must be thrown in. They are not factors which you can measure as you would stock dividends, perhaps, in individual cases—but the question of risk, of obsolescence, of getting in and getting out of the enterprise, and, so on—are factors which in the NASA instance, as a case in point, have led NASA to contract for many things which in other agencies have been done in-house. And, one of the questions, as you are well aware, I am sure, on the NASA side is whether we have gone too far on the contracting side.

Representative RUMSFELD. I have had the feeling, as we go over the NASA authorizations year after year, and deal with personnel limitations, is that Congress tries to exercise some control over the items in the budget dealing with personnel, and the next thing we find, they are popping up through contractor services.

Mr. HUGHES. Well, we are involved in the personnel ceiling business. We administer personnel ceilings for the Government in the Bureau of the Budget. We do our best to keep the ceiling consistent with the personal services money that goes with the budget.

Representative RUMSFELD. We deal with it, not from numbers of people, but money, of course.

Mr. HUGHES. Yes. But, in those instances where the ceilings are tighter than the money would otherwise permit, there is a tendency to drive the agency to contract out. We have tried to avoid it. I think Mr. Webb, and others on his behalf, have testified that at least, generally speaking, the ceilings are not the problem—rather that contracting out—to use that as a kind of term of art—has been a policy

of NASA's to take advantage of the flexibility, the capability that we discussed earlier, that industry has in some situations.

Chairman PROXMIRE. Go ahead.

INTEREST RATES—COST OF MONEY, GOVERNMENT AND PRIVATE

Mr. HUGHES. Another question identified in the subcommittee's report relates to interest costs—Should interest rates for cost comparison purposes be those in the private sector or the rates paid by the Government? Under provisions of the revised circular, Government costs will continue to include interest for any new or additional capital to be invested based upon the average rate of yield for long-term Treasury bonds, as shown in the current Treasury bulletin.

We believe this to be appropriate since, if the Government made the investment, this would be the rate that would actually apply. While we recognize that long-term money costs in the private sector are higher, this seems to us a differential which logically should be recognized in implementing the provisions of the circular.

Representative RUMSFELD. Isn't that a third link in this chain I have been building?

Mr. HUGHES. The cost of money is cheaper to the Government and therefore the Government costs would be lower on that account. The answer to your question is "Yes." Cheaper money tilts the scale somewhat in the Government's favor.

Representative RUMSFELD. Somewhat? It tilts it—period.

Mr. HUGHES. Yes; but the question is, When we have added up all of the components, have we made a fair comparison? That is our objective.

Representative RUMSFELD. I have mentioned two others.

Now, what is the cost of money to the Government? Is it the interest rate we are going to pay?

Mr. HUGHES. The one we are using is current long-term yield.

Chairman PROXMIRE. It is lower than you are borrowing at now; isn't it?

Mr. HUGHES. Current long-term yield.

Chairman PROXMIRE. Long-term yield.

Mr. HUGHES. Yield on long-term bonds.

Chairman PROXMIRE. What is it precisely—the coupon on long-term bonds—3¼ percent?

Mr. HUGHES. Not the coupon. It is the average long-term yield—would be a composite of current rates and old rates and would be below current rates. I think the average yield would be above 4 percent, but not as high as the price of money today.

Mr. RUSSELL. Mr. Hughes, if we were making a cost comparison analysis today, we would use the rates shown in the current Treasury bulletin, and that rate would be 4.97 percent.

Chairman PROXMIRE. That is more like it.

Mr. RUMSFELD. I do not know. It just seems to me that—from a decisionmaking standpoint—the figure that would have to be paid in the private sector would be a more accurate reflection on that decision-making process than the figure you authorize to be used in your circular.

Mr. HUGHES. Certainly—

Mr. RUMSFELD. That is my view. You don't have to comment on it.

Mr. HUGHES. We have studied some of the arguments. I have seen Dr. Stockfish's paper.

Chairman PROXMIRE. I am glad you are familiar with that. I was very impressed by it. I think Congressman Rumsfeld was, too.

Mr. HUGHES. Again, if we are developing a cost comparison, item by item, it seems to us that we ought to reflect actual Government costs on the Government side of the ledger. In a broad economic sense, there is much to be said for the argument—

Mr. RUMSFELD. Which is the way I am putting it. Putting it in the context of our society, and the effect of these costs—well, go on. I am sorry to interrupt.

Mr. HUGHES. In considering these cost items—taxes, interest, and all the others which are outlined in detail in the circular—we are keenly aware of the fact that there can be many uncertainties and differences of opinion when one gets down to the practical problem of making comparative cost analyses in a specific case, and reaching a determination as to whether the Government should itself supply the product or service or obtain it from private enterprise. In this context, we direct particular attention to the following statement on pages 3 and 4 of the circular (see also, app. 13, p. 611).

However, disadvantages of starting or continuing Government activities must be carefully weighed. Government ownership and operation of facilities usually involve removal or withholding of property from tax rolls, reduction of revenues from income and other taxes, and diversion of management attention from the Government's primary program objectives. Losses also may occur due to such factors as obsolescence of plant and equipment and unanticipated reductions in the Government's requirements for a product or service. Government commercial activities should not be started or continued for reasons involving comparative costs unless savings are sufficient to justify the assumption of these and similar risks and uncertainties.

In revising the circular, we considered carefully the question of whether we should change the 10-percent differential in favor of private industry under the "new start" section. We concluded that we should not do so—that this is a subjective judgment that can best be made by the responsible administrators in light of all the facts in a particular case. We did, however, add a sentence to further emphasize that the 10-percent cost differential in favor of private enterprise is not intended to be a fixed figure—and that the differential may be more or less than 10 percent, depending upon the circumstances in each individual case.

We believe further changes in the circular will be desirable. I think the State and local taxes is the most likely of these. We are working with GAO and hope to work with the National Industrial Conference Board and see what we can evolve that will enable us to do this on a reasonable basis.

The transmittal memo to the heads of agencies dated August 30, 1967, said:

We intend to keep the provisions of the Circular under continuing review. We anticipate that further changes will be desirable in light of experience gained from implementing the Circular's provisions, including the required reviews of existing Government commercial or industrial activities to be completed by

June 30, 1968. We intend to give special attention to the adequacy of the guidelines contained in the Circular for such matters as comparative cost analyses; the circumstances under which cost differentials in favor of private enterprise are appropriate; and the use of contracts involving support services that require minimal capital investment.

We welcome your suggestions.

PROGRESS REPORT ON A-76

Since issuance of A-76, revised, on March 3, 1966, we have required two reports from the agencies on the progress being made by them in implementing the provisions of the circular. Briefly, the situation is as follows: (a) Organizational and staffing arrangements for assuring that the policies and procedures are being effectively applied are complete; (b) the inventory of commercial and industrial activities has been completed; (c) the "new start" provisions of the circular are being implemented in all agencies; and (d) most agencies expect to finish their reviews of existing commercial- and industrial-type activities by the target date specified in the circular, June 30, 1968. On the last item mentioned, much work remains to be done, especially in the larger agencies, and until it is complete it is not possible to obtain a composite summary picture of the results achieved in terms of activities continued and discontinued.

DR. STOCKFISH'S ARGUMENT ON OPPORTUNITY COST

Chairman PROXMIER. I am not sure if it is pertinent at this point, but it seems to me that the Stockfish argument, and the argument by the other very competent economists who were here, which they said represented the overwhelming view of the economics profession, is that what Government should do in determining whether to invest in a reclamation project, for example, which is something a little different from this, or for that matter in almost any other kind of investment, is the opportunity cost, which is not a 4.9-percent return, but at least a 10-percent return. And that is the average return for industry before taxes. And that seemed most logical to me. As I say, this is not a matter of conservative economics. This is a matter of the whole economics profession—Otto Eckstein, all these people—agreeing this is a fair basis. If this element comes in here, in this particular circular, it would seem to me that you might very seriously consider revising the circular on that basis, because the economic profession, as I say, is united, and their case is very logical.

Mr. HUGHES. We are sympathetic, Mr. Chairman. With respect to the general question of interest rates—you mentioned reclamation projects, public works projects in general—we know of your views on this. We think the interest rates applied in evaluating the benefits and costs of these projects are somewhat lower than desirable, in a true economic evaluation.

Chairman PROXMIER. You have a gross misallocation of resources on the basis of—what is it now, $3\frac{1}{4}$ percent they use for reclamation projects?

Mr. HUGHES. Generally it is a coupon rate. We have a lot of bent and broken lances in working on this problem. One of the most recent ones was so-called section 7 of the Department of Transportation bill.

Chairman PROXMIRE. I was one of two Senators who voted against that bill, and that is the reason I voted against it. Of course, others did not pay attention to that particular thing. But it results in a perfectly enormous excess in Government spending that in my view just cannot be justified.

I do not want to delay you now on this.

But, I hope, if you are revising this, this can be brought up. After all, you are putting Government money to work, and when you put it to work, it would seem to me that the fair base—not only the fair basis, but the economical basis for the whole society is that you put it to work on an opportunity cost basis which would be close to 10 percent. At least this should be raised and carefully considered.

Representative RUMSFELD. If I may add to that. I think the significance of it is not only this question we are talking about, public and private—but the decision as to whether it should be done at all.

Mr. HUGHES. That is quite right. The same problem exists in the public works area.

Representative RUMSFELD. Particularly in the public works area.

Mr. HUGHES. I certainly want to make it clear that we agree with the desirability of—

Representative RUMSFELD. Getting a new lance?

Mr. HUGHES. We get new ones all the time, and break them all over again. We will be dealing with this by project. That is the way the issues are set up.

With respect to Mr. Stockfish's view, and those of the others—I think in broad economic terms there is great validity to the concept that they set forth.

They do assume a degree of fluidity with respect to interchange, Federal Government versus private, and as among Government programs, which I think is greater than in reality exists. But nonetheless, the appraisal of opportunity costs on this basis is worthwhile.

Representative RUMSFELD. What would you think about having the Congress pass a requirement that the Bureau of the Budget submit, with the budget, and with every request contained in the budget, a statement indicating what the computations are with respect to the recommendations that have been made by the witnesses before our committee. Just simply go ahead and don't make your decision on that basis if you do not want to, but print it. I would think that would be a nice discipline for the House of Representatives—of which I can speak for personally—and, I think, from my observation, the other body could use a little of that discipline.

Chairman PROXMIRE. Even more.

Mr. HUGHES. We would certainly have no objection. I think you are going to have trouble. But, we would have no objection.

Representative RUMSFELD. It sounds fairly innocuous on the face.

Mr. HUGHES. This was the section 7 problem, really. We dealt with it also in the context of so-called water compelled rates for navigation projects, in terms of getting what we regarded as economically sound cost comparison. And, there are difficult social as well as economic problems here.

Representative RUMSFELD. Spelled "political."

Mr. HUGHES. I would spell them social. I would make the point, even as a Budget Bureau representative, that sometimes we want to do things that are not economic for social reasons.

Chairman PROXMIRE. What gets me is——

Mr. HUGHES. But we ought to know what we are doing.

Chairman PROXMIRE (continuing). Everything I have seen lately indicates if we follow this rational basis, we are going to make some excellent humanitarian investments. I just read in the paper this morning the value of a college education has a return of around 14 percent, 14 to 18 percent. And the poverty programs, for example, many of them have a much greater rate of return than the reclamation projects have. Not all of them, certainly, but many of them do have. These human investments can be justified on this basis. And we are not saying that you apply that across the board relentlessly and always, and just use a computer. That would put Congress out of work, and we would not have a job. But, we are thinking of at least having this as a guide, so we know just what we are doing. And we recognize when we are using intuition or using a social preference instead of using a rational application. We are just fooling ourselves as to what we have now on reclamation projects.

Representative RUMSFELD. To point out my recommendation here is not as wild as it sounds. Mrs. Griffiths has proposed we get Bill Veeck to construct a scoreboard in the House and Senate, and possibly at the Budget Bureau to show the cost of everything, and the deficit. Every time a bill is passed, it would be rung up on a board. My proposal is a more subtle way of doing it, at least.

Mr. HUGHES. We welcome anything that the committee would wish to do to reflect more realistically the cost of money or other more realistic economic factors in appraising public works projects or considering competition with business. Other areas where these kinds of considerations are applicable.

Representative RUMSFELD. But you really do not have good cost accounting systems in the agencies referred to in the paragraph.

Mr. HUGHES. Well, I think our costs data varies somewhat, depending on the program, and depending on the agency involved. In the public works area, for instance, I think our data are relatively good. We do not always use it well. But we have, I think, relatively good basic information to work from. The problem lies in the use of those data and what standards and tests, and so on, we apply.

REAL PROPERTY MANAGEMENT

With respect to the management of the Federal Government's real property holdings, we advised the subcommittee last May that the Bureau of the Budget had issued a revised Circular A-2 which provided improved guidelines to agencies for the acquisition, utilization, and retention of real property. We believe now, as we did then, that these guidelines will aid the agencies in improving the management of Federal real property.

REPORT ON REAL PROPERTY HOLDINGS DUE JUNE 30, 1968

The revised circular provides for annual reporting beginning with fiscal year 1968, which will include data summarizing the results of

each agency's action in response to the circular. The report will be based on annual reviews required by the circular. It will indicate whether or not all properties under the custody of an agency are needed, the action which has been and is being taken to screen, report excess, or otherwise dispose of unneeded properties.

It will also indicate the number of properties returned to the public domain and properties made available to other agencies by permit. Copies of new and revised instructions or criteria developed and issued by the agency to implement Circular A-2 will also accompany the report. The Bureau of the Budget will critically review these reports and the agencies' criteria for implementation of Circular A-2.

We believe, generally speaking, that the agencies are doing an effective job in the management of their real property holdings. We as well as the agencies, however, are trying to find better ways of attaining our overall objectives of—

- Effective and economic use of current property holdings in meeting program objectives;

- Identification of unneeded property;

- Reporting unneeded property as excess;

- Disposing of surplus real property for its highest and best use;

and

- Limiting acquisitions to actual program requirements.

We believe the results attained during the last 5 years are significant. In the 5-year period, ending June 30, 1967, Federal agencies identified as unneeded and reported to GSA as excess, real property costing \$4.4 billion. During this period, excess real property, costing \$542.4 million, was transferred between agencies, thus avoiding the need to seek funds to purchase or construct new holdings for new or expanded Federal programs.

Disposals of surplus real property for the 5-year period ending June 30, 1967, amounted to \$2.5 billion, in terms of acquisition cost. Of the total disposals, in terms of acquisition cost—

- \$1.9 billion or 74.9 percent was sold at fair market value;

- \$278.6 million was conveyed on favorable terms for health and educational purposes;

- \$187.6 million was donated for airport purposes;

- \$15.2 million was donated for wildlife and historic monument purposes;

- \$44.4 million was sold at 50 percent of current value for park and recreational purposes; and

- \$115.7 million was disposed of by special legislation, abandonment, destruction, and writeoff.

VALUE OF FEDERAL REAL PROPERTY STEADILY INCREASES IN DOD

Chairman PROXMIRE. In spite of all that, I am very much concerned that the amount owned by the Federal Government seems to be growing relentlessly, and very sharply.

For instance, in the DOD I note that in 1955 there was \$21 billion, went to \$23 billion the next, \$25 billion the next, \$27 billion, next, nearly \$30 billion the next, \$33 billion the next year, \$34 billion, \$35 billion, \$37 billion, close to \$38 billion—and, it is \$38.3 billion in 1966. So that each

year this Defense Department holding increases. I wonder if we are being aggressive enough in our disposal activities.

Could you tell me—would much of this be accounted for by the rise in real property value in those 11 years, or would it be the fact that the Federal Government, in fact, is holding much more real property?

Mr. HUGHES. I believe those figures are acquisition cost figures, but I am not sure. If I am correct, then escalation in property values is not a factor, and the figures reflect increases in acreages held.

I think, as you suggested, they reflect Defense acquisitions to meet Defense needs.

Your question as to whether we are sufficiently aggressive in disposing of property—whether we are as aggressive in disposing of property as we are in acquiring it—

Chairman PROXMIRE. You have put it much better.

Mr. HUGHES (continuing). Is the basic question. And, I think, all I can answer is, that we are very aggressively attempting to both better utilize and to dispose of the property we have.

Chairman PROXMIRE. There are good budgetary reasons for disposition.

Mr. HUGHES. There certainly are. These are capital investments. We have every incentive, we in the Bureau of the Budget, and to an extent the agencies do also.

GOVERNMENT-WIDE INCREASE IN REAL PROPERTY HOLDINGS

Chairman PROXMIRE. In 1955, the overall figure was \$38 billion. In 1966, it was just short of \$70 billion. So that is almost—close to a doubling in a period of 11 years. Increase of 82 percent, to be precise.

So I hope we can redouble our aggressiveness in disposition.

PROGRAMS TO UTILIZE REAL PROPERTY

Mr. HUGHES. We have mentioned here some of the things that we are trying to do in addition, above and beyond the circular.

The President's Council on Recreation and National Beauty is exploring methods of meeting the country's needs for parks and recreational areas to the maximum extent possible by utilization of available, suitable surplus real property.

The Secretaries of Defense and Housing and Urban Development, the Attorney General, and the Administrator of General Services have been assigned the task of surveying unneeded Federal real property throughout the Nation to meet critical urban needs for housing.

Another group, chaired by the Secretary of Commerce, is striving to utilize unneeded Federal properties in their efforts to locate industry in or near hard-core disadvantaged communities to provide employment and training opportunities for the disadvantaged.

We are continually reviewing Federal policies and practices relating to the utilization of excess, and the disposal of, surplus real property, and believe significant results are being attained. We are not wholly satisfied with the results to date but believe a critical review of the reports prescribed by Circular A-2 coupled with action as dictated by this review will result in additional improvement in the management of Federal real property.

NEED FOR OBJECTIVE EVALUATION OF REAL PROPERTY HOLDINGS

Chairman PROXMIRE. Why wouldn't it be good to get a clear directive from Congress, or from the President, that the Budget Bureau or some objective group would apply pressure and force to the agencies to get rid of the property they do not need? It seems to me there is a perfectly natural and understandable tendency for these agencies to hold on to property—they do not want to get rid of it unless there is real pressure on them to do it. And absent this kind of declaration from the Congress or from the President, it is understandable.

I can see that once in a while you come along with some kind of a program—and I don't mean to be demeaning of the efforts you have made—but it would seem to me that an overall policy, that the Federal Government should dispose of these holdings—especially by sale—would be helpful.

Mr. HUGHES. I think policy is very clear as far as the executive branch is concerned. There are Budget Bureau issuances, besides Circular A-2, letters and so on, which make this clear.

Chairman PROXMIRE. Maybe there ought to be more of a policy on acquisitions—in other words, to slow down on the acquisition unless you can justify it.

Mr. HUGHES. The revision of Circular A-2 was intended to help.

Chairman PROXMIRE. One area we have discussed in great detail in these hearings is the Government going out and buying equipment for private contractors. This is an example of that. That would be right in here; would it not? Not real property, but it would be in addition to it—the same kind of thing.

Representative RUMSFELD. Is there any way you could force an evaluation of the extent to which a request for the power to acquire something could be coupled with a reevaluation as to what might be disposed of to compensate for it?

Mr. HUGHES. I think you will find that the provisions of Circular A-2 do that. You come back to the problems of judgment, of discrimination as between, for example, the suitability of an existing piece of property for a new purpose, and the disposability of a piece of property in offsetting a new acquisition—those kinds of tests.

I think you will find that the circular is intended and does in fact confront the agency with the kind of choices that you are suggesting should be made.

We look forward to the product of the review of property in the form of the report that we will get at the end of the fiscal year, as a tool to see how well the agencies are doing in exercising their judgment in acquisitions versus using existing property versus disposal.

PAYMENT OF TAXES AS A DISCIPLINE AND EQUITY

Chairman PROXMIRE. Congressman Curtis has suggested that one discipline that could be used to help on this, is to require these agencies to make some kind of payment, in lieu of taxes, to local and State governments that have personal property taxes, not only in terms of discipline, but, more particularly, in terms of equity to the State and local governments involved.

Mr. HUGHES. The equity argument I regard as a more meaningful one than the discipline.

There are some areas at the present time where payments, in lieu of taxes, are made—nothing very spectacular has happened there, with respect to disposal. The fact is, I think, that the payment, in lieu of taxes, tends to be built into the system in much the same fashion that some of the other things we have discussed get to be built into the system. And while first time around, there is some incentive value, as time passes, the tax becomes a part of the base. And, I think, personally, it is not particularly helpful, therefore, as a disposal incentive.

Representative RUMSFELD. Wouldn't it, however, act as a discipline—as a piece of property depreciates—I forget the name of the Army base in San Francisco.

Mr. HUGHES. Presidio.

Representative RUMSFELD. If you had a payment, in lieu of taxes, that would jar people, wouldn't it? Can anyone tell me that the work that is being done on the piece of property by the U.S. Army, could not be done at half the price someplace else?

Mr. HUGHES. I think some people will tell you that, not all of them in the executive branch, probably. The question has come up before as with the Navy's Annapolis dairy farm, where there is a similar kind of problem, similar emotions are aroused, and where we are kind of up against it.

Again, I simply point out to you that as far as the Bureau of the Budget is concerned, and to an extent as far as Defense is concerned, there are massive incentives, massive values to be achieved in disposing of some of these properties. Nonetheless, they are hard to move many times, particularly properties like the Presidio or Fort DeBussey, another difficult kind of situation. And there are many more.

Again, we undoubtedly will sally forth with a new lance from time to time. But, the going is hard in this area.

A congressional expression of intent, concern, and so on, it would seem to me, would be helpful in this area.

CONGRESSIONAL EXPRESSION OF INTENT WOULD HELP

There is substantial expression of executive branch policy on these matters, and it all leans in the direction of disposal for market value or otherwise for highest and best use of the property.

Chairman PROXMIRE. In our July 1967 report,¹ we had what, I think, is a good section on the use of real property holdings, real estate management. And, without objection, that page and a half will be printed in the record at this point. Beginning on page 29 it goes through the so-called general provisions, on page 30.

(The document referred to follows:)

III. REAL ESTATE MANAGEMENT

USE OF REAL PROPERTY HOLDINGS

Federal real property holdings worldwide have increased in value by \$31.3 billion or 82 percent from fiscal 1955 to 1966. In millions of acres the increase has been 11.8, or 2 percent in that period.⁶⁸

¹ "Economy in Government," report of the Subcommittee on Economy in Government, July 1967.

⁶⁸ Staff materials, 1967, pp. 11-12.

The increase in cost of real property owned by the United States in the United States from fiscal 1956 to 1966 was: ⁵⁹

Land -----	\$265, 000, 000
Buildings -----	1, 160, 000, 000
Structures -----	1, 111, 000, 000

Despite the fact that the DOD and GSA have done some notable work in disposing of real properties, accruing proceeds thereby, augmenting the tax base or placing the property to approved public use, the subcommittee is and has been of the belief that a more vigorous program of identifying and screening excess and surplus real property should be undertaken.

The subcommittee report of May 1966 recommended: ⁶⁰

Recommendation

There is a continuing need to screen the Government's real property holdings to determine if they are being put to the best and highest use from the national point of view. Since the holding agencies may not be entirely objective in the matter and have the sole authority to make the declarations of excess, it is recommended that a high level economic policy committee be assigned the task of reviewing agency real property holdings and making recommendations to the President as to their continued retention and highest use.

The strength of the recommendation lay in the idea of a high-level economic policy committee which would review agency holdings and make recommendations to the President concerning the retention of the property. This would put the spotlight on the agency heads who have the sole authority to make excess property declarations but often fail to do so.

In lieu of adopting the subcommittee's recommendation, the Budget Bureau on April 5, 1967, issued Circular No. A-2, revised,⁶¹ to the heads of executive departments and establishments on the subject of utilization, retention, and acquisition of Federal real property.

Deputy Budget Director Hughes explained the purposes of the new circular: ⁶²

GENERAL PROVISIONS

Circular A-2, as now revised, requires Federal agencies to develop criteria to achieve effective and economical use of real property holdings consistent with program requirements. It also provides that agencies are to identify real property, or any separable unit thereof, as unneeded when—

It is not being used by the agency for program purposes, or

There are no approved current plans for future use of the property, or

Substantial net savings to the Government would result if properties used for essential purposes could be sold at their current market values and other suitable properties of substantially lower current values substituted for them, or

The costs of operation and maintenance are substantially higher than for other suitable properties of equal or less value which could be made available by transfer, permit, purchase, or lease.

RELATIONSHIP TO RELIANCE ON PRIVATE ENTERPRISE

In addition to the guidelines enumerated in Circular A-2, Circular A-76, on which I commented previously concerning the Government's general policy of relying on the private enterprise system, bears on the problem. Circular A-76 establishes guidance for agencies for reviewing industrial and commercial type activities which may result in real property becoming excess incident to discontinuance of such Government activities.

REPORTS OF EXCESS PROPERTY

Circular A-2 provides that all unneeded real property as defined in the Federal Property and Administrative Services Act is to be reported as excess

⁵⁹ Ibid., p. 15.

⁶⁰ Report, 1966, p. 12.

⁶¹ Hearings, 1967, p. 234.

⁶² Ibid., pp. 215, 237.

to GSA or, in the case of public domain which is no longer required for the program for which withdrawn, reported to the Bureau of Land Management, Department of the Interior, or, if covered by other statutes, disposed of as provided by applicable law.

Growth of Real Property Holdings

We share the committee's concern relative to the growth of Federal real property holdings which totaled \$69.4 billion as of June 30, 1966. To assure that acquisitions are kept to an absolute minimum as to area, A-2 instructs Federal agencies to acquire only those amounts of real property necessary for effective program operation.

Control of New Procurements

Also, before an agency acquires new property the agency head must make a determination that the best economic use is being made of existing holdings and, in the first instance, attempt to fulfill the need by using property under the agency's jurisdiction. If the need cannot be met by using existing agency holdings, the possibility of utilizing other satisfactory existing Federal properties must be exhausted. Procedures are provided for notifying the General Services Administration and the Bureau of Land Management, Department of the Interior, as appropriate, to ascertain if excess, surplus, or unreserved public domain lands are available which might fill the need. When existing holdings are not available for transfer, agencies then are to consider the possibility of joint use of real property held by other agencies before action can be instituted to condemn, purchase, construct, or lease.

* * * * *

GSA'S RESPONSIBILITY AND CAPABILITY CONCERNING PUBLIC UTILITY SERVICES

Mr. HUGHES. The last matter that you wish us to discuss, Mr. Chairman, was GSA's responsibility and capability concerning public utility services.

GSA's authority and responsibility stems from section 201(a)(4) of the Federal Property and Administrative Services Act of 1949, as amended, and reads as follows:

With respect to transportation and other public utility services for the use of executive agencies, represent such agencies in negotiations with carriers and other public utilities and in proceedings involving carriers or other public utilities before Federal and State regulatory bodies; * * *

GSA's authority is, of course, limited to representing the Federal agencies as users of utilities services. While the Government's use of utilities is substantial, GSA has taken the position in the past that its staff assigned to this work, plus its ability to utilize other professional staff to supplement the work of assigned staff, is adequate to assure effective representation of the Government as a user.

Also, I believe, Mr. Knott, the Administrator of General Services, has testified before your subcommittee this week as to cumulative savings attributable to GSA efforts as well as to savings made since the hearings last May. We also have been advised of a recent reorganization by the GSA of its Transportation and Communications Service which it believes will make for a more efficient and effective organization. With this recent reorganization in mind, we are exploring with GSA as a part of our budget review its ability to handle the workload involved in representing the Government as a consumer of utility services.

Mr. Chairman, this concludes my prepared statement.

NEED FOR LEGISLATION ON CONTRACTOR-HELD EQUIPMENT

Chairman PROXMIRE. Thank you very much. I wish for the record, Mr. Hughes, if you could provide for us the opinion of the Bureau of the Budget—it does not have to be formal or detailed—on the helpfulness or the constructive use of legislation on contractor-owned equipment—specifically, on inventory controls, including access, clear access, by—

Mr. HUGHES. You mean Government-owned in the hands of contractors?

Chairman PROXMIRE. Yes; Government-owned in the hands of contractors. Control of the total inventory of such equipment, including access to premises of the contractor—which, I understand, on some occasions have been denied—so that they can make physical check. Second, the use of records; that is, the time used for the Government work, time used for commercial work, the idle time. The practicality of having quarterly reports on such records made available, the liability of property if such property is misused, and also the possibility of in lieu provisions for local and data taxes when privately used. And, the provision for sale at reasonable prices of this property to the contractor who is using it.

Now, I would like to—

Representative RUMSFELD. I have a unanimous-consent request that the full text of the article by Mr. Gonzalez be included in the record.

Chairman PROXMIRE. Without objection, the full text of an article by Congressman Gonzalez in the *Progressive* will be printed in the hearings. (See p. 156.)

NEED FOR BETTER TOP MANAGEMENT

Mr. Hughes, for a number of years, this committee has been pointing to our economic dilemma which is also social and political; namely, that our budgets get higher, our indebtedness greater, our taxes higher, et cetera. While on the other hand, we should do much more to improve our democracy in many areas.

We have said, and still say, that much if not all that we genuinely need can be financed from what we waste.

This simply means that we must have better management in the areas of our great expenditures, some of which we have been discussing here this week.

BOB VIEWS ON ANOTHER "HOOVER COMMISSION"

There is another wave of opinion that we should create another Hoover Commission. But the Congress has vested great authority in the Bureau of the Budget, the GAO, and the GSA. I believe that these hearings and those going on in the Ways and Means Committee today and many other evidences show that our top management has been deficient insofar as economy and efficiency—and effectiveness—are concerned. Will you give this some serious thought and give us your ideas in letter form. We are meeting again on December 8, 1967, this room, 10 a.m., to again hear the Comptroller General on some subjects which

time did not permit us to cover on November 27. We will be in recess until that date.

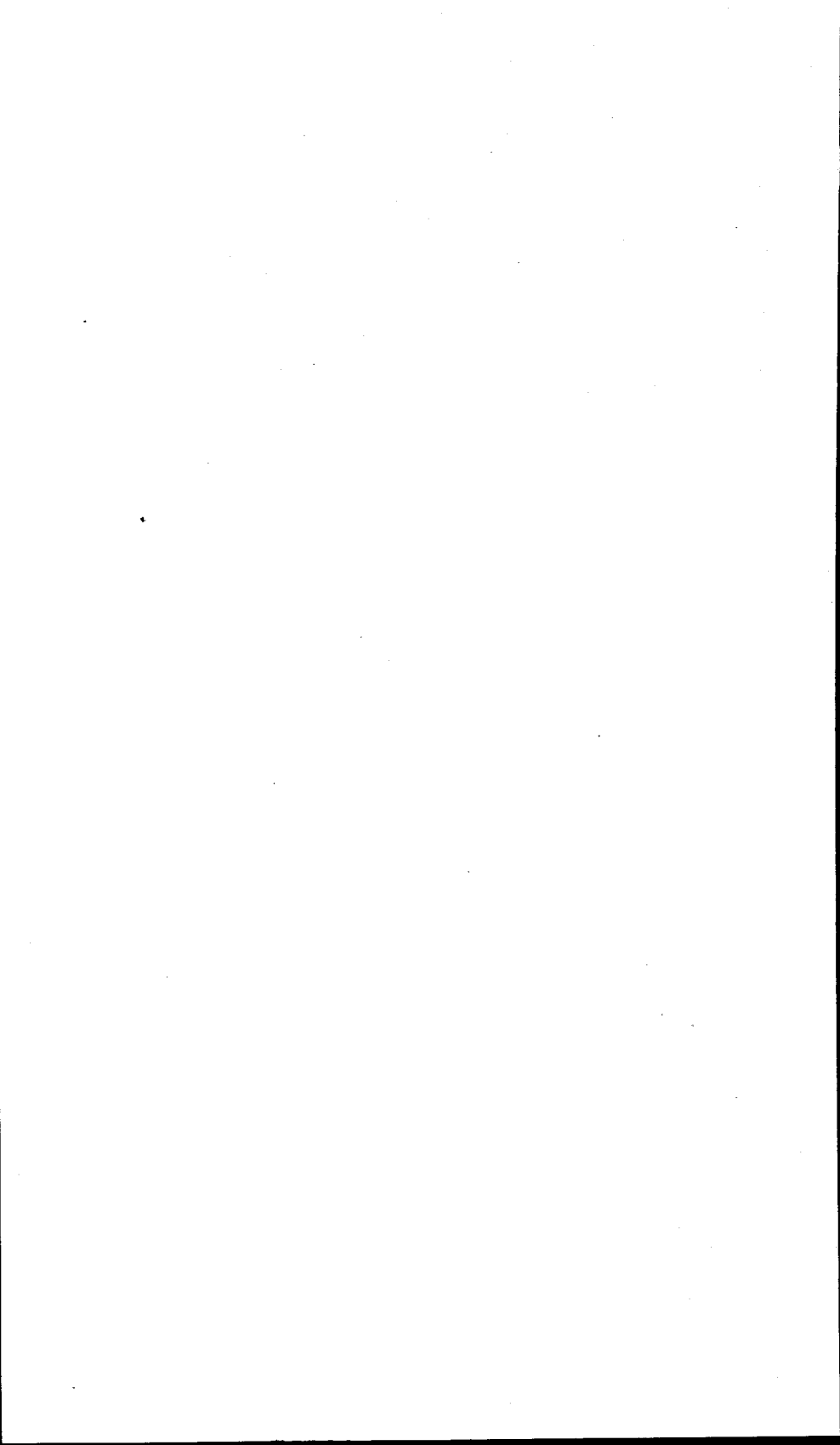
(The following was subsequently supplied:)

We do not see a need to propose additional legislation at this time. Our reasoning is that the Budget and Accounting Procedures Act of 1950, as amended, and the Federal Property and Administrative Services Act of 1949, as amended, provide specific statutory direction to agencies to develop adequate procedures and systems for the physical and financial control of Government property, regardless of where located. However, during the course of the current GAO and DOD cooperative study to tighten up existing controls over Government-owned property in contractor plants, additional legislative authority or direction might be found desirable. If that proves to be the case we will assist whenever needed in proposing such legislation for congressional consideration.

Chairman PROXMIRE. Thank you very much for an excellent job. You and your associates were very responsive and helpful.

Mr. HUGHES. Thank you, Mr. Chairman.

(Whereupon, at 12:50 p.m. the subcommittee was recessed, to reconvene at 10 a.m., Friday, December 8, 1967.)



ECONOMY IN GOVERNMENT PROCUREMENT AND PROPERTY MANAGEMENT

FRIDAY, DECEMBER 8, 1967

U.S. SENATE,
SUBCOMMITTEE ON ECONOMY IN GOVERNMENT
OF THE JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The subcommittee met at 10 a.m., pursuant to call, in room S-407, the Capitol, Senator William Proxmire (chairman of the subcommittee) presiding.

Present: Senators Proxmire and Symington; and Representative Rumsfeld.

Also present: Ray Ward, economic consultant.

Chairman PROXMIRE. The Subcommittee on Economy in Government of the Joint Economic Committee will come to order.

Before we hear from Mr. Staats, who has very kindly agreed to return, I want to insert in the record, with unanimous consent, a statement by Congressman Gonzalez, of Texas, who has a very deep and a very competent interest in these matters. Unfortunately, he had to be in Texas today, so he couldn't be here. His statement will be printed in full in the record. It is an excellent and thoughtful statement.

STATEMENT OF HON. HENRY B. GONZALEZ, A U.S. REPRESENTATIVE FROM THE 20TH CONGRESSIONAL DISTRICT OF TEXAS

Representative GONZALEZ. Mr. Chairman and members of the subcommittee, I consider it a high honor and a rare privilege to appear before you today. Your investigations into defense procurement practices are of the highest importance, and I wish to lend my small voice in commendation. I should add that I am very grateful to be addressing such a distinguished body of legislators in the first committee forum accorded me relative to my interest in the activities of the Renegotiation Board and my concern about the unreasonably restricted role it now plays in returning excessive profits to the American taxpayer.

It was entirely through happenstance that I first became aware of the existence of the Renegotiation Board. This was a year and a half ago when Mr. Farris Bryant, Director of the Office of Emergency Planning appeared before the committee I serve on, Banking and Currency. Although the topic was stockpiling, I was interested in figures that prime defense contract awards were approaching a magnitude higher than the Korean war peak. I asked about possible disloca-

tions in the economy and whether special controls were being contemplated. I was not answered directly, but in the exchange the name of the Renegotiation Board was mentioned.

At the time I knew nothing about the Board. I have been pained to discover that the same is true with most of my colleagues. But the more I learned, the more hearty became my support of the Board, and the more strongly I have urged that it be strengthened. I introduced a bill, H.R. 6792, which would return the Renegotiation Board to its Korean war effectiveness. I have requested hearings on my bill. I have made 12 exhortations in the Congressional Record, covering 19 pages. I have written to the President several times. And often, I confess, I have gotten the impression that mine was a lone voice crying in the wilderness. So I am very pleased to have such a distinguished audience this morning.

I have also authored an article for the August 1967 issue of the *Progressive* magazine entitled "The War Profiteers." In the November 28 hearings of this subcommittee, a distinguished member, Congressman Donald Rumsfeld, questioned the Assistant Secretary of Defense for Installations and Logistics, Mr. Thomas D. Morris, about my article. Since my views in this article were injected into your hearings and my conclusions challenged, I requested the opportunity to reply. I am grateful to Chairman Proxmire for graciously scheduling my appearance. (See p. 156.)

Mr. Rumsfeld asked Mr. Morris whether my charges that war profiteering is increasing were correct. Mr. Morris replied: "I know of absolutely no evidence to support those statements."

I cannot come before this subcommittee with figures and statistics proving that the volume of war profiteering is increasing by this or that amount, any more than Mr. Morris can prove that it is not increasing. The reason for this is not complex: there is simply no comprehensive scrutiny of war profiteering. The Department of Defense certainly does not keep track—it took them 5 years to order audits of cost estimates in order to better comply with the Truth in Negotiations Act. The General Accounting Office is not interested in the profits a contractor may realize except as resulting from unreasonable cost and pricing data at the time the original contract was negotiated. And the Renegotiation Board does not have purview over enough of the defense spending. With its present list of exemptions, and with its present minimum floor, I estimate that the Renegotiation Board annually misses at least \$6 billion in Government contracts and misses about 7,600 contractors. And also, while the preponderant majority of the contractors and subcontractors the Board reviews are defense related, the Board also reviews contracts with NASA, AEC, FAA, GSA, and the Maritime Administration. Therefore, its experience cannot be considered solely defense contracts.

The fact that there are such gaps in congressional or quasi-judicial scrutiny of war profiteering is precisely the matter which causes me concern.

Despite the absence of statistics, I am confident there is a clear inference that war profiteering is increasing. I do not retract one iota from my statement that "the facts make it clear that profiteering is taking place on a considerable scale" and that "there is evidence it is

on the upswing." I say this because the volume of defense contracts has risen sharply as a result of the Vietnam War. This year we are spending more in Vietnam, both in dollars and in percentage of total U.S. spending, than we did in the peak year of Korea, which was 1953. Specifically, Vietnam is costing \$26 billion now, contrasted to \$10 billion for Korea in 1953. I say profiteering is on the upswing because the jurisdiction of the Renegotiation Board has been cut back by Congress over the years. The successive exemptions to renegotiations allow more and more profiteering for two reasons. First, the number of contracts and the number of contractors within the Board's jurisdiction have declined. For example, in 1952 the Board reviewed the profits of 13,104 companies; but in 1966 the number of companies had dropped to 3,387, a cut of nearly 75 percent. And secondly, these exemptions increase profiteering because the deterrent effect of the Board has vanished in those exempted areas.

Like the policeman of the beat, the Board casts a long shadow. To illustrate, in 1966 the Board made determinations of \$24.5 million in excessive profits, but corresponding to this figure was an additional \$23.2 million in voluntary refunds by the contractors which were reported to the Board. I suspect that the effect of the Board is like an iceberg—a good deal of its weight is below the surface.

Also, despite the direct denial of Mr. Morris, I stand squarely behind my statement that the "annual reports of the Renegotiation Board reveal that profiteering is going on now, is increasing, and will continue to increase unless something more realistic is done to stop it." Mr. Morris said, "The Renegotiation Board reports of past years certainly do not bear it out."

I disagree. The Board's reports certainly do. The fact that the Board in its latest report could point to its recovery of \$47.7 million in excessive profits determinations or voluntary refunds certainly does confirm my statement that war profiteering is going on now. If I might be excused in appropriating the same argument used by Mr. Morris, I would say that I know of absolutely no evidence to support the contention that war profiteering has somehow ceased.

Further, the following table of Renegotiation Board determinations of excessive profits from 1962 to 1966 certainly does confirm my statement that profiteering is increasing:

Fiscal year:	<i>Excessive profits</i>
1962 -----	\$7, 840, 000
1963 -----	10, 070, 000
1964 -----	24, 160, 000
1965 -----	16, 150, 000
1966 -----	24, 510, 000

And finally, the fact that the first rash of contracts awarded during the Vietnam buildup are now coming before the Board does indicate the validity of my statement that profiteering will continue to increase.

While I am on the Renegotiation Board's latest report, I might mention that the Board recovered this \$47.7 million in excessive profits with a total of 178 employees. This amount of profiteering is even more amazing to me when I consider all the contractors and their contracts now exempt from renegotiation. Though not entirely fair, it is nevertheless suggestive to contrast these 178 employees of the Renegotiation Board with the 25,000 "procurement professional people" that Mr.

Morris said work for him. You might also be interested in my calculation that for every \$1 spent on the renegotiation, the Board has recovered for the American taxpayer about \$18 in excessive profits.

Perhaps Assistant Secretary Morris objects to my use of the term "war profiteering." I contend there is a war going on. I contend excessive profits are being made on defense contracts. I contend, therefore, that war profiteering exists. I refuse to mince words. At a time when we are engaging in the involuntary procurement of men for Vietnam through the draft—at a time when we are asking nearly half a million American troops in Vietnam to be prepared to make the ultimate sacrifice for their country—at a time when nearly 200 of our boys are dying each week, I say it is unconscionable that even one contractor should be allowed to make a killing on a defense contract.

The position of Mr. Morris on whether war profiteering exists amazes me. He tries to have his cake and eat it, too. For one thing, he said he knows of "no evidence" to support my statements there is war profiteering, and yet he admits there "may be * * * individual cases." But my credence is taxed to the utmost by his statement that "we have no valid information" of overcharging except that disclosed by Congressman Pike. "Nor," Mr. Morris states, "has GAO brought any to our attention that I am aware of."

Surely Mr. Morris is not unaware of the charges of excess profits against Colt's on the M-16? Surely Mr. Morris is not unaware of the 10 examples of questionable profits picked out by Senator Young from among "private letters" of the GAO to his Department? Surely Mr. Morris is not also unaware of the questionable practices by the companies picked at random by Congressman Charles Whalen from among the "private letters" of GAO to DOD? Surely Mr. Morris is not unaware of the 222 out of 242 contracts which the Comptroller General stated before this subcommittee lacked evidence to support the cost or pricing data submitted by contractors? Surely Mr. Morris is not unaware of the 33 out of 101 cases of overpricing that the Assistant Comptroller General spoke of before the House Subcommittee on Military Procurement?

Surely Mr. Morris is not unaware of the Comptroller General's recent report to Congress charging improper use of Government-owned industrial plant equipment? In this connection, surely Mr. Morris is not unaware of the situation described by Jack Anderson in last week's Parade magazine under the title "How Uncle Sam Is Cheated: The Multi-Billion Dollar Machinery Giveaway"?

Mr. Chairman, I would like to call attention to attachment No. 1 of my remarks, which contains a short bibliography of recent charges of what I call profiteering, as compiled by my staff. Clearly, the Defense Department and the contractors must be heard in the full on these charges. But how anyone can imply that the GAO and the Congress has not brought to light serious indictments of war profiteering is beyond my comprehension.

If not already a part of the record of this subcommittee's hearings, I would like permission to include the Parade magazine story after my remarks. It is a very revealing article, and it gives an excellent account of the efforts of Chairman Proxmire and Mrs. Griffiths of this subcommittee in behalf of the national interest.

(The article referred to begins on p. 347.)

Representative GONZALEZ. You may have noticed that the examples of defense overcharging as listed in my attached bibliography were disclosed by persons interested in procurement practices. They are important to me because they confirm my conviction that if profiteering did not exist in this war, it would be the first time in our history. But I have not brought here similar, current examples from the renegotiation process. This is due to the nature of the Renegotiation Act itself. The Board does not deal in current contract awards. It does not review contracts until several years after they are negotiated. And the renegotiation process is not constituted on a contract-by-contract basis, but lumps all renegotiable business of one firm together.

Another reason the Renegotiation Board does not make news is because the records submitted to them are held in strict confidence. This is because the records required by the Board are based on a contractor's income tax records, and are covered by the same nondisclosure laws as income tax returns. Not unless a contractor appeals an excessive profits determination to the Tax Court do the details of his case become public. And since more than 90 percent of the Board's determinations of excessive profits are agreed to by the contractor, few cases are disclosed. Those cases that do reach the Tax Court are older still.

I realize my presentation so far has not been a model of orderliness. I hope I can be excused for my interest in demonstrating that my facts on the Renegotiation Board and my charges of war profiteering were based on all the evidence I could locate. I know that the Renegotiation Board is not the first order of interest of this subcommittee, and I appreciate your patience. This is not the place to go into the whys and wherefores of my bill to strengthen the Board, although I would like to repeat that it would bring at least \$6 billion more renegotiable business under the Board's scrutiny, and cover about 7,600 more defense Government contractors. However, I believe it would be of some value to this subcommittee if I briefly compared my understanding of the renegotiation process with the truth-in-negotiations procedures.

I firmly believe there is no substitute for sound, tight procurement practices in the Government. I heartily endorse the investigations by this subcommittee into defense contracts. But I suggest that there is another way to help halt war profiteering than by fully implementing the Truth-In-Negotiations Act. I wish to suggest here that the statutory renegotiation process, developed during World War II and practiced by the Renegotiation Board, is an essential complement to the audit process of truth-in-negotiations.

I am also in agreement with the opinion advanced by Adm. Hyman Rickover this year during the House appropriations hearings on DOD that "the Government cannot rely on the Renegotiation Board to insure fair prices for defense equipment. The Board is not adequate for this purpose."

"First of all," Admiral Rickover said, "under renegotiation profits are averaged over all defense work so that high profits on individual contracts tend to have only slight effect on overall profit levels." This is correct, but I will argue later that there are advantages in this overall view.

He said, "Second, much Department of Defense procurement is exempt from renegotiation." Hence the need for my bill, H.R. 6792.

He said, "But most important, the Board cannot really determine how much profit a supplier makes since, as I have said before, there are no real accounting standards which industry must follow in accounting for work under Government contracts." Here, I defer to the admiral.

My knowledge of the DOD procurement process is not extensive but I do see several difficulties in present DOD practices which the Renegotiation Board can partially compensate for.

First, it is my conviction that the procurement process is not weighted as it should be, in favor of the American taxpayer. Admiral Rickover said, "I think the Defense Department is influenced too much by people who have an industry viewpoint." An article in the National Observer for November 6, 1967, and an AP wire story which appeared about October 16, 1967, both pointed to disturbing connections between defense procurement officers and the "military-industrial complex." I do not believe the Department of Defense can be expected to adequately police its own procurement work. It took 5 years and heavy prodding from Congress before DOD this year issued regulations implementing the audit provisions of the Truth In Negotiations Act. It can be documented that the history of the Department of Defense in complying with its own regulations is not a glorious one. I believe Senator Proxmire and Congressman Minshall are correct in continuing to push for their legislation to strengthen the Truth In Negotiations Act.

The Renegotiation Board, in contrast, is independent, judicious and nonpolitical. Its only job is to police excessive profits. The Board is not arbitrary. Nine out of 10 contractors reach agreement with the Board on its excessive profits determinations, and more than one-third of every 10th contractor eventually concedes the Board's position. Apparently, the Board is so fairminded and nonpolitical that few members of this Congress have had the occasion to learn about its functions.

A second difficulty with the procurement process is that the so-called competitively bid contracts cannot always be called competitive by any stretch of the imagination. Congressman Pike uncovered several such cases. For example, the DOD had contracted to pay \$312.50 apiece for a small-sized plastic adjusting knob for field generators. It turned out that the supplier was paying only \$1.62 apiece for them from the manufacturer. But the irony is this: since the contract was formally advertised, it was considered competitive and DOD therefore chalked it up as a saving for the U.S. taxpayer of 25 percent on the \$33,000 contract. And the Armed Services Procurement Regulations that describe contract awards as competitive when one response is received just so two or more proposals were solicited is perpetrating a definition of competition that is beyond me. The ASPR that permits purchases of \$2,500 and under to be considered competitive also escapes me.

Although the Truth in Negotiations Act is not applicable to so-called competitive contracts, there is no limitation on the type of contract the Renegotiation Board can review. They review competitive contracts and negotiated contracts, whether cost-plus, firm fixed-price or incentive. I should say all types of contracts are reviewed by the

Board as long as the contractor of his contracts do not escape under one of the numerous exemptions to renegotiation.

Thirdly, the Renegotiation Board has the advantage of taking a much broader view. It has jurisdiction over all contracts of subcontractors as well as prime contractors. A contractor is subject to renegotiation if he was awarded a total of \$1 million of nonexempt business within a single fiscal year with either DOD, NASA, AEC, FAA, GSA, or the Maritime Administration.

The Board customarily looks at contracts several years after they are negotiated. It looks at the finished contract or at least the first year's experience with the contract. From this vantage point, the cost estimates as originally negotiated assume a different complexion. This is important when the Government has contracted for such innovative hardware as an Apollo booster or a new weapons system. Where new ground is being broken, cost estimates cannot be precise, and honest mistakes can occur. The Renegotiation Board is in a position in this respect to correct mistaken cost and profit estimates from the procurement process.

This broad view is advantageous in other situations. Take the hypothetical case of a company with an Air Force contract against which it must charge a certain amount of overhead. But further suppose that later in the same year this company gets a Navy contract that would rightfully relieve the Air Force of some degree of overhead costs. The Renegotiation Board can take this into account.

This overall view taken by the Board is also favorable to the contractor. A contractor is allowed to have a loss or a negligible profit on one contract balanced against profits on another contract that might otherwise be considered excessive. Further, the contractor gets a 5-year carry forward on his losses for renegotiation purposes.

The contractor also benefits from the flexible criteria of the Renegotiation Act. The Board must give due weight to a contractor's efficiency, to the character of his business, to the extent of risk assumed (i.e., whether the contract is fixed fee or cost plus, etc.), to his contribution to the defense effort, to his capital employed, and to the reasonableness of costs and profits. On this latter point, the Board allows costs and profits on the basis of the tax code definitions, which are more liberal to a businessman than costs as allowed by the procurement regulations.

Undoubtedly there are legitimate gripes from businessmen on some aspects of the Renegotiation Act or the Board's activities. But the basic act has always been so well-balanced that I cannot conceive of any reputable firm complaining that renegotiation is onerous or repugnant.

To summarize, the renegotiation has a threefold value as I see it (1) It strengthens the procurement process. I can imagine an alert procurement officer saying to a contractor's representative, "Don't get cagey; you know the Renegotiation Board will look at these costs on this contract we want to award you. Let's have some realistic cost estimates." (2) The Board's very presence is responsible for a large amount of voluntary profit refunds and generally acts as a restraint upon profiteering. Only finally (3) do I point to the actual determinations and recoveries of excess profits by the Renegotiation Board.

I am very grateful for your kind attention. Thank you.

(The attachment referred to by Representative Gonzalez follows:)

WHAT WAR PROFITEERING?—I'M GLAD YOU ASKED

1. *Excessive Profits by Colt's*

"A 10-percent profit rate was negotiated on all production contracts. The records and information made available by Colt's indicate that profits before taxes were 19.6 percent for calendar year 1965; 16.8 percent for calendar year 1966; and 13.4 percent for the first 4 months of 1967, for an average of 16.8."

Quotation from the Report of the Special Subcommittee on the M-16 rifle program of the Committee on Armed Services, October 19, 1967, p. 5342.

2. *Ten Examples of Excess Profits from "Private Letters" from GAO to DOD*

Senator Stephen Young picked ten examples from the "private letters" of the General Accounting Office calling the attention of the Defense Department to excessive profits and profiteering on defense contracts. Sen. Young gave details and the amounts of the excess profits alleged by GAO, but withheld the company names. The cases include "a giant Ohio corporation that has a record for veracity in its dealings with the Government that leaves much to be desired"—\$143,681, "a Minnesota corporation, also a frequent violator"—\$1.5 million, "one of the largest aircraft manufacturers"—\$1.6 million, "a leading radar manufacturer"—nearly a half million dollars, "a Texas corporation"—\$921,000, "a missile manufacturer"—\$150,000, "an electronics company"—\$108,000, "an Ohio missile supplier"—\$134,000, "yet another aircraft manufacturer"—\$435,000, "another well-known New York company." These are from Senator Young's remarks in the July 21, 1967 *Congressional Record*, pages S9937 to S9939.

3. *More "Private Letters from GAO on DOD being Overcharged*

Rep. Charles Whalen (R., Ohio) has also reported on several of the "private letters" from GAO to DOD. Randomly selecting from these letters, Rep. Whalen pointed to Company A which overstated its proposed costs for electrical equipment by more than \$50,000. Company B won a contract for reconnaissance equipment for a price about \$16,400 higher than it should have been. Company C was awarded an aircraft procurement contract at a level, GAO concluded, "about \$17,500 higher than indicated by information available at the time of negotiation." Company D estimated its costs for a new weapon \$700,000 higher than the situation warranted, with an overstatement of the company's fee of \$88,000. Company E, providing a navigation system, made two errors resulting in an overcharge of more than \$250,000, and another error of \$55,000 in overcharge. Company F should have used data on its aircraft accessory contract which would have reduced the cost by \$52,900. Company G overcharged for construction and operation of a storage facility, based on cost figures 42% more than the only available estimate. Rep. Whalen detailed these cases in the *Congressional Record* of August 23, 1967, pages H11049 to 11051.

4. *Excessive Profits Made by Litton Industries, Inc. on the LN-3 Navigational System of the F-104 Fighter*

"I believe that Litton has made very substantial excess profits on this system. ... Yesterday the General Accounting Office advised me that Litton had declined to provide them with certain essential data as to their profits on these multi-million dollar procurements."

Congressional Record insert by Congressman Otis G. Pike (D-NY), September 27, 1967, H12554.

5. *Overcharges Incident to Negotiated Contract Awards*

"(1) Despite the clearly expressed intention of the Congress, and the continual urgings of this subcommittee, it is clear that insufficient use has been made of competitive bidding, particularly in our military procurement.

(2) Moreover, the overcharges to the Government incident to excessive reliance on negotiated contract awards have been accentuated by the serious lack of compliance with the so-called Truth-in-Negotiation Act. The Comptroller General of the United States had made repeated reports on the insufficient enforcement of the provisions of this act."

From the Report entitled *Economy in Government* of the Subcommittee on Economy in Government of the Joint Economic Committee, "Procurement Policies," July 1967, p. 1.

6. *Overpriced Cleveland Pneumatic Tool Co. Contracts*

"In three contracts (1963 & 1964) with the Cleveland Pneumatic Tool Co., totaling nearly \$2 million, the Army allegedly was charged \$239,000 more than

was justified. This civil finding was made by the U.S. General Accounting Office. . . ."

Part of an article from the *Cleveland Plain Dealer*, April 10, 1967 as included in the *Congressional Record* in the remarks by Senator Stephen Young (D-Ohio), April 20, 1967, S5622.

7. DOD Being Sold Down the River on 222 of 242 Procurements?

"Mr. Staats. . . . we took 242 cases of either prime or first-tier subjects.

. . . in 1965 of these awards we found that the agency officials and prime contractors had no records identifying the cost of pricing data submitted and certified. . . .

. . . of the remaining 57 of the 242 procurements examined . . . there was not a record showing the basis for the contracting officer's determination."

Testimony of the Honorable Elmer B. Staats, Comptroller General, in Hearings before the Joint Economic Committee, part 1 entitled *Economy in Government*, May 1967, pp. 62-63.

8. GAO Reports to Congress

"This report we sent over in draft from (sic) to the Department of Defense will come to Congress when we get their comments. It covers, I think, 101 contracts and finds overpricing in 33 of those contracts."

Extracted from the remarks of Mr. Frank H. Weitzel, Assistant Comptroller General in Hearings before a Subcommittee of the Committee on Government Operations, entitled *Defense Contract Audit Agency*, July 28, 1967, p. 20.

9. Improper Use of Government-Owned Industrial Plant Equipment

"During the 3 years ended December 31, 1965, the 8,000 ton press was used 78 percent of actual production time for commercial work without advance OEP approval (i.e., illegally) . . . Also this contractor had used 10 machines, costing from \$29,000 to \$141,000 each, 100 percent of the time for commercial work during the first 6 months of 1966 without obtaining advance OEP approval. . . . In another case, during the 9-year period ended September 1966, an ammunition facility was used about 80 percent of the time for commercial work. . . .

Report to the Congress by the Comptroller General, "Need for Improvements on Controls Over Government-Owned Property In Contractors' Plants," Nov. 24, 1967, p. 19.

10. Multi-Billion-Dollar Giveaway

"But no one disputes that some contractors have misused and abused the free government machinery entrusted into their care . . . One company which had gotten a whopping \$55 million of free special tooling 12 years ago, couldn't locate much of the stuff when GAO inspectors came around."

Article in the *Parade* magazine of the *Washington Post* by Jack Anderson entitled "How Uncle Sam Is Cheated: The Multi-Billion-Dollar Giveaway," December 3, 1967, pages 6-7.

[From *Parade* magazine, the *Washington Post*, Dec. 3, 1967]

HOW UNCLE SAM IS CHEATED: THE MULTI-BILLION-DOLLAR GIVEAWAY

By Jack Anderson

The Pentagon is pumping billions into American industry to provide businessmen with sophisticated machinery to help them produce essential military hardware. Instead, many of the machines are also being used to produce commercial items—and big profits for the manufacturers.

No one knows the exact extent of the Great Machinery Giveaway. Neither the Pentagon nor the recipients have kept adequate records of the equipment, and a substantial number of machines can no longer be located. Other equipment, too large or too vital simply to disappear, has been diverted from defense to civilian production despite federal regulations and military needs. Still other equipment has been worn out producing commercial items, so that it can no longer be used for the purposes the government intended.

All told, machinery, facilities and materials turned over to defense contractors by the Pentagon has been valued by the Comptroller General at more than \$11 billion. Pentagon officials claim this figure is far too high; some government auditors insist it is too low. But no one disputes that some contractors have

misused and abused the free government machinery entrusted into their care. Indeed, as a recent U.S. audit of 17 plants showed, this amazing charity program for big business has added up to an enormous swindle of the American taxpayers.

Ironically, the whole idea was to save the taxpayers money. Manufacturers who are given free machines for their production lines are expected to pass on the savings to the taxpayers. More often, they have passed on the dividends to their corporate stockholders.

Of course, most of the contractors working on defense items are honest. But the case of one aerospace contractor illustrates how the taxpayers are being taken. The company complained that the 4000-ton presses which it had received free to produce blades for jet engines weren't adequate to stamp out parts for the latest military engines and meet production schedules. The Pentagon obligingly delivered to the company a one-of-a-kind 8000-ton press. Three years later, investigators learned that the military jet blades were primarily being stamped out on the smaller presses, while the 8000-ton press was being used to service commercial contracts 78 percent of the time.

An ammunition contractor used government equipment worth \$4.2 million to produce military rockets only 20 percent of the time between 1957 and 1966. During the same period, he made \$24 million worth of commercial orders on the machinery. When the Navy ordered the plant to begin producing rockets for Vietnam, the contractor wailed that he couldn't meet the production schedule. Investigators detected no noticeable cutback in commercial production, but the contractor insisted that the machinery could no longer meet the tolerances needed for rocket work. Apparently, the commercial work had worn out the government machines, although there was no way for the government to prove it. Instead, the taxpayers had to pay for more equipment to produce the rockets.

Federal regulations demand that contractors get permission to use government equipment for non-defense work and that they pay rent for the time it turns out civilian production. If the commercial use exceeds 25 percent, special authority has to come from the President's Office of Emergency Planning.

These rules are seldom enforced, however, and manufacturers often laugh at them. During one eight-year period, an aircraft company used government equipment to produce \$500 million worth of airplane engines for commercial customers without paying a dime of rent to the U.S. Treasury. Even after a U.S. estimate that \$5 million in rent was due, the money was never collected. It is a story that is repeated every day by other defense contractors.

In several instances, government equipment and machinery was used for commercial production as much as 97 percent of the time. One company had ten machines costing up to \$141,000 which were used full time for commercial production in the first half of 1966.

Despite its celebrated computer systems for cost accounting, the Pentagon has confessed that it cannot completely keep track of all the equipment it has distributed to manufacturers out of the taxpayers' great grabbag. Astonishingly, the Pentagon has left it up to the contractors to inventory all this machinery and to log the hours it is used on commercial production. This is equivalent to putting the geese in charge of the corn.

The General Accounting Office—an investigative arm of Congress—disclosed a number of inventory abuses during a routine spot check in the Dallas area. One plant, which had been given \$21.8 million worth of special equipment, couldn't explain satisfactorily what had happened to it. At another plant, 5000 special items were missing. At a third, "special use" tools supplied by the Pentagon were intermingled with commercial equipment. The Defense Department's own records were found to be so botched that in four Dallas plants the probers located 88 government-owned machines which weren't even listed among the Pentagon's possessions.

One company which had gotten a whopping \$55 million of free special tooling 12 years ago, couldn't locate much of the stuff when GAO inspectors came around. A company spokesman said it would take 20 men one full year to make such an inventory. It should be mentioned at this point that contractors are not required to report on or keep records of special tooling and special test equipment. Thus it is no surprise that the Pentagon was unable to tell PARADE how much of this stuff it had given away, or where it was.

The discoveries in Texas can be multiplied by hundreds of defense plants across the country. The Pentagon simply doesn't know how much machinery it owns nor where all of the stuff is located. "We're not talking about little sausage

grinder machines," one investigator told PARADE. "A lot of this equipment costs many thousands, even millions of dollars. Defense not only has no idea where all of it is but doesn't know how extensively it's being used by private corporations for their own commercial purposes."

Members of Congress who have become aware of the situation are horrified by the waste and inefficiency. "It's all a monstrous disgrace," Rep. Martha W. Griffiths (D., Mich.) told PARADE. "The contractors, in my opinion, are stealing, they're cheating. They do this because they see that nobody in the Pentagon cares about it. The Pentagon doesn't want to be bothered."

Mrs. Griffiths speaks with authority. Before her election to Congress, she spent nearly five years as an Army purchasing agent. "No one knows better than I how stupid these military people can be," she said. "This whole area of defense procurement and lack of controls over government-owned property is a mess. It's a real gyp not only to the taxpayers but to legitimate business. How can you possibly compete when your competitor gets his equipment absolutely free from the government?"

The great machinery giveaway began during World War I to speed production of war materials and to aid manufacturers who otherwise would have been stuck with specialized tools having no peacetime use. This subsidy to contractors steadily gained momentum and, in 1956, the Pentagon began replacing the equipment that had grown old and tired through civilian use.

As the use of government machinery spread to 3500 of the nation's plants, the abuses multiplied. Manufacturers bid for military contracts even when they didn't have the necessary machinery, confident that they could easily obtain the machinery from the government, according to Rep. Griffiths.

Other manufacturers hoarded special tools long after their military contracts had run out. Government auditors found "many instances" of plant equipment that should have been given back to Uncle Sam being diverted from military to civilian production. All too often, the government was obliged to duplicate these expensive tools and machines for other manufacturers.

An analysis of the utilization of \$15.9 million worth of government equipment, scattered among several manufacturers, revealed that most of it had been used exclusively for commercial production or at least hadn't been used for defense work for a long while. Not one of the 328 items involved, however, was reported to the Pentagon as no longer needed. Yet 81 of them were urgently needed at other defense plants.

One Midwestern radio manufacturer, given special tools to produce Army radios, kept the machinery going to meet its commercial commitments after its defense contract had expired. The government had to pay its new contractor an extra \$418,000 to speed production on the needed radios. Another contractor, with a small production order from the military, wangled 30 special machines from the government and spread the work out so he could swear that he had used them all. The total machine use, however, was 40 hours a month. The work could have been done by one machine in one week.

Other contractors have wheedled multipurpose tools, good for commercial production, out of Uncle Sam by claiming they were specialized tools. In one plant alone, government auditors listed \$36 million worth of multipurpose tools that had been classified by the contractor as non-reportable "special tooling".

Use of government machines is controlled by regulations, not law, and the government's only recourse is through negotiations and civil lawsuits, not prosecutions. Armed with this immunity, the Pentagon's indifference and their own skill at juggling records, manufacturers are free to do almost anything they wish with the billions of dollars worth of machinery owned by the taxpayers. Even the General Accounting Office, which can find the hidden figures in most bookkeeping, was confused by one contractor's ability to mask his activities. The contractor had \$8,858,833 worth of taxpayer-paid machinery. "This manufacturer's volume of commercial business was significant," grumped the GAO auditor who checked the books, but the "lack of detailed utilization records and basic agreement documents," he confessed, made it impossible for him to determine "whether equitable rental fees were being paid." The message between the lines was that this manufacturer likely was doing a lot of "moonlighting" with government equipment.

Checks by government investigators are infrequent in the plants, and contractors confidently play the loopholes. As long as they are keeping the records, they realize that they can be compelled to pay rental on the machines only for

those days when government inspectors actually see the machines turning out commercial products.

"It's not really true that these tools, machines, presses and other equipment are useful only in making what the government orders," said Congresswoman Griffiths. "In the first place things like aircraft and electronic items are often identical to commercially used products. And much of the equipment the government hands out free is sophisticated enough to turn out all kinds of commercial items. There are exceptions, and I say the government should only supply equipment absolutely incapable of producing anything but government-needed items."

Sen. William Proxmire (D., Wis.), who has also interested himself in the great machinery giveaway, has summed up his feelings. "I cannot come to any other conclusion," he said angrily, "except that it seems incredibly sloppy, a clear dereliction of duty in the management of inventory, a cost to the taxpayers of hundreds of millions of dollars, maybe even billions and billions of dollars."

The Department of Defense, on the defensive against GAO and Congressional charges of inadequate control and management of "government-owned property in the hands of contractors," is forming "implementation teams" to ride herd on this vast supply of equipment and machinery. Improved auditing, mechanized record keeping, and improving the caliber of government inspectors are also in the mill.

But perhaps the question should also be raised, as some officials in government already have, as to whether the government should even be in the business of supplying billions of dollars of free equipment, machinery, material, buildings, real estate and even whole plants to industry. There is also the question of whether Uncle Sam should rent out equipment paid for by taxpayers, for commercial production sidelines by manufacturers already making a no-risk profit on government defense work.

At a time when President Johnson is demanding higher taxes to pay for the Vietnam war, he might also insist on greater care with the money the taxpayers have already shelled out.

This story of a multi-billion-dollar boondoggle—the Pentagon's blatant waste of machinery and the enormous profits industry reaps from this waste—is the result of weeks of dogged digging into the facts. Mountains of documents were examined, charts and tables scrutinized. When it came time to interview the responsible officials, however, they ran for cover. Even some members of Congress, while admitting that the situation was "bad," didn't want to discuss it. One acknowledged that some of the companies involved were located in his state and they were "quite good to me."

Pentagon officials ducked calls and, when cornered, said they couldn't talk without clearance. The clearances never came. One official admitted to Parade: "The individual from whom the information should be forthcoming was frankly hoping that you would go away. Now that he's convinced you won't go away, I'm hoping for an answer within the next 36 hours."

When it did come, the answer was an evasion of the facts, cloaked in "credibility gap" semantics. "The Defense Department has no knowledge," said the spokesman blandly, reading from a prepared statement, "of any illegal use of government industrial plant equipment by contractors. For that matter, the General Accounting Office has made no report that indicates such a problem exists. Period. End of statement."

In the broadest sense, the spokesman was telling the truth. The misuse of government machinery, though against regulations, strictly speaking is not "illegal" but merely "unauthorized." When challenged, however, the spokesman smiled weakly and responded: "Well, they didn't really believe you'd buy it."

On the question of the legalities, Rep. Martha W. Griffiths (D., Mich.) told Parade: "Whether or not this is illegal is within the control of the Defense Department, and if they haven't made it illegal, then in fact the Pentagon is teaming up with contractors to fleece the American public."

Chairman PROXMIRE. Mr. Staats, we are delighted to have you here again. We feel that your rebuttal testimony to the testimony of the Defense Department, GSA, the Budget Bureau and others who have appeared can be very, very helpful to us.

Maybe rebuttal isn't exactly the right word, but your comments on their observations will be very helpful because some of these things are in conflict.

I feel that you will enable us to go into more critical detail on some of the serious errors which I feel, and some of the rest of us feel, the Defense Department and others may have made in their procurement and inventory management policies.

STATEMENT OF ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES; ACCOMPANIED BY FRANK H. WEITZEL, ASSISTANT COMPTROLLER OF THE UNITED STATES; CHARLES M. BAILEY, DEPUTY DIRECTOR, DEFENSE DIVISION; J. EDWARD WELCH, DEPUTY GENERAL COUNSEL; STEPHEN P. HAYCOCK, ASSISTANT GENERAL COUNSEL; JEROLD K. FASICK, ASSOCIATE DIRECTOR, DEFENSE DIVISION; JAMES H. HAMMOND, ASSOCIATE DIRECTOR, DEFENSE DIVISION; AND CHARLES KIRBY, ASSOCIATE DIRECTOR, DEFENSE DIVISION

Mr. STAATS. Thank you very much, Mr. Chairman.

As you have indicated, we are appearing here again today to comment on and to follow up on some of the points which were raised both in our testimony and in the testimony of the other agencies on the general subject of Government procurement and supply management.

My statement today will cover three areas: Inventory management, agency audit rights and recovery from subcontractors, and, third, the Government property in possession of Defense contractors.

We are also prepared, Mr. Chairman, to respond to other questions which we know you have in mind, which are not included in our formal statement.

But I hope we will be able to add to the record on several points about which, we have been informally advised, the committee has an interest in our views.

INVENTORY MANAGEMENT

Turning first to the subject of inventory management:

The primary objective of inventory management in the military departments is to provide adequate material support to their organizations and to avoid the accumulation of excesses. If this objective is to be attained, no more money should be invested in inventories than is necessary for effective support.

Therefore, accurate and current records of quantities of specific items in the inventory must be available for use in determining whether user requisitions can be satisfied and whether, on the basis of requirements computations, procurement actions are necessary. This entails controlling and accounting for the massive volume of transactions which daily affect the status of the over 4 million items in the inventory.

As a part of inventory control and accounting, the Department of Defense has directed that all items held in stock be physically inventoried not less than once each year either by full count or by statistical sampling techniques; however, exceptions are permitted for slow-moving items and other items, provided that storage con-

ditions and lack of movement insure adequate physical protection and accuracy of records.

Also, the Department of Defense has directed that inventory records and reports be reconciled promptly on the basis of physical inventories.

Each of the three military departments and the Defense Supply Agency has published policies and procedures which implement the Department of Defense policy. In addition, the procedures of the military departments provide for special physical inventories which are one-time unscheduled physical counts of one or more line items (1) when the stock record shows a balance on hand but the warehouse indicates no stock physically available to fill a request for the material, (2) to correct a suspected discrepancy between the recorded stock record balance and the assets on hand, and (3) on request from the inventory manager or another appropriate official.

These special inventories are recognized by all the supply components of the Department of Defense to be emergency measures which are not meant to substitute for the scheduled physical inventory program.

Chairman PROXMIRE. Is there any substantial difference in the actual procedures which they purportedly follow? I know there are sharp differences you have highlighted in your analysis of the way they actually handle these things. But in the orders they provide, are there substantial differences between the Army, Navy, and Air Force?

Mr. STAATS. I believe this comes out a little bit further, Mr. Chairman; if not fully, we will amplify it.

Chairman PROXMIRE. Please proceed.

Mr. STAATS. Last May, before this subcommittee, we expressed some concern over the need for substantial improvements in inventory control within the Department of Defense. The inaccuracy of inventory records, and the consequent adverse effect on the efficiency and economy of inventory management within the Department of Defense has been the subject in the past of a number of reports by the General Accounting Office.

EFFECTIVENESS DEPENDENT UPON ACCURATE RECORDS

Chairman PROXMIRE. Isn't it true it is not only a matter of efficiency and economy but also a matter of having the records accurate and available so that you can give the maximum kind of support to the troops in the field, in Vietnam?

Mr. STAATS. This is probably under the present circumstances, a more important consideration than the dollar costs involved.

Chairman PROXMIRE. And you cannot do that with full efficiency unless you have an accurate and up-to-date inventory.

Mr. STAATS. That is correct.

TWELVE REPORTS ISSUED BY GAO ON INVENTORY CONTROL

We have done quite a number of reports on this subject. I believe, if I am not mistaken, there are around 12 fairly major reports in this area in the time since 1962. I believe they have all contributed to the objectives which you have indicated.

The internal audit organizations within each of the military services have also consistently pointed out a number of serious defects in this area. The problem area continues to be one which, in our opinion, needs considerable attention.

DOD HAS \$37 BILLION STORES INVENTORY

Inventories in the Department of Defense are valued at about \$37 billion, excluding aircraft, ships, and supplies and equipment in the hands of using units.

Chairman PROXMIRE. Do you have any overall figures including these aircraft and ships and so on?

Mr. STAATS. I do not have. We would be glad to see if that is available. If so, we will be glad to put it into the record.

SUMMARY OF DOLLAR VALUE OF WEAPONS AND OTHER MILITARY EQUIPMENT AND SUPPLY SYSTEMS INVENTORIES IN THE DEPARTMENT OF DEFENSE AS OF JUNE 30, 1964-66

In billions of dollars]

	Army	Navy	Air Force	OSD and other Defense agencies	Total
June 30, 1964:					
Weapons and other military equipment in use..	9.2	38.2	33.6	0.03	81.0
Supply system inventories.....	10.5	11.6	10.8	2.2	35.1
Total.....	19.7	49.8	44.4	2.2	116.1
June 30, 1965:					
Weapons and other military equipment in use..	9.4	41.2	34.3	.03	84.9
Supply system inventories.....	11.2	12.8	11.0	2.0	37.0
Total.....	20.6	54.0	45.3	2.0	121.9
June 30, 1966:					
Weapons and other military equipment in use..	9.6	42.9	35.1	-----	87.6
Supply system inventories.....	11.9	12.7	11.0	2.0	37.6
Total.....	21.5	55.6	46.1	2.0	125.2

Source: Real and personal property of the Department of Defense as of June 30, 1964, 1965, and 1966. Figures for 1967 not available as of Dec. 12, 1967. Totals have been rounded to nearest \$100,000,000.

Representative RUMSFELD. As of what date is that?

Do you have comparative figures on inventory evaluation?

Mr. STAATS. This is a 1966 figure, Congressman Rumsfeld. I am sure we can give you comparative data. You are thinking, I assume, in terms of the buildup, what has happened, as to whether this is approximately level.

Representative RUMSFELD. We are talking about a problem which comparative figures for 1965, 1966, and 1967 would be useful in evaluating.

Mr. STAATS. We will be glad to provide that.

(NOTE.—See app. 14, p. 624, for fiscal 1967 date subsequently provided the subcommittee.)

On November 14th of this year, we issued a report to the Congress on the results of our review of inventory controls over that portion of this inventory which is held in depots in the United States. These inventories totaled \$10.4 billion in spare parts, components, and supplies, exclusive of ammunition and vehicles. (See text of report in app. 5, p. 513.)

We found in our review that significant differences existed between stock record balances and the actual quantities of items in depot inventories throughout the supply systems. This was evidenced by frequent and voluminous adjustments being made to the stock records by the services. We found that the inventory records were adjusted up or down, that is, gross adjustment, an average of \$2.4 billion annually in fiscal years 1965 and 1966.

Factors which we feel contributed to the significant amount of inventory adjustments were (1) inaccurate stock locator cards; (2) physical inventories frequently made without proper control of documentation for receipts and issues occurring during the period of the inventory; (3) lack of proper reconciliations between the physical inventory counts and the stock records at the completion of these inventories and determinations as to the causes of the imbalances; and (4) failure of supply personnel to follow inventory control procedures.

Following are examples of some of the conditions noted in our review and included in our report. A draft of this report was submitted to the Department of Defense for comments prior to its issuance to the Congress. These examples, we believe, demonstrate the extent and significance of inventory control problems and the impact that loss of inventory control has on the functioning of the military supply systems.

Significant differences between stock records and actual inventories:

One. The Navy Supply Center, Norfolk, had an average inventory of \$442 million. Approximately 61 percent of the records for the 239,000 items physically inventoried during fiscal year 1965 and 1966 contained significant errors requiring gross inventory adjustments totaling \$33 million.

Chairman PROXMIRE. Does this mean they are off by 8 or 9 percent?

Mr. STAATS. That is right. As to the dollar relationship to the total inventory, but it would be somewhat higher with respect to the value of the items actually inventoried.

Two. As a result of special physical inventories taken in fiscal year 1966, the Oklahoma City air materiel area found it had over \$37 million worth of assets in store which were not reflected on either the stock records or the locator records.

Chairman PROXMIRE. Are these typical or how were they selected?

Mr. STAATS. These were selected on the basis of the different kinds of situations, Mr. Chairman. I think that was it, and to go into different services.

Chairman PROXMIRE. It wasn't because there was a complaint, that you thought perhaps this was a bad situation that ought to be investigated?

Mr. STAATS. No; I don't believe there was any background of that kind that was involved here. I think it was more an effort to try to get into different kinds of situations.

Chairman PROXMIRE. So there is no reason to suspect that this was atypical.

Mr. BAILEY. No. We tried to take representative areas, in each one of the services, depots or air materiel areas, where we felt we could get an indication of what the situation was with respect to inventory.

Representative RUMSFELD. Just so that I will understand exactly what No. 2 means, the Oklahoma City air materiel area has what volume that we are comparing the \$37 million against?

Mr. BAILEY. About \$600 million, I believe, would be a ballpark figure of their inventories, their assets.

Representative RUMSFELD. And this is part of the Air Force?

Mr. BAILEY. It is part of the Air Force.

Representative RUMSFELD. How many such air materiel areas are there?

Mr. BAILEY. There are six materiel areas.

Representative RUMSFELD. So this is one of the six?

Mr. BAILEY. Five; I beg your pardon.

Representative RUMSFELD. So this is one of the five, and we are talking about \$37 million out of \$600 million, which was not reflected on either stock records or locator records?

Mr. BAILEY. That is correct, sir.

Representative RUMSFELD. Thank you.

Mr. FASICK. May I clarify that a little bit?

This \$37 million doesn't represent a wall-to-wall inventory as such. This just represents those adjustments they made as a result of special inventories they took during this period of time.

Chairman PROXMIRE. Do you have any notion of how big an inventory they took? What is a fair comparison? Did they take half of it?

Mr. FASICK. The Air Force does take complete inventories in addition to special inventories. A great bulk of the complete, or regular inventories are inventories taken on the basis of statistical sampling. Sensitive or high-valued items are supposed to be completely inventoried once a year, and the lower valued items are sampled. In that sense, you don't have a complete wall-to-wall depot inventory.

Chairman PROXMIRE. You say it is not complete. There was not an inventory, apparently, of the full \$600 million of equipment; is that what you are saying?

Mr. FASICK. That is right.

Chairman PROXMIRE. What would the \$37 million be compared with? It is in comparison to how much inventory?

Mr. FASICK. That would be very difficult, sir, to relate to another figure.

Chairman PROXMIRE. It would be difficult for us to analyze its significance. If there was only an analysis of \$100 million worth, this is a fantastic overage. If it is \$600 million, it is bad but not quite as bad.

Mr. BAILEY. These were special physical inventories taken under the conditions mentioned earlier in Mr. Staats' statement. That is, when a stock record shows a balance on hand but the warehouse indicates they have no stock available to fill that item, or to correct a suspected discrepancy between the stock record and the assets on hand, or on request from an inventory manager or other official. In other words, these were special physical inventories.

Representative RUMSFELD. But the figure you would compare it against would be something between \$37 and \$600 million, and you would have to further define it down by saying that it was things that were keyed as special items to be looked at or special areas. These were problem areas.

Mr. STAATS. In either of these three circumstances which we have indicated, in order to be able to give you direct dollar comparisons, we would have to go back and price out those particular items.

But I think the overall point that we are making is that the system, itself, was not adequate to produce the kind of information which was needed under these particular circumstances.

Chairman PROXMIRE. That is right. You see, it is difficult for us to assess this. If you could, as you go along, and I know it is hard to do it, and don't do it unless you feel it is responsible and proper to do it, but when you indicate an error if you could put in perspective by indicating what would be a standard, either in private business or in Government, it would be helpful.

Mr. STAATS. That is quite right. It is something we need to do more of in all of our reporting and we will be doing more of it. You do need this kind of information to put it in perspective. I don't know whether we could give you an approximation as to what the \$37 million represented out of the \$600 million, but we will check to see if there is any way we can give you that kind of an estimate.

Senator SYMINGTON. May I ask a question, please?

Chairman PROXMIRE. Senator Symington.

Senator SYMINGTON. Mr. Comptroller General, I am sorry I was late. I have read your statement in part. In looking at item 1 on that page, 61 percent looks pretty high. That is an error in operation and not an error in system, is it not? I don't know how they do an inventory there. I don't know whether it is on a bin basis, bin maximum, whether it is an annual point of replenishment basis, past experience, or what it is. But if you are 61 percent off, that is simply poor operation, is it not?

Mr. STAATS. It would be 61 percent of the items inventoried on which the errors totaled out to the \$33 million.

Senator SYMINGTON. Wouldn't that simply be improper handling?

Mr. STAATS. I think that would be correct.

Senator SYMINGTON. So that, in itself, wouldn't be a criticism of the system would it?

Mr. STAATS. We tried to identify the source of the error on the previous page. There were four different things involved in these errors, inaccurate stock locator records, physical inventories made without proper control of documentation and receipts, lack of proper reconciliation, and failure of supply personnel.

Senator SYMINGTON. I read those four, but I would think that in any business you would have the same problem, if you didn't have it operated properly. Having read those four, that was my point about the top of page 5. There doesn't seem to be anything wrong with the system, but as I read to this point, it seems to be the way the system is operating.

Mr. STAATS. I think this will be one of the things the Defense Department will be looking at, how much of this is the fault of the system and how much is the fault of the way it is being operated.

I might add here, as I think it is pertinent, we were advised informally as of yesterday that the Defense Department is going to set up a high-level task force to go into this whole problem of the inventory control and inventory management.

One of the purposes, I am sure, is to deal with the question of how much improvement they need in the system, and how much of it involves faulty administration of the present system.

Senator SYMINGTON. Thank you, Mr. Chairman.

ERRORS IN STOCK LOCATOR RECORDS

Mr. STAATS. The second category is "errors in stock locator records."

First. A systemwide error rate of about 13 percent was found to exist in Navy stock locator records as a result of location audits performed at 23 Navy stock points during fiscal years 1965 and 1966. The location audits revealed that 778,000 of the 6 million audited stock locations were discrepant. The discrepancies included (1) materiel in storage but not shown on stock locator records; and (2) actual storage location did not agree with recorded storage location.

Chairman PROXMIRE. How does this affect operations?

Mr. BAILEY. For example, you cut a materiel release order for a warehouse to deliver certain items to fill a user's requisition. You go out and look for that item in the warehouse and it isn't where it is stated to be. You don't fill that requisition until you either find the materiel where it happens to be or acquire some more materiel to fill the requisition. You simply can't find it.

Chairman PROXMIRE. Thank you.

Mr. STAATS. Second. An analysis of 3,475 materiel release denials processed by the Sharpe and Red River Army Depots during a 3-month period ending September 1966 disclosed that 1,232 or about 35 percent, of the denials were caused by a mislocation of stored stocks.

Chairman PROXMIRE. At this point, that means the stock was there but not so recorded.

Mr. STAATS. That is right.

Chairman PROXMIRE. How much work, cost, and delay was occasioned by this? This happened in 1965-66. I assume it was rectified. Have you had a chance to follow up to see if it was rectified?

Mr. STAATS. Mr. Fasick tells me that in cases of these situations they would take special inventories to try to correct it. These were all examples which were developed in the course of our reports and we gave them to the Defense Department for comment.

I do believe that the Defense Department has, in all of these cases where we have called it to their attention, taken corrective action. But what we were concerned with was the broader problem of whether the system as a whole was functioning in the way in which it should.

Mr. BAILEY. Mr. Chairman, it might be appropriate at this point to point out that if you don't find the item where it is supposed to be in the warehouse, you have to go looking for it. Consequently, there is an expenditure of time by the people that are involved; there is a delay in filling the customers' requests for the item, and these are expensive propositions when you have to go out on an individual line item basis and take an inventory and try to locate materiel that should be at a particular location.

Senator SYMINGTON. You either do that or you buy equipment on the basis that you haven't got it, don't you?

Mr. BAILEY. Yes, sir.

Senator SYMINGTON. If you had a warehouse superintendent in private business like that, you would give him his pay as he left that night, but in Government he has a rather entrenched position, does he not?

Mr. STAATS. You don't have the flexibility that you have in private industry, Senator Symington. Part of the difficulty, I believe, that we would identify all through this is the rotation of personnel and the turnover of personnel has undoubtedly contributed very substantially to the problem.

Chairman PROXMIRE. How about the training of personnel?

Mr. STAATS. This is another area that we think needs more attention.

Mr. WEITZEL. In addition to the deficiencies in the system, itself, have to give consideration to the deficiencies in the system, itself.

At these two Army depots that were mentioned, Sharpe and Red River, we felt that adequate controls didn't exist to provide reasonable assurance that assigned warehouse locations for storage of incoming material receipts were being recorded in the computerized locator records and that incoming stocks were being stored in designated warehouse locations.

The stock locator division was responsible for assigning warehouse storage locations. The data processing division was responsible for input of assigned stock locations into the computerized locator record, and the storage division was responsible for the storage of the stocks.

There wasn't any central control, so far as we could find, over the interrelated functions of these divisions to provide assurance that the materials were being stored in the designated locations and that the storage locations were being entered in the computerized locator records.

So it wouldn't be sufficient to follow up just on these particular 3,745 release denials and find out what happened. There would be further work to be done to devise some coordination or some control to improve the system.

Representative RUMSFELD. In any of these instances has any individual who has been responsible been relieved.

Mr. STAATS. I could not answer that.

Mr. BAILEY. Not to our knowledge. I wouldn't be able to answer that.

Mr. STAATS. We can check.

Chairman PROXMIRE. Would you check that for us and let us know what has been done?

Mr. STAATS. Yes.

INFORMAL REPLY BY MR. PAUL H. RILEY, DEPUTY ASSISTANT SECRETARY OF DEFENSE (SUPPLY AND SERVICES)

In response to the subcommittee's question, we requested the Department of Defense to determine whether any individuals responsible for errors in the inventories of the military departments and the Defense Supply Agency had been relieved of their duties. Officials of the Department of Defense indicated to us that differences between the inventory records and physical quantities on hand generally result from an accumulation of errors in a number of transactions over varying time periods. When these differences are disclosed through the taking of physical inventory, because of the volume of transactions processed and the complexity of the data processing systems, it is impracticable to attempt to reconstruct a historical record that would identify the different individuals who had participated to some extent in the total processing of the transactions that contributed to the error.

Officials of the Department of Defense, the military departments and the Defense Supply Agency recognize the desirability of identifying the responsibilities of organizational elements and personnel with the functions performed. They also recognize the importance to measuring the effectiveness and efficiency with which these responsibilities are carried out. However, accumulating data by individual on the tremendous volume of transactions handled has not been considered to be practicable in the past.

Mr. STAATS. We found that the Navy Supply Centers, Norfolk and Oakland, did not have effective controls over receipts to insure that materiel was properly stored and entered on the records within the prescribed 5-day period.

At Norfolk, we tested the receipt processing time required for 54 receipts of materiel which were logged in at a central receiving warehouse during the period February 1966 to July 1966. We found that the processing time required for 38, or 70 percent, of these receipts ranged from 6 to 72 days. We also found that three materiel receipts, valued at about \$34,000, had been in storage for varying periods up to 200 days but had not been entered on the records.

EXCESSIVELY LARGE NUMBER OF SPECIAL INVENTORIES

As a result of the extensive differences between stock records and actual inventories, DOD supply activities resort to a large number of special inventories to resolve the differences and to locate missing stocks. For example:

One. The data furnished to us by the Army Materiel Command indicate that its depots, which are responsible for 514,000 line items of depot stocks, conducted over 900,000 special inventories between January 1965 and June 1966.

Chairman PROXMIRE. Just that figure seems shocking.

What does this really mean? Is this prima facie evidence of something being wrong?

Mr. STAATS. We think so.

Chairman PROXMIRE. How can we assess this? What does a special inventory mean? Do they do this when they find there is a discrepancy, then they go and do a special inventory?

Mr. STAATS. That is correct.

Mr. BAILEY. This goes back to those same three factors that I mentioned earlier in connection with special inventories. They either couldn't find the stock when they went to look for it, they felt that there was some discrepancy that they wanted to resolve, or an inventory manager had asked for a special inventory to see what the actual situation was with respect to the item.

Chairman PROXMIRE. Is there anything in the history of this with regard to time that we can compare it with? Is this a big increase over what happened before or is it less? Is there any way of knowing?

Mr. STAATS. We don't have figures.

These refer to a summary of special inventories conducted over an 18-month period. The result indicates that the problem is there.

Chairman PROXMIRE. Does it indicate the problem is growing?

Mr. STAATS. I could not answer that question, whether it is worse or better.

Chairman PROXMIRE. Can any of your staff answer that question?

Mr. FASICK. I think it has grown in the last couple of years, primarily because of the workload placed by the Vietnam buildup. So the

problem I think is more acute in the last couple of years than it was before, although it has always been serious.

Senator SYMINGTON. Mr. Chairman?

Chairman PROXMIRE. Senator Symington.

Senator SYMINGTON. Based upon what Mr. Weitzel said, Mr. Comptroller General, does this mean that they had to search for the 92 items five times in 30 days?

Mr. BAILEY. Yes, sir; this is correct.

Senator SYMINGTON. What happens when that is done? He goes out and says, "I haven't got it," and they say, "Go back and look again," or does he say he does have it and they find out later he is wrong?

What is the chronological procedure of looking five times for one piece in a 30-day period? How can that happen? I just don't understand the way it works.

Mr. STAATS. The sequence of it?

Senator SYMINGTON. Yes.

Mr. BAILEY. Again, if they receive five requisitions for a particular item and went out and counted it and didn't make appropriate adjustments in the inventory records, the next time they receive a requisition they may have to go back and count again in order to find the materiel, or if the location is changed, something of this kind, and it doesn't get into the records with an appropriate indication—

Senator SYMINGTON. I don't want to belabor this, but if you were in private business the man in the shop would try to correct it himself. He wouldn't just say, "It isn't right. Let's go have lunch."

Isn't there some way?

It is hard to visualize missing the same piece five times in that period of time.

Mr. WEITZEL. They have told us for one thing they are trying to develop new overall systems, for another thing concentration of manpower on trying to fill the orders for the buildup in Vietnam has prevented proper attention in some cases to these errors.

It may result simply in their feeling that they can't depend on their inventory records so every time they get a requisition for the item they go out into the warehouse and start looking.

Senator SYMINGTON. That would seem to be the logical answer.

Chairman PROXMIRE. What they need is a dependable system and then they wouldn't have to conduct these special inventories. As long as they don't have it, they have to do it over and over again.

Mr. WEITZEL. It should greatly minimize the necessity for special inventories if regular inventories can be taken at regular times.

Chairman PROXMIRE. This must also be very wasteful in terms of personnel. Special inventories take time.

Mr. WEITZEL. In the long run, it can take more time, as Mr. Staats testified.

In these 900,000 special inventory cases, as an average every item was counted 1.7 times during the 18-month period.

Senator SYMINGTON. I jumped the gun on you a little bit. I read No. 3 on page 7. I believe that is the worst thing I have seen. They ought to give a prize to the fellow who missed the most.

Mr. STAATS. I think the general point Mr. Weitzel was referring to comes out a little bit more in the text.

From this it appeared that in addition to regularly scheduled physical inventories, it was necessary to count each item an average of 1.7 times during the 18-month period. However, some items were counted many times. For example, one depot conducted, within a 30-day period, five or more special inventories for each of 92 items.

Two. For fiscal year 1966, the Air Force Logistics Command indicated that its five active air material areas (AMA) had conducted special inventories of 277,254 line items. This number of special inventories are equal to about 30 percent of the total items in their inventories.

Three. At the two Navy supply centers included in our review, we found that, in fiscal years 1965 and 1966, approximately 90 percent of the inventory effort was concentrated on special inventories.

Chairman PROXMIRE. This is the horrible example that Senator Symington referred to.

Senator SYMINGTON. That means that 90 percent of your normal inventory effort was ineffectual.

Mr. STAATS. It means it did not solve the problem of being able to yield the information that you needed as of a given time, and, therefore, were exerting manpower and losing time doing something which, with the proper investment either could be eliminated or minimized.

Chairman PROXMIRE. Even though there was an understandably difficult situation with the Vietnam war escalation taking place just during this time, the Vietnam effort would have been aided substantially, it would seem to me, by accurate, up-to-date records where you wouldn't have to go through this special inventory.

Mr. STAATS. That is right. I think we indicated in the previous hearing, Mr. Chairman, we are making at the present time, a special review in Southeast Asia, in part trying to get at this problem of improving the supply lines into Vietnam. We are getting good cooperation from Defense on it.

I think you are quite right in saying that what we are after here is improvement of the way the system responds to the need, the need of the Defense Department.

Chairman PROXMIRE. What we need is the assurance that vigorous action is being taken by the Defense Department in this area, and progress reports so we can measure it with some objective criteria. After all, this took place 2 years ago, 1 and 2 years ago, 1965 and 1966, so we should know whether improvement is being made now and we ought to have, as soon as possible, a further audit so we have a comparative basis.

Mr. STAATS. What we could do here, as we do in many other special types of audit situations, where we go in and make this kind of review we go back in after a reasonable period of time to see what has been done to improve the system, to determine whether there has been action taken to deal with the problem which we identify and which they agree with.

PROGRAM REPORTS NEEDED

Chairman PROXMIRE. I know you have the ability and the experience to give an appropriate study to that, but we want the reports for this committee, if we can get them, on a progress basis.

Mr. STAATS. All right.

In our opinion, the widespread use of special inventories in lieu of improved inventory control practices is costly and ineffective. The extensive workload associated with taking these special inventories frequently restricts the taking of systematically scheduled physical inventories.

INADEQUATE INVESTIGATION OF DISCREPANCIES

We noted instances in which a series of offsetting adjustments to the records on individual items of supply were made without adequate investigation to determine the reasons for the discrepancies.

Chairman PROXMIRE. I remember when Mr. Morris testified, he said that the Defense Department wasn't much different than private industry. He said that the almost 25-percent error which you pointed out in their overall inventory, \$10 billion, roughly, and \$2.5 billion off, he said these balanced out and the actual discrepancy was only actually between 1 and 2 percent which compared favorably with Sears, Roebuck. Is this the appropriate time for you to deal with that?

GAO DISAGREES WITH DOD ON DISCREPANCIES

Mr. STAATS. We deal with that a little later.

The short answer is we don't agree with him for reasons which we spell out later. (See p. 220.)

I will repeat myself a little bit.

We noted instances in which a series of offsetting adjustments to the records on individual items of supply were made without adequate investigation to determine the reasons for the discrepancies. For example:

One. At one Defense Supply Agency center, we noted a series of six adjustments made in about a 1-year period to the records for water chlorination kits. These six adjustments ranged from a minus adjustment of 9,404 units to a plus adjustment of 11,829 units. The result of this series of adjustments was a net increase to the records of 1,225 units.

Personnel of the center concluded that no further investigation or corrective action was necessary on this item inasmuch as the series of adjustments appeared to be offsetting.

EXAMPLE OF INVENTORY ADJUSTMENTS

Senator SYMINGTON. Would you give the sequence of that? Over what period of time did you go from a minus 9,400 to a plus of 11,800?

Mr. BAILEY. Senator, I will give you the sequence in which these adjustments were made.

In May 1965, on the basis of a physical inventory of the item they increased the quantity by 11,829 units. In September, they made an additional plus adjustment; in other words, added to the number, 640 units. There is no reason given for that adjustment.

Then in 1966, in January, they took a physical inventory and they decreased the item by 8,341 units.

Senator SYMINGTON. They found 8,000 less than they thought were there?

Mr. BAILEY. Less than they thought were there; yes, sir.

Then in March they took another physical inventory, a special physical inventory, and added 5,201.

Senator SYMINGTON. Was that because they didn't find the 5,000?

Mr. BAILEY. They found 5,000 more than they thought they had.

Senator SYMINGTON. These were not additional purchases?

Mr. BAILEY. No, sir.

Chairman PROXMIRE. None of these represent purchases, I understand. These are all adjustments.

Mr. BAILEY. These are adjustments to the stock records; yes, sir.

Then in April, they added another 1,300 units. The reason for this adjustment was not stated.

Then in June, they took another special physical inventory, apparently because of some discrepancy or other, and reduced the inventory by 9,440 units.

Senator SYMINGTON. How could they do that? They probably put all identical items in one part of a shop. How could they have gone up and down and sideways that way, five, nine, 11?

Mr. BAILEY. All of these items are not necessarily in the same location in a warehouse. They may have them in separate locations in a warehouse.

Senator SYMINGTON. You are not speaking about any particular group of items?

Mr. BAILEY. This is one line item; a water chlorination kit.

Senator SYMINGTON. Then why wouldn't they put them all in one place or reasonably close to one place? Why would they spread them around?

Mr. BAILEY. Sometimes they may have all of a particular place filled with this item and may have to put it in another place.

Senator SYMINGTON. But you say this is at one Defense Supply Agency center—one place.

Mr. BAILEY. Yes; but the locations in the warehouse may be several locations.

Mr. WEITZEL. It may be the locations where these are supposed to be kept are filled up when another shipment comes in and they have to have a place to put it, so it goes somewhere else rather than reshuffle everything else.

Our problem there was that they didn't seem to follow up on why these adjustments were necessary and what should be done to prevent them.

Mr. STAATS. Two. As a result of physical inventories taken in four Army depots during 1966, inventory adjustments totaling about \$197 million were made to the stock records without research and reconciliation of major stock variances. Our tests of some of these adjustments showed that the adjustments were in error. If reconciliations had been made of the discrepancies, it would have become clear that the differences could have been accounted for by transactions in process.

Senator SYMINGTON. Just to be sure I understand, what do you mean without research and reconciliation of major stock variances?

Mr. BAILEY. In other words, attempting to find out why they have these differences between the physical inventory on hand and what the

stock records show is on hand. They make the adjustment without attempting to find out why this difference.

Senator SYMINGTON. Why do they make the adjustment?

Chairman PROXMIRE. They found there was an error.

Senator SYMINGTON. What kind of an error, an error in inventory or in figures?

Mr. BAILEY. They will determine they have so much stock on hand on the basis of physical inventory. They say, "Okay, we will change our records to show this much stock on hand." But they don't go back to find out why did the records show they had this other stock on hand.

Chairman PROXMIRE. Proceed.

PREScribed PHYSICAL INVENTORIES NOT TAKEN

Mr. STAATS. One. Overall data for the period February 1965 to June 1966 submitted for the 20 Army depots show that none of the depots performed the number of regularly scheduled physical inventories or location audits required by Army regulations. In many instances, complete counts of items were omitted and, in some instances, required sample inventories were omitted.

Furthermore, five of the depots performed no location record audits. The reasons given for these failures to conduct scheduled physical inventories were (1) utilization of personnel resources for special inventories; (2) conversion to new or revised major logistical systems; and (3) the workload caused by the Southeast Asia buildup.

Chairman PROXMIRE. Mr. Morris testified this had been rectified. His testimony, or that of his assistants, was that this was during the Vietnam buildup period, that they deliberately suspended inventories, knowing they would have a tremendous demand for personnel and so on. But they have now begun taking these inventories.

Is this your understanding, also?

Mr. STAATS. I do know that on these specific cases, as I indicated earlier, when we called them to their attention, we have not had difficulty getting them to respond to them, to make corrections.

But I don't have, personally, information as to whether in this particular situation involving the 20 Army Depots, they have been corrected.

ARMY WILL NOT BE ON SCHEDULED INVENTORIES UNTIL 1969

Mr. BAILEY. We understand, Mr. Chairman, that it will take the Army until about 1969 to get back on schedule for taking physical inventories.

Chairman PROXMIRE. This should be a lesson to all of us, I take it. It is your conclusion, and certainly my conclusion, that this was a serious mistake, suspending this physical inventory. We would be much better off in supplying troops in Vietnam, not only in terms of economy, which is important at all times, but in terms of a more effective military effort, if they had the physical inventory and knew where the supplies were.

Mr. STAATS. That is right.

Chairman PROXMIRE. In terms of timing and getting what you need there at the right time, you are much better off if you know what you have and where it is.

Mr. STAATS. That is right.

Representative RUMSFELD. Mr. Staats, isn't it correct to say that the problems that come with the buildup are no great surprise to the U.S. Government, and that we have gone through previous buildups of a less substantial nature? Certainly with the Berlin situation there was a change in the activity level, and there were similar problems discovered during the Berlin buildup period. Isn't this correct?

SYSTEM NEEDS IMPROVEMENT

Mr. STAATS. Yes; I am sure this is true. Of course, in any of these emergencies, no one can be sure at the time they occur what period of time is to be involved, or, for that matter, what the size of the buildup will be. I think it is important to keep it in perspective to the total size of the problem.

Given the size of the problem undoubtedly there will be errors and mistakes made if you have an uncertain situation ahead of you. But we believe, and I don't believe we have basic disagreement in the Defense Department on the central point, that the system, itself, needs a lot of attention and a lot of improvement.

If these regulations had been followed and there had been the manpower allocated to conduct the physical inventories in these 20 locations, I think, looking at it hindsight-wise, they would agree it was a mistake for them to have not continued them.

SYSTEM SHOULD BE CAPABLE OF EXPANSION FOR BUILDUP

Representative RUMSFELD. What I am saying is that Mr. Morris, and, in fact, those of you who have testified from the GAO, state periodically that the problem has to be considered in perspective, that there was a buildup.

My point is we have had previous buildups since World War II. We know, I would think, by now what happens when there is a buildup. We know that there is a greater demand and stress put on the systems, plural.

It would seem to me that recognizing the nature of the world we live in, we would be well advised to see that the system is so developed and constructed that it can expand for a buildup. I am a little bit tired of hearing, "But there was a buildup." It didn't just happen. People knew it was going to happen.

The people involved in making the decisions for the buildup to take place were also the people who have the responsibility for seeing that the system is capable of handling a buildup. I don't think that is an unreasonable position.

Mr. STAATS. No; I wouldn't quarrel with your basic point that the system should be capable of responding to this kind of a buildup.

Representative RUMSFELD. If this were the first time it happened since World War II, one might say, "Well, surprise; we were caught with our hands in our pockets." But it wasn't.

Mr. WEITZEL. Paradoxically enough, Mr. Rumsfeld, some of the very things they have tried to do to improve the system, they report, and I think our people would confirm, have caused some of the problems.

For example, computerizing some of the systems. The Defense Department said that would introduce transitional difficulties due to trying to control the stocks from remote locations. In other words, they had to work out some of the problems that the new system had originally built into it.

USE OF COMPUTERS

Mr. STAATS. To get really effective control, you have to use computers very extensively. This is a mammoth job, as I think you will appreciate.

I am convinced, myself, that the Government is behind private industry in using computers in this area of supply management. The size of the job, to be sure, is larger. There is no private enterprise even close to the size of the Defense Department's inventory management problem.

But, nevertheless, without the use of the computer, I don't believe we are ever going to get on top of the situation.

Senator SYMINGTON. Mr. Chairman?

Chairman PROXMIRE. Senator Symington.

Senator SYMINGTON. You mentioned it would take the Army until 1969 to get its inventories straightened out.

Would you care to comment about the Navy and the Air Force?

Mr. BAILEY. In the Air Force, the Air Force has been making physical inventories pretty much on schedule.

The Navy is somewhere in between. I don't know that we have any time factors with respect to the Navy.

Senator SYMINGTON. Thank you.

NINETY PERCENT OF INVENTORY EFFORT ON SPECIALS

Mr. STAATS. No. 2. Another case we have is: The two Navy locations included in our review were required to perform scheduled inventories annually on approximately 920,000 line items in fiscal years 1965 and 1966. However, during these fiscal years, less than 6 percent of the scheduled inventories were taken. Special inventories accounted for 90 percent of the inventory effort.

Chairman PROXMIRE. Was this on a directive of the Secretary of Defense? Was there a formal order in which this was decided as a matter of policy? Where was this decision made that the inventories required would not be taken in 94 percent of the cases?

Mr. STAATS. At the local level, I am advised.

I am also advised that there was no general statement of policy to the effect that this would be done.

Chairman PROXMIRE. Isn't this a violation of orders?

Mr. STAATS. I think this would be correct.

Chairman PROXMIRE. It seems to me it would be subject to some pretty serious discipline.

One thing, if they missed a few, that would be one thing. But they only took less than 6 percent of the scheduled inventories.

Mr. STAATS. The question we would have to check into is whether or not they had been allocated the necessary personnel and funds to do this. If they had the funds and personnel to do the special inventories, it is a little hard to see why they wouldn't be able to do the regular inventories.

Chairman PROXMIRE. Would this be known by the Secretary of the Navy or the Secretary of Defense until you disclosed it on the basis of your studies?

Mr. STAATS. I could not answer that.

Mr. FASICK. Yes, sir; they would be known in the sense that there were quite a number of internal reports of the individual services, internal audits, where this was pointed out and should have come to the attention of the secretarial level in the services.

Senator SYMINGTON. I would like to ask this question: If there was no general statement of policy there would be no order. How could a man at the working level violate an order?

Mr. STAATS. What I was referring to was the general regulations to provide for the inventory and they were not taken. They were allowed to slide.

Senator SYMINGTON. Just for the record, what do you mean there was no general statement?

Mr. STAATS. There was no specific statement of policy or directive, as far as I know, to give them permission to abandon the general regulations.

Senator SYMINGTON. In other words, it was on the negative side. I understand you. Thank you.

Mr. STAATS. Yes.

Three. Available data showed that Defense Supply Agency activities had about 1.9 million active line items on hand. During fiscal years 1965 and 1966, approximately 40 and 9 percent, respectively, of the DSA active items were physically inventoried by complete or statistical sampling methods. In addition, the data indicated that the DSA supply activities made less than 50 percent of the required location audits.

DSA officials indicated that one of the reasons for the substantial decrease from 1965 to 1966 in the number of line items physically inventoried was the workload associated with increased support to Southeast Asia. They indicated also that the failure to make the majority of the location audits was due in large part to a new depot warehousing and shipping system.

GAO FINDINGS REPORTED TO SECRETARY OF DEFENSE

At the conclusion of our review, we brought our findings to the attention of the Secretary of Defense along with our proposal that the military departments and the Defense Supply Agency be directed to take the necessary steps to attain an acceptable degree of stock record accuracy for depot inventories.

GAO PROPOSED A HIGH-LEVEL STUDY GROUP TO STUDY PROBLEM

We proposed further that the Secretary of Defense establish a group, composed of representatives from the military department and the Defense Supply Agency, to study the problems of inventory control in depth with an objective of resolving the broad basic causes for these problems and to make recommendations that will correct the conditions uniformly throughout the Department of Defense.

This is the task force, Mr. Chairman, which I referred to a while ago. Defense advised us yesterday they had decided to establish it.

The Department of Defense, in commenting on our draft report, in July 1967, concurred, in general, with our findings.

Chairman PROXMIRE. You say "in general." What disagreements were there?

Mr. WEITZEL. With the need for high-level management attention to the inventories, the importance and concern to the Department.

Chairman PROXMIRE. Did they disagree with that?

Mr. WEITZEL. No; they agreed in general.

Chairman PROXMIRE. My question was, What disagreements?

Mr. WEITZEL. The only point they reserved for further study, as I recall, was whether there should be established the high-level management group of the representatives from the military departments and Defense Supply Agency. They indicated they wanted to make a further study of that point. That is the one Mr. Staats said they have now agreed with.

Mr. STAATS. We should strike out the words "in general" in view of the information we received yesterday.

We were advised that each of the military services and DSA had initiated specific programs to eliminate the types of inventory control problems discussed in our report and each was in the process of installing new procedures which were aimed at more accurate inventory control.

I think this point was the reason that they did question the need at that point in time for the overall task force, but which they have now agreed to.

We were advised that the installation of the new procedures had advanced to the point where fruitful results could be anticipated within a relatively short period of time. We were told that the need for establishment of a special inventory study group would be reconsidered and, if necessary, organized after an evaluation of the results was obtained from the new procedures.

In testimony before this subcommittee on November 28, 1967, the Defense representatives testified that the material included in our report dealt with discrepancies that show up in a 4 million item inventory. The Defense representatives went on to say that the net difference between gains and losses in dollars was only 1 percent in 1965 and 1.4 percent in 1966 and that the largest merchandising houses consider 2 percent net adjustment to be quite satisfactory. (See p. 220.)

We recognize that in private industry a net adjustment figure (gains offset by losses) can be used to measure the extent to which profit or loss has been affected during a particular accounting period or the extent to which capital investment in inventories has been affected by inventory adjustment. However, this figure does not give a satisfactory indication of the effectiveness of inventory controls or the reliability of the inventory records. For these purposes, gross adjustment (the total of gains and losses) is a more meaningful figure.

An excessive volume of gross inventory adjustments is a clear indication that, in a large number of instances, the inventory accounts for specific items were inaccurate in relation to actual stocks on hand and, therefore, represented potential management problems.

In those cases where records indicate more stock on hand than actually exists, there is a distinct danger that when stocks are depleted,

orders cannot be filled. On the other hand, when the inventory records do not reflect all of the stock that is actually available, unnecessary procurements may be made and potential excesses generated. Since either of these conditions represent an unsatisfactory condition requiring management attention, it seems more appropriate that gross inventory adjustments be used as a measure of the effectiveness of the stock control practices and records.

Since the purpose of maintaining inventory records is to have accurate information available as to the quantities and location of stock on hand, an excessively high ratio of gross adjustments to average inventory is a strong indication that such inventory records are not accomplishing the purpose for which they are maintained and that necessary controls over the inventories are absent or inadequate.

NEED FOR STANDARDS FOR EVALUATIONS

Chairman PROXMIRE. This makes a lot of sense to me and I think it is a very good response to the position taken by the Defense Department.

I wonder, again, if you can give us some standard. Is there any basis for determining whether or not a 25-percent gross error is bad? It sounds terrible, but how do we know?

Mr. STAATS. I have been raising the same question with members of our staff. I think the only answer we can give you here is that it would be difficult to establish an overall standard. We think it is quite clear that this rate of gross inventory adjustment is higher than necessary and higher than we ought to live with.

Chairman PROXMIRE. Can you do it on the basis of consultation with the biggest and most competitive entrepreneurs? Sears, Roebuck has been brought up here. How about their gross adjustment? Do you know what that is?

Mr. STAATS. I am advised we are making this check. This is something which I have been pushing quite a lot. I do think we need, in this area as in many others, standards against which we can make a judgment as to the adequacy of an agency's operations.

In an organization as big as the Defense Department, you also have the risk of overall figures, either overstating or understating the problem in a particular vital operation in the Defense Department. That is another factor.

Chairman PROXMIRE. Once again, we can't compare it with a standard. Can we get anywhere by considering whether or not this is a deterioration of performance or whether, as bad as it is, it is an improvement?

Mr. STAATS. We do not have that information.

Chairman PROXMIRE. I hope we develop this over time.

Mr. STAATS. It would be very useful to have this, and we certainly want to move in that direction. I don't know at this point of time whether we can commit ourselves as to the feasibility of doing it. But I agree with you that it is a desirable thing to do, if we can do it.

Senator SYMINGTON. Mr. Chairman, I have to leave. If I may, I would like to congratulate you on these very constructive hearings, and also congratulate Mr. Staats and Mr. Weitzel, and the staff. I have known Mr. Staats over a quarter of a century now, and I think he

and his staff have saved the Government a good many millions of dollars.

As this committee continues to demonstrate, the Government could save a good deal more money in following the advice of experienced people. My staff and I intend to study this further.

Chairman PROXMIRE. Thank you very much.

There is no one who is more qualified, as everyone in this room knows, than Senator Symington, from his lengthy experience in both private business and in the executive branch of the Government.

Mr. STAATS. Thank you.

CONCLUSIONS AND ADDITIONAL ACTIONS REQUIRED

We believe that the increased emphasis which DOD has stated that the military services and DSA are placing on more positive enforcement of the existing policies and procedures for control of depot inventories should, if effectively pursued on a continuing basis, result in greater stock record accuracy and increased supply effectiveness.

However, on the basis of other studies we have made of inventory controls and supply system responsiveness, we believe that there are certain broad basic factors which have a significant bearing on the effectiveness of inventory controls in the Department of Defense.

For example, we believe that the organizational structure of the supply systems in some cases may contribute substantially to the difficulties encountered in control of inventories. The responsibility for physical receipt, storage, and issue of stocks of the same item is frequently decentralized to several storage activities.

The management and accounting responsibility for these same stocks is centralized at another supply activity which has no direct authority or control over the practices of the storage activities. Thus, it is difficult to establish responsibility for errors or loss of control because no single organization has the direct authority, responsibility, or perhaps motivation to reconcile differences and insure closer control.

Another important factor which we believe warrants considerable attention is the need for increased supply discipline throughout the supply systems. This is essential if the accuracy and completeness of inventory records and related supply management data is to be improved.

Frequently, we find that the services have devised adequate system and procedures, but the people upon whose actions the operation of the systems depends do not always do that which is required and when it is required. To the extent that people at all levels of the supply system are motivated to follow prescribed procedures and maintain a high degree of accuracy in their work, more accurate and complete management data and information will result.

We do not believe at this time that there is any need for specific legislation in connection with improvement of inventory controls. The basic responsibilities and authorities have been established. Rather, we believe that creative thinking needs to be applied to basic problems and causes such as organizational structure and supply discipline cited above.

It is to deal with basic factors such as these that we suggested a special study group within the Department of Defense should be established.

We believe the interest and concern with inventory controls evidenced by this subcommittee, as well as others in the Congress, is especially important in assuring that a high degree of management attention is focused on this problem. In other words, we believe the Congress and its committees can be a strong motivating factor to the departments to further their efforts in developing solutions.

For the immediate future, we intend to concentrate our efforts on study of the organizational structures, alinement of responsibilities and authority, and numbers and types of personnel involved in inventory management.

We also intend to examine more closely the policies, procedures, and practices used by the military services and DSA relative to the receipt and storage of material, and the processing of related transaction documents affecting the inventory records. In connection with this work, we intend to consider the organizational structure and methods used in commercial enterprises to determine if there are any techniques that may have application to the solution of inventory control problems in the Department of Defense.

Chairman PROXMIRE. Your investigation was made in February of 1965 and June of 1966—18 months ago. The Department of Defense is just getting ready now to do something about it. Is that right?

Mr. STAATS. As indicated here, they had not established the kind of overall study which we felt was necessary until now. They did have a number of things that were in process by the individual services and by DSA. That was their argument for not setting up the overall group at the time we made our report.

Chairman PROXMIRE. Who has been in charge of this in the Secretary of Defense's office?

Mr. STAATS. Until recently, Paul Ignatius, who is now Secretary of the Navy, was in charge. But Assistant Secretary Tom Morris has been moved fairly recently into this responsibility.

Chairman PROXMIRE. I was very much impressed by Mr. Morris. He is a most thoughtful and I know a dedicated man. I know he works 12, 14, and 16 hours a day, 7 days a week. How much experience has he had in this area?

Mr. STAATS. He has had rather considerable experience, going back to the previous administration. He was responsible for working with the Deputy Secretary, Reuben Robertson, in this area, when they were establishing the Defense Supply Agency.

Subsequently, after about a year in the Budget Bureau, he was appointed by Secretary McNamara to the present post that he holds. He served in that post for, I believe, approximately 3 years or $3\frac{1}{2}$ years, and became Assistant Secretary for Manpower.

After the appointment of Mr. Ignatius to the Secretary of the Navy post, Mr. Morris was returned to the present position which he now holds. So he has had rather considerable experience.

Chairman PROXMIRE. He has been in this position for how long?

Mr. STAATS. This is his second tour in this position.

Chairman PROXMIRE. And he has been in this position for how long? When did he take over?

Mr. STAATS. I don't know whether I can give you that.

Mr. WEITZEL. It must have been about August 1967.

With further respect to timing, Mr. Chairman, this review covered the period that was mentioned, but we did our fieldwork from May 1966 through March 1967 and, as a result of that, we sent a draft report to the Defense Department on May 3, 1967, with our findings and our recommendations, and in replying to this in July, on July 21, 1967, Mr. Riley, the Deputy Assistant Secretary of Defense for Supply and Services, in what is now Mr. Morris' area again, did call our attention to the fact that each of the military services and DSA had initiated specific programs to eliminate the deficiencies, many of which they had recognized, and Mr. Riley said, for example:

The Army initiated a six-phase program in September 1966. Three of these phases were completed by the end of December 1966, but not in sufficient time to be reflected in the draft report prepared by the GAO staff.

The major phases, which involve the establishment of new inventory procedures would be phased in between May and October 1967. Likewise, the Navy, Air Force and DSA are in the process—

he said—

of installing new procedures which are aimed at more accurate inventory control.

As we have already testified, they did defer action on the constitution of this high-level task force and have just now determined that they will go forward also with that.

Chairman PROXMIRE. Our experience has been that they are very cooperative, friendly, and responsive and then not much gets done, so often, as you know. So, we hope that we have follow up reports at regular intervals, as comprehensive as possible, so we can stay right on top of the situation.

Mr. STAATS. I have the exact dates that you asked for, Mr. Chairman. Mr. Morris was appointed to the post of Assistant Secretary of Defense for Installations and Logistics in January 1961 and served there until December 1964. He returned to this post in September 1967.

Chairman PROXMIRE. You may proceed.

Mr. STAATS. The second part of our testimony has to do with agency audit rights and recovery from subcontractors.

Chairman PROXMIRE. I am very interested in this.

Mr. STAATS. This is designed to elaborate and bring up to date the information on this subject.

AGENCY AUDIT RIGHTS AND RECOVERY FROM SUBCONTRACTORS

AGENCY AUDIT RIGHTS

About 2 years ago, we recommended to the Secretary of Defense that a provision be included in all contracts, required to be negotiated on the basis of cost or pricing data, giving agency officials the right to examine all records related to the contract performance. This recommendation was made to provide agency officials a more effective means of implementing the Truth in Negotiations Act, Public Law 87-653.

We had found that significant cost information was often not disclosed to Government negotiators at the time of price negotiations. Such undisclosed information could be more readily detected in post-award reviews of the contract performance records.

Although an examination of such records provided the best means of verifying that the data submitted before negotiations was accurate,

current, and complete, agency officials did not have the right to do so under negotiated firm fixed-price contracts and subcontracts.

This matter was discussed in hearings before your committee in May 1967.

In June 1967 both you and Congressman Minshall introduced bills to provide agency representatives the right to examine all data related to the negotiation, pricing, or performance of contracts and subcontracts where cost or pricing data are required.

In commenting on the proposed legislation in July 1967 we stated that we were in favor of its passage.

Thereafter, in September 1967, the Deputy Secretary of Defense directed that action shall be taken to include in all noncompetitive firm fixed-price contracts a contractual right of access to the contractor's actual performance records. The directive was silent on the agency's right of access to the subcontractor's records.

We advised Defense officials of this apparent omission, and we were advised that this matter would be considered in drafting the regulations. The Armed Services Procurement Regulation was revised November 30, 1967, effective as soon as received, to provide for an appropriate clause to be included in all contracts and subcontracts, where cost or pricing data are required. (Pertinent excerpts from the regulation are attached. For full text, see p. 162.)

(The information follows:)

ATTACHMENT A

EXCERPTS FROM DEFENSE PROCUREMENT CIRCULAR No. 57, NOVEMBER 30, 1967

Agency Audit Rights

"ITEM IV—REVISED AUDIT CLAUSES

"To provide adequate contractual coverage for access rights to contractor's records necessary to perform post-award reviews, when required under Public Law 87-653, changes have been made in the clauses in ASPR 7-104.41. Effective as soon as received, these revised clauses will be used in contracts as provided in 7-104.41 herein. * * *"

"7-104.41 *Audit and Records*

"(a) Insert the following clause only in firm fixed-price and fixed-price with escalation negotiated contracts which when entered into exceed \$100,000 except where the price negotiated is based on adequate price competition, established catalog or market prices of commercial items sold in substantial quantities to the general public, or prices set by law or regulation. * * *"

"AUDIT (NOVEMBER 1967)

"(a) For purposes of verifying that certified cost or pricing data submitted, in conjunction with the negotiation of this contract or any contract change or other modification involving an amount in excess of \$100,000, were accurate, complete, and current, the Contracting Officer, or his authorized representatives, shall—until the expiration of three years from the date of final payment under this contract—have the right to examine those books, records, documents, papers and other supporting data which involve transactions related to this contract or which will permit adequate evaluation of the cost or pricing data submitted, along with the computations and projections used therein.

"(b) The Contractor agrees to insert this clause including this paragraph (b) in all subcontracts hereunder which when entered into exceed \$100,000, unless the price is based on adequate price competition, established catalog or market prices of commercial items sold in substantial quantities to the general public, or prices set by law or regulation. When so inserted, changes shall be made to designate the higher-tier subcontractor at the level involved as the contracting and certifying party; * * *"

Similar clauses have been provided for price adjustment to formal advertised contracts, and negotiated contracts that are not firm fixed price.

Mr. STAATS. We believe that the revised regulations will accomplish by administrative action what would be required by enactment by the legislation. We recognize that regulations are more easily changed or rescinded than an act of Congress and are perhaps more susceptible to misinterpretation or oversight.

While we have no reason to anticipate, in this case, that the regulations will be either later rescinded or not followed, we would, of course, have no objection if the Congress should decide to enact this provision into law. We intend to observe closely the contracting agencies' practices with regard to the regulations.

HISTORY OF NEGOTIATED PROCUREMENT SINCE 1947

Chairman PROXMIRE. I would like to ask about that.

The Armed Services Procurement Act was passed in 1947?

Mr. STAATS. That is right.

Chairman PROXMIRE. And the Government could have made contract provisions consistent with the Truth in Negotiations Act, Public Law 87-653 and in the proposed amendment, any time in the last 20 years?

Mr. STAATS. They could have; yes.

Chairman PROXMIRE. But they didn't see the need until you made numerous reports to the Congress.

Mr. STAATS. I think that is correct. I believe this particular issue came more sharply into focus after the Truth in Negotiations Act of 1962 was enacted.

Chairman PROXMIRE. The GAO finally persuaded the Congress, in our judgment, to enact the Truth in Negotiations Act?

Mr. STAATS. It was a result of many reports by the GAO to the Congress.

Chairman PROXMIRE. Until that there was no requirement that the contractors provide, even though the overwhelming part of procurements were by negotiations and this is the only discipline by which you can keep the costs where they should be, there was no requirement in law on regulation that the contractor provide accurate, up-to-date and comprehensive records.

Mr. STAATS. I believe that is correct. It is a matter of law.

Chairman PROXMIRE. Did the Defense Department favor the enactment of that legislation?

Mr. STAATS. Mr. Welch or Mr. Bailey are better able to answer that.

Mr. WELCH. As I recall, Mr. Chairman, DOD initially took the position that this legislation was not necessary because similar requirements were already contained in the ASPR. Also, I would like to point out that the General Accounting Office has the right to examine contractors' books and records and subcontractors' books and records under negotiated contracts which stems back to the examination of records law that was passed in 1951. We are talking here about the agency's representatives' rights to examine subcontractors' records.

Chairman PROXMIRE. We say that was enacted in 1962, the Truth in Negotiations Act.

On the basis of your subsequent reports since 1962, it was clear that it was honored more in the breach than in the observance. It wasn't followed up at all on the basis of very, very comprehensive reports that you made to us, the real indictment, until very recently. As far as we know, it is still not being enforced.

Mr. STAATS. They, of course, as you know, disagree in some respects with the conclusions we reached in that report. But, nevertheless, as we testified here at our previous hearing, they have taken a series of actions which respond to the points we made in our report and which, if carried through, we feel—

Chairman PROXMIRE. But in the 5 years from 1962 to 1967, that law was not enforced vigorously and you have replete examples of how the contractors didn't provide the records. You showed, I thought, a devastating case in this respect.

Mr. STAATS. We do feel this is a very significant report. I believe some 2 years was required to develop a more comprehensive regulation. Our work was initiated in 1965 and involved contracts signed after the revised, more comprehensive regulation was issued.

POSITION OF DOD IN MAY 1967

Chairman PROXMIRE. Did they—the Department of Defense—favor the enforcement, more vigorous enforcement, in our hearings of May 1967?

Mr. WEITZEL. Mr. Chairman, if you will recall, the Defense Department testified in May 1967, that in its opinion it was enforcing the Truth in Negotiations Act. The differences in opinion related to the area of the identification of documentation or the requirement for written documentation in support of the cost or pricing information so that the contracting officers and the other Government representatives would be able to know what was relied upon by the Government in making the contract.

We stated in your hearings in May that there hadn't been full compliance with the Truth in Negotiations Act. The basic purpose of that law was to give the Government negotiators a better basis for pricing a contract.

Chairman PROXMIRE. Not only that, but you had examples where in 90 percent of the cases there hadn't been full compliance with the Truth in Negotiations Act.

Mr. WEITZEL. I think we need to clarify what is meant by the question of compliance with the act.

Chairman PROXMIRE. There wasn't full compliance in those cases.

Mr. WEITZEL. The act, itself, requires the furnishing of cost or pricing data, the submission of cost or pricing data. On this, the Defense Department testified that they were complying with the act.

The act also requires a certification by the contractor that the cost or pricing information that he has submitted is the most accurate, current and complete, available up to a certain date, which is supposed to be as close to the date of negotiation as possible.

The Defense Department testified that it was also requiring that certification.

The act, itself, does not say exactly how there shall be implementation of the act. In other words, what administrative details will be promulgated and followed in seeing that this information is furnished and is used in an effective form so that in the event it is found by the Government as a result of an audit that the contract has been overpriced to the Government because of a failure of the contractor to comply with these other two points—in other words, the submission of the proper information or the certification—the Government will know how much to charge back to him.

This was where we found that in our opinion there wasn't sufficient identification of what was furnished; there wasn't a sufficient audit trail. We felt that to the extent the data submitted either weren't complete, weren't accurate, or weren't current, or when it wasn't clear what data the certificate covered, there had not been full compliance with the intended purpose of the law.

The law, itself, requires implementation by regulation. We believe the Defense Department has done a reasonably good job in the regulation it has issued. As to be expected in the regulatory implementation of any new law, the experience developed weaknesses. We discovered evidences of weaknesses in our survey and recommended corrective changes.

DOD PROCUREMENT CIRCULAR NO. 57 COMPLIES IN GENERAL WITH
GAO RECOMMENDATIONS

The Defense Department has now agreed, in the issuance of Procurement Circular No. 57, with practically all of the changes that we recommended. The major thrust of this is to make it more clear that the requirement for submission of data is not satisfied simply by access to the data, that the data have to be submitted in writing or identified in writing to the contracting officer. Thus, it will be known what actually was submitted and there will be a record, as you said before, a standard against which later developments can be measured.

Chairman PROXMIRE. Let me read two short paragraphs from your testimony in May 1967, in which you said, speaking of the 242 cases which you had studied:

In 165 of these awards, we found that the agency officials and prime contractors had no records identifying the cost or pricing data submitted and certified by offerors in support of significant cost estimates. We also found that of the remaining 77 of the 242 procurements examined, agency and contract records of negotiations indicated that cost or pricing data were not obtained, apparently because the prices were based on adequate pricing competition or on an established catalogue of commercial items sold in commercial quantities to the general public. But there was not a record showing the basis for the contracting officer's determination.

So, really what you are saying is that in the 165 cases, only 20 were in full compliance with the law, and I concluded about 10-percent compliance, really.

Mr. STAATS. I think the essential point has to do with the phrase, that without adequate documentation and without an adequate record, neither the Defense Department, nor we, nor anyone else, can be certain that the information had been supplied.

To that extent, I believe we disagree with Defense in their statement that they could be sure that this information was actually supplied.

In a great many of these cases they had a statement from the auditor to the effect that he had seen this information, but there is no way to go behind that statement.

There is no itemization; there is no listing. There is nothing which refers it back into anybody's files.

Chairman PROXMIRE. We agree wholeheartedly on the necessity for this. There just isn't any question.

Once again, I want to say that I really meant it when I said that I had the greatest respect and admiration for Mr. Morris and his dedication, but, after all, Mr. Morris has a long record of opposition to the enactment of this law, enactment of the kind of thing we are suggesting as a matter of law.

What has Mr. Malloy's position been on it?

Mr. WEITZEL. I am not prepared to say that the Defense Department vigorously opposed the enactment of Public Law 87-653, the reason being the Defense Department staffs and GAO staffs cooperated in drafting the provisions of 87-653.

Mr. Bannerman was the main Defense Department representative, as I recall, and several of us worked on the GAO side. It was true that they had provisions in the regulation before requiring the certification. We felt the regulations were not being adequately followed and it was for this reason that we felt a law was necessary.

I would have to reexamine the situation way back in 1962 to confirm whether they opposed or didn't oppose.

Mr. STAATS. This would be a matter of record.

Chairman PROXMIRE. As far as the so-called Minshall-Proxmire proposal is concerned, the proposal that we want to put this into law for the audit and also for what we feel and you seem to feel is the proper procedure and not leave it to regulation—we have a change in the Defense Department coming up now, knowing Mr. McNamara is going to leave—under these circumstances, it seems to us it would be very wise for a procedure which all of us agree is proper, appropriate, necessary, and efficient, not just in terms of economy but in terms of a better military effort, that we should provide a solid legal basis for it.

You have no objection, but without some positive force behind it, it is pretty hard to get anything through the House and Senate.

Mr. WEITZEL. As to that provision, it is certainly true that the feeling in the Defense Department for a considerable period of time was that it would not be proper for the Defense contract auditors to have access to performance cost records under negotiated fixed-price contracts.

As to the other types of negotiated contracts, such as cost-reimbursement contracts, they already had access. But as to this particular type of contract, which is a major portion of their total contracting—

Chairman PROXMIRE. It certainly is. It is hard to see how the procurement officials can really understand what the fair price should be if they don't have access to the records, comprehensive access and full access right along.

Mr. WEITZEL. We had recommended to the Congress as early as 1966 that the Defense auditors should have access to the performance records. There was some legislative history on this.

Another committee had recommended that if Defense auditors were to be given access to this, it ought to be by legislation rather than by

administrative action, which we felt could have been done even in 1966.

There was that aspect and also the rather strong feeling in the Defense Department that to have performance costs audited under a fixed-price contract would be, in effect, invalidating the integrity of the contract. In other words, they were trying to get the contractors to assume more risks of performance and the top people in the Defense Department, whose influence had prevailed up until recently, felt that this effort would be affected by going into a contract after it was made and, in effect, second-guessing the contractor on his costs.

This wasn't our objective at all. Our reason for suggesting access by Defense auditors to performance records was so that it could be determined whether fair prices had been gotten by the Government in the negotiation of the contract, not to affect the contractor's profit if he was able to adopt more efficient procedures or if he was able to go out and get the material more cheaply than he had originally estimated.

This is the tack that has been adopted by the Deputy Secretary of Defense in the new directive, that the performance records will be opened to the DSA auditors for the purpose of comparing the prices that were actually paid with those that were offered to the Government at the time of negotiation, to see whether the contractor had information, such as a lower subbid, for example, that he should have disclosed to the Government but did not.

Mr. STAATS. There is no question in our mind, as Mr. Weitzel is saying, that better pricing information is essential to any negotiated contract situation.

Chairman PROXMIRE. How much money has been involved since 1947? Do you have any estimate of what the procurement has been? It is billions and billions and billions of dollars.

Mr. STAATS. It is in the hundreds of billions of dollars.

Chairman PROXMIRE. And without this kind of information there is no question that the Government, in my view, has lost billions of dollars. We have spent billions of dollars we shouldn't have spent. We wasted it. We will continue to waste it unless we have the assurance, it seems to me, by law, that this information is being provided to Defense procurement officials.

NEW REGULATIONS RESULT OF GAO AND COMMITTEE ACTION

Mr. STAATS. The Truth in Negotiations law, in our opinion, is very fundamental to the situation where we have so much of our procurement done through negotiated contracts. I think it is a sound law, and I think it is also a fair conclusion, Mr. Chairman, that without our report and without the attention this matter has had in this committee and in the Congress, that these new regulations probably would not have been issued.

I believe the Defense Department is now of the view that these further steps are required. I don't know of any basic quarrel in the industry, itself.

Chairman PROXMIRE. As an arm of Congress, I do hope you will reconsider what seems to me to be a much too mild no "objection" position here. I think we have the same objective. We know this is certainly in the interest of the taxpayer.

TEST OF ENFORCEMENT OF NEW REGULATION

Let me ask you: How shall we test the enforcement of this regulation?

Mr. STAATS. We will do it by the same processes we went through in developing our initial report; namely, of making audits of individual contract situations.

Chairman PROXMIRE. And when shall we review the situation?

Mr. STAATS. We have it in our program to do this periodically—not periodically, but, rather, as a part of a regular audit program of Defense contracts.

Chairman PROXMIRE. What does that mean in terms of the next time we will have a review?

Mr. STAATS. It is a question, really, of what would be a reasonable period of time to give the regulations a chance to change the situation.

Chairman PROXMIRE. Six months?

Mr. STAATS. I would say more nearly a year, probably.

REVIEW IN FALL OF 1968

Chairman PROXMIRE. As late as next fall, then, I think we ought to have a comprehensive review. Meanwhile, I hope we can get this enacted into law.

Go right ahead.

Mr. WEITZEL. Our situation, Mr. Chairman, is that we are simply very happy that they have adopted this suggestion.

Chairman PROXMIRE. They have adopted suggestions so often in the past and as long as they are under regulation not a matter of law I just have a feeling that we are not going to get results. After all, so very much is at stake here, billions of dollars, and the contractors who are all fine, honest men, nevertheless have their own special interests and their own desires, understandable desires, in the drive for profits. They aren't going to volunteer information which is going to sharply reduce those profits unless the law makes it explicit and emphatic that they have to do so.

Go right ahead.

RECOVERY FROM SUBCONTRACTORS

Mr. STAATS. The next point has to do with recovery from subcontractors, closely related to the point we have been discussing.

Under the existing provisions of the ASPR, the Government's right to reduce the contract price extends to cases where the prime contract price was increased because a subcontractor furnished defective cost of pricing data. Problems have arisen with respect to the Government's right to a price adjustment where the subcontractor has submitted defective data after the prime contract price has been established. These problems are being studied by the Department of Defense and by our office.

Again, we attach pertinent excerpts from the regulation to our statement.

(The information follows:)

ATTACHMENT B

EXCERPTS FROM DEFENSE PROCUREMENT CIRCULAR NO. 57, NOVEMBER 30, 1967

*Recovery from Subcontractors**"3-807.5 Defective Cost or Pricing Data*

"(d) Under 10 U.S.C. 2306(f) and the 'Price Reduction for Defense Cost or Pricing Data' clauses set forth in 7-104.29, the Government's right to reduce the prime contract price extends to cases where the prime contract price was increased by any significant sums because a subcontractor furnished defective cost or pricing data in connection with a subcontract where a certificate of cost or pricing data was or should have been furnished. * * *"

"Paragraphs 3-807.5(d) and (e), which are concerned with the area of subcontractor coverage, are still under study and may be revised in the near future. In event of revision, the clause in 7-104.29 will likewise be revised."

GOVERNMENT PROPERTY IN THE POSSESSION OF DEFENSE CONTRACTORS

Mr. STAATS. The third and final subject which we are covering in our statement today has to do with Government property in the possession of Defense contractors.

It is the policy of the Department of Defense that contractors will furnish all facilities required for the performance of Government contracts, except that facilities may be provided by the Government when (1) contractors are either unwilling or unable to do so and no alternate means of obtaining contract performance is practical; or (2) furnishing existing Government-owned facilities is likely to result in substantially lower cost to the Government of the items produced, when all costs involved—such as costs of transporting, installing, maintaining, and reactivating such facilities—are compared with the cost to the Government of the contractor's use of privately owned facilities.

Also, it is the policy of the Department of Defense to have its contractors maintain the official records of Government-owned property in their possession.

The Government's inventory of property in the hands of contractors consists of property which the Government has furnished and property procured or otherwise provided by contractors for the account of the Government. Basic policies governing the control of this property are set forth in the Armed Services Procurement Regulation.

At your subcommittee hearings on November 28, 1967, representatives of the Department of Defense indicated that the total value of Government-owned property in the possession of contractors amounted to about \$14.9 billion. This figure includes an estimate of \$3 billion, representing the value of special tooling and special test equipment held by contractors.

Chairman PROXMIRE. Do you have a breakdown of what the rest is? Is any real property included?

Mr. STAATS. We have a breakdown of it. Mr. Bailey has it here. He can read the highlights of it. We have a detailed statement to insert into the record.

Mr. BAILEY. Government material, in other words, the raw materials, used by contractors, such as cloth, duck to make tents, maybe electronic gear, this type of thing that goes into the production of an end item—material in the hands of contractors—

Chairman PROXMIRE. Electronic gear?

Mr. BAILEY. Black boxes or subassemblies, something of this kind that they have purchased and acquired for production of an end item or which may have been furnished by the Government out of its procurement. This material amounts to about \$4.7 billion. Active real property, industrial property in the hands of contractors—

Chairman PROXMIRE. This is land?

Mr. STAATS. Land and buildings.

INCREASE IN CONTRACTOR-HELD INVENTORY FROM 1965 TO 1966

Mr. BAILEY (continuing). \$2.1 billion. Plant equipment—these are machines, metal working machines, lathes, milling machines—this type of thing, \$4.1 billion. This totals \$10.9 billion, or \$11 billion, roughly, which, plus the \$3 billion that they estimated for special tooling and special test equipment, makes up the total included in Mr. Staats' statement.

Mr. STAATS. I think the comparable figure to the \$11 billion for fiscal year 1965 was \$7.2 billion. So there has been a substantial increase from 1965 to 1966.

FINANCIAL ACCOUNTING ON SPECIAL ITEMS, ET CETERA

The Department of Defense does not collect financial data regarding the value of special tooling, special test equipment, and military property held by contractors.

Chairman PROXMIRE. Don't you think they should? This is Government-owned equipment. Shouldn't they have concise, full, and complete data of what the taxpayers own that private individuals are using?

Mr. BAILEY. Yes, sir. In our report, which we made this month, on Government property in the hands of contractors, we recommend that such an inventory be kept.

Mr. STAATS. I believe there is definitional problem of what you would include. I believe that has been the main consideration here, if I understood correctly. But we have recommended that it be done.

Department of Defense records show that as of June 30, 1966, the cost of facilities in the hands of contractors amounted to \$6.2 billion. This amounted to an increase of \$700 million over that reported at June 30, 1965. About \$300 million of this increase is attributed to the inclusion in inventory records of several Government-owned plants that had been inactive. The remainder is primarily applicable to increases in the amount of industrial plant equipment provided to Army and Air Force contractors. Comparable data for the period ended June 30, 1967, is not yet available.

Chairman PROXMIRE. On the basis of any period for which you have data for comparison, this has been an increasing problem or at least an increasing policy of buying equipment for private contractors to use. It is not decreasing and is not stable. It is going up.

Mr. BAILEY. I think there is another factor that we have to consider here, too, Mr. Chairman. That is the point that Government procurement has been increasing because of the effort in Southeast Asia.

Chairman PROXMIRE. Except the records we have seen, the Defense indicators—perhaps during this period it is increasing—from about the middle of 1966 to date it has been stable.

Mr. STAATS. 1965-66 was the big buildup.

Chairman PROXMIRE. There was increasing procurement in that time.

Did you say another element of this has also been increasing, just before you started to read this paragraph?

Mr. STAATS. I don't think so.

Chairman PROXMIRE. At any rate, the only time comparison you have is 1965-66, when there was a substantial increase.

Mr. STAATS. Yes.

Chairman PROXMIRE. Will you be able to get us more detailed data on this? This is something that the Congress ought to be able to get immediately from the Defense Department. They ought to know how much they own. At least, they ought to have figures on how much they have, that the contractors have, and they ought to be able to tell us each year.

Mr. STAATS. For these two categories of material and real property, I understand the records are available for prior years. We could very readily supply that.

(The material follows:)

SUMMARY OF MATERIAL, ACTIVE REAL PROPERTY, AND PLANT EQUIPMENT IN HANDS OF CONTRACTORS
[In thousands of dollars]

	Fiscal year 1962	Fiscal year 1963	Fiscal year 1964	Fiscal year 1965	Fiscal year 1966
Material (procurement, source, GPM, in custody of contractor):					
Department of the Army.....	(1)	(1)	485,000	252,000	616,000
Department of the Navy.....	(1)	(1)	119,000	105,000	1,633,000
Department of the Air Force.....	2,461,000	2,729,000	1,114,000	1,276,000	1,422,000
Other.....	12,000	11,000	17,000	18,000	24,000
Total.....	2,473,000	2,740,000	1,735,000	1,651,000	4,695,000
Active real property (industrial), contractor operated:					
Department of the Army.....	685,768	662,704	631,712	660,931	1,061,080
Department of the Navy.....	489,615	425,869	396,502	399,154	378,994
Department of the Air Force.....	745,012	784,126	724,286	736,214	688,423
Total.....	1,920,395	1,872,699	1,752,500	1,796,299	2,128,497
Plant equipment (in custody of contractors) ²:					
Department of the Army.....	966,461	859,980	838,339	894,996	1,042,851
Department of the Navy.....	835,077	513,692	765,130	678,995	680,791
Department of the Air Force.....	1,604,928	1,622,403	2,112,693	1,953,758	2,343,039
DSA.....	(1)	(1)	(1)	210,624	52,432
Total.....	3,406,466	2,996,075	3,716,162	3,738,373	4,119,113
Grand total.....	7,799,861	7,608,774	7,203,662	7,185,672	10,942,610

¹ Information not available.

² Plant equipment is personal property of a capital nature, including machinery, equipment, furniture, vehicles, machinery, tools, and accessory and auxiliary items for manufacturing or administrative use. Information obtained from Mr. Francis Jameson (OSD Comptroller), Directorate for Statistical Services.

Source: All data, except noted, obtained from report on real and personal property of the DOD for the fiscal years shown.

Chairman PROXMIRE. We would like to know whether this has been increasing or not, and the reasons for it. You give one reason, which is legitimate. But we want to know what other reasons there are.

Mr. BAILEY. One example would be the inventory in 1966 of inactive real property which went down \$300 million. The active real property in the hands of contractors went up \$300 million, but the inactive real property went down \$300 million, roughly.

Chairman PROXMIRE. In 1965-66, the inactive property was down? Mr. BAILEY. The inactive real property; yes, sir.

RISE IN VALUE DUE IN PART TO MODERNIZATION AND REPLACEMENT PROGRAM

Mr. STAATS. It is shifting between the active and the inactive status.

One of the factors contributing to the rise in the value of Government-owned property held by contractors is the Department's program for modernization and replacement of Government-owned machine tools. Annual expenditures for this program averaged about \$27.4 million during the period 1958 through 1963. Fiscal year 1966 expenditures amounted to \$51.5 million and expenditures of \$65.8 million were forecast for the fiscal year 1967.

Chairman PROXMIRE. Once again we have a situation in which the Federal Government has purchased equipment for contractors and it is following a policy, apparently, and the tenor of your remarks suggests that maybe there is approval and maybe not, maybe I misconstrue it, of providing better equipment, more modern equipment for the contractors.

It would seem to me that every one of these purchases should be made with the greatest reluctance and only on a showing that it is absolutely necessary. When you have to buy more modern equipment, there should be a real effort to get the contractor to buy it himself.

ADHERENCE TO POLICY INVOLVED

Mr. STAATS. That would be a correct reading of the statement of policy on the part of the Department of Defense. What is suggested here at least is a question, and maybe it can only be a question absent more specific information on individual cases: Whether or not they have vigorously applied the policy which the Defense Department, itself, has enunciated in modernizing equipment at Government expense.

Chairman PROXMIRE. Do you have anything in greater detail as to what kind of justification they require to enable the Defense Department to go ahead and make purchases for a private contractor?

Mr. STAATS. We do not have it here today, I understand, but we will be glad to see if there is anything we can obtain for the record.

Chairman PROXMIRE. We would like to know the justification, what they go through, what the criteria are.

(The justification follows:)

NATURE OF JUSTIFICATION REQUIRED AND THE CRITERIA USED BY THE DEPARTMENT OF DEFENSE FOR REPLACING GOVERNMENT-OWNED INDUSTRIAL EQUIPMENT IN THE POSSESSION OF PRIVATE CONTRACTORS

The Department of Defense's general policy on replacement of industrial equipment as stated in DOD Directive 4275.5 is that basically, the contractor will be encouraged to replace old, inefficient Government-owned equipment or manufacturing processes with modern, more efficient, privately owned equipment. The weighted guidelines for negotiation of profit or fee is cited as encouraging the contractor to provide equipment required on DOD contracts.

When the contractor cannot be persuaded to replace Government-owned equipment or improve manufacturing processes, the replacement may be effected if

such action is in the interest of the Government and can be justified on economic grounds.

The analysis required to justify the replacement of Government-owned equipment on economic grounds is prescribed in DOD Directive 4215.14. This involves a comparison of projected operating costs to be incurred on Government orders during the next immediate 12-month period using the present equipment with projected operating costs using the proposed replacement equipment. The operating costs considered, include such factors as direct labor, indirect labor, maintenance, power, scrap/rework, tooling, etc. The cost projections are based primarily on the projected machine load for the 12-month period. The projected machine load for the proposed replacement equipment reflects a productivity increase ratio for the new equipment as developed through engineering studies and estimated production potential from machine tool builders.

The annual operating costs savings, if any, resulting from the proposed equipment is then compared to the annual amortization costs of the equipment. DOD Directive 4275.5 states that replacement costs for equipment to be used by the aerospace industry will normally be amortized within 3½ years; in other industries new equipment should normally be amortized within 5 years. If the annual operating costs savings exceeds the annual amortization costs of the new equipment the analysis is considered as favoring replacement.

The economic justification is usually prepared by the Government contractor and is subject to review and approval at various management levels depending on the cost of the replacement equipment. For example, in the Air Force the Systems Command may approve projects up to \$500,000. Projects costing more than \$500,000 must be reviewed and approved by Headquarters USAF. All projects costing more than \$1 million must be approved by the Office of the Assistant Secretary of Defense (Installations and Logistics).

As a result of our report to the Congress on the need for improvements in controls over Government-owned property in contractors plants (B-140389) issued November 24, 1967, the Deputy Assistant Secretary of Defense (Procurement) has indicated that current procedures would be modified to require the specific consideration of and a statement as to the contractor's inability or unwillingness to finance equipment modernization.

CONTRACTORS NOT ASKED TO INVEST IN MODERN TOOLING

Mr. HAMMOND. We found in some cases in review of the tooling modernization program that contractors were not asked to invest in the modern tooling. The Government furnished it without requesting a contractor to make their own investment and in some cases did not find out whether or not he was in a position to do it. Information on this is included in our report. (See app. 4(a), p. 411.)

Chairman PROXMIRE. You say in your report you show that in the past there has not been a policy of requiring or asking the contractor to buy the equipment?

Mr. HAMMOND. There is a policy that they will be required to furnish equipment, but in actual practice they did not, in many cases, ask contractors to furnish it.

Chairman PROXMIRE. Are you reassured that at the present time they do in all cases do everything they can to request the contractor to buy his own equipment?

Mr. HAMMOND. We have recommended that the Department of Defense do that. We do not have the final action that they have taken on it.

Chairman PROXMIRE. You do not have it? You don't know?

Mr. HAMMOND. That is right.

Mr. WEITZEL. Mr. Chairman, the Defense Department policy requires the contractors to submit justifications on the purchase of new equipment. They have a directive which is set out on page 39 of our

report on the "Need for Improvements in the Controls Over Government-Owned Property in the Contractor's Plants" that says basically the contractor will be encouraged to replace old, inefficient Government-owned equipment or manufacturing processes with modern, more efficient, privately-owned equipment. (See p. 433.)

We found, though, that in submitting justifications contractors generally weren't required to include statements as to their ability or willingness to finance the equipment. Most locations where we inquired into this we found that either the contractors had not been requested to acquire privately owned equipment or the files gave no indication that use of private funds had been considered in evaluating the proposals that we examined.

As to some of these cases, Government officials told us that contractors had been encouraged to use private capital. However, we did not find records of that. At two locations, we did find evidence that the possibility of contractor financing had been questioned in connection with certain submissions, in which cases Government financing was justified because of contractor investment in other equipment or facilities.

It appeared to us, and we so reported, that the Government's investment in this program is sufficiently great that the question of contractor financing should receive positive attention in all cases.

FAILURE TO COMPLY WITH POLICY

Chairman PROXMIRE. The policy apparently on the part of the Department has been that the Government would only procure this equipment for contractors under certain exceptional circumstances. This has been the policy. But the practice has been that they have in many cases, and you don't say how many, you don't say what the proportion is, but in many cases, the Government has not applied this policy, that the Government has gone ahead and purchased this equipment for the contractor.

Mr. WEITZEL. We feel that there should be stronger application of the policy and also of that other part of the policy which directs that replacement of machine tools be justified on economic grounds.

Chairman PROXMIRE. And you have no knowledge that the Defense Department is now pursuing a different policy?

Mr. STAATS. We do not.

Chairman PROXMIRE. Under these circumstances, if the Congress should decide that this is a policy that should be provided in law, a requirement in law, why wouldn't that be desirable and necessary?

Mr. WEITZEL. All we can say at this point is that the Deputy Assistant Secretary of Defense agreed with our proposals in this area, that he said that it was DOD's policy that the contractor be encouraged to replace these old, inefficient Government tools with privately owned ones. He said that current procedures would be modified to require the specific consideration of and a statement as to the contractor's inability or unwillingness to finance equipment modernization.

Also, he said that they would review the need to revise their guidelines as they apply to both new and existing major defense programs.

That is the latest we have.

COST STUDIES ON ADVANTAGE IN GOVERNMENT PROVIDING EQUIPMENT

Chairman PROXMIRE. Perhaps I should wait until you complete this statement because as far as I know you are going to recommend, I hope, that we enact a law on this. But let me ask on the part you have completed, your second exception is that these facilities can be purchased by the Government and should be when it is likely to result in substantially lower cost to the Government of the items produced.

Have you seen any cost studies to prove that there are any examples of this?

Mr. STAATS. I have not.

Chairman PROXMIRE. Wouldn't this be helpful? Wouldn't this be a good way to follow up to determine whether this exception is meaningful?

It is hard for me to, offhand, imagine that this would be very common. I can't conceive of a situation in which this would be likely to occur, given an accurate and proper cost accounting system.

Why would it be cheaper for the Government to own equipment? Certainly, all motivation is for an entrepreneur who buys his equipment to buy it more carefully, to maintain it more rigorously and to make sure that it is the equipment that can do the job in the most efficient way. If the Government buys it, there is far less incentive for him to exercise this kind of diligence.

REDUCED COSTS FOR GOVERNMENT-OWNED EQUIPMENT

Mr. BAILEY. Mr. Chairman, in our report which we referred to before, we do point out that in some cases where reduction in cost of production was one of the reasons for acquiring Government machinery, adjustments were not made in contract prices to reduce or reflect these revised production costs. That is, for existing contracts in the plant. Whether these reductions in cost would be reflected in new contracts would be a matter of negotiation of new contract prices.

Chairman PROXMIRE. What you are saying is that even though the Government owned the equipment and, therefore, the price of the product produced should be less inasmuch as the contractor did not have to amortize—

Mr. BAILEY. Where the equipment being used to produce Government property was modernized on the basis that it would cost less to produce the Government material.

Mr. STAATS. There was no flow through on the saving.

Mr. BAILEY. The contract price of the material was not reduced.

Chairman PROXMIRE. This is the point which has evaded me. I think it is a good point.

If you are going to modernize the equipment, you certainly ought to do it on the basis of renegotiating the price of the item being produced.

You say the record shows there has not been such a reflection?

Mr. BAILEY. In some of the instances.

Chairman PROXMIRE. You are helping the contractor to make a bigger profit, at the same price, with more efficient equipment, the efficiency provided by the Government, by the taxpayer. So he has a lower cost and his profits are bigger. That is the ultimate result.

Mr. BAILEY. Of course, in our report we recommended that we get these profits in the future, or this reduction in price.

Chairman PROXMIRE. Of course, if you don't enforce the Truth in Negotiations Act, and don't have accurate cost records, it is hard to know whether or not the price should be reduced on the basis of the actual cost, either.

Mr. STAATS. On the relative cost price you referred to, we will be glad to examine that.

But the general points that I think we have to keep in mind would be that a great deal would depend on whether it is general purpose equipment or specialized equipment.

I think you would find a great variance as to what your tradeoffs would be in terms of cost of providing it by the Government or by the contractor. We will be glad to look into it.

Chairman PROXMIRE. Fine.

OEP APPROVAL FOR COMMERCIAL USE

Mr. STAATS. The Department of Defense allows rent-free use of its facilities for military orders.

In June 1957, the Office of Emergency Planning established a requirement for contractors to obtain advance approval to use Government-owned machine tools on commercial work exceeding 25 percent of the total usage. The procedure for prior approval was established primarily to preclude contractors from obtaining a favored competitive position through rent-free use of Government-owned production equipment on commercial work. (See p. 213.)

OEP APPROVALS NOT OBTAINED

Generally, we found from our review of the records covering the years 1965 and 1966 that contracting officers were not requiring contractors to request and contractors were not requesting approval to use Government-owned industrial plant equipment for commercial work in excess of the 25-percent criteria.

Chairman PROXMIRE. That 25-percent criteria leaves a lot of leeway, it seems to me, for extracurricular use on Government-owned equipment that is unfair competition and also exploiting the taxpayer.

If you have a million dollars worth of equipment and you can use that equipment up to 25 percent of the time for your own private use, this is a big advantage. Of course, you could have tens of millions of dollars of equipment.

Mr. STAATS. We were not questioning this point so much in our report as we were the fact when it exceeded 25 percent it still wasn't getting approval. That was the point we were referring to the other day.

Chairman PROXMIRE. So it could be 50 and 60 percent and so on. The examples that you gave in your report were 57 percent and another was greater than that.

Mr. STAATS. That is correct. There were a number in excess of the 25-percent rule.

Chairman PROXMIRE. But the 25-percent rule doesn't satisfy you, does it?

Mr. STAATS. I don't really know what consideration went into the establishment of the 25-percent rule.

Chairman PROXMIRE. They don't even have to request approval to use Government-owned industrial plant equipment as long as they use it less than 25 percent of the time? Why shouldn't they be required to have some kind of approval? It can be routine, but there should be some kind of approval.

Mr. STAATS. It is a question of local approval versus approval by the Office of Emergency Planning. There is a procedure requiring local approval even in cases under 25 percent.

Mr. HAMMOND. Even under 25 percent they get the local approval and are required to pay rent for the commercial use.

Chairman PROXMIRE. Wasn't your conclusion that in some cases even with more than 25-percent use they may not have been required to pay rent?

Mr. STAATS. No; it was to get approval.

Chairman PROXMIRE. Wait a minute. How about on the rent part.

Mr. BAILEY. In some cases there was some rent, yes.

Mr. WEITZEL. Later in the statement we point out that the rent is inconsistent and in some cases inequitable.

Chairman PROXMIRE. In some cases nonexistent?

Mr. WEITZEL. The rent is not paid on a machine-by-machine basis. It is not computed that way now. We have some recommendations to that effect.

Mr. Hammond, would you care to comment?

Chairman PROXMIRE. The contractor keeps the records, too.

Mr. HAMMOND. In some cases the contractors did use the equipment without getting the approval and paying the rent. We have recommended a machine-by-machine utilization record so that the Government will know when the equipment is used and will collect the necessary rent.

ASPR NOT PRECISE AS TO "25 PERCENT USE"

Mr. STAATS. The further point we are making is that the armed services procurement regulation does not precisely define what constitutes "25-percent, non-Government use." It is not clear whether the criteria refers to total planned use or a portion of manufacturing hours available under one or more work shifts, or if it is to be administered on a total plant or an item-by-item basis. That is the point which has just been made.

Insofar as we can determine, the approval obtained from the Office of Emergency Planning places no restriction on the extent to which a contractor may use the facilities on commercial work provided rental payments are made.

LACK OF UNIFORMITY IN RENTAL RATES

Although uniform rates for the rental of Government-owned machines to contractors have been prescribed, as currently stated in Defense Mobilization Order 8555.1 of the Office of Emergency Planning and section 7-702.12 of the Armed Services Procurement Regulation, we found that the various bases upon which the rent payments were negotiated resulted in a lack of uniformity in the rates actually