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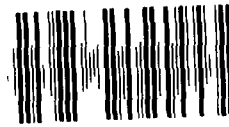
United States General Accounting Office 130258

Briefing Report to the Vice Chairman,  
Subcommittee on Economic Resources,  
Competitiveness, and Security Economics  
Joint Economic Committee  
Congress of the United States

June 1986

# NAVY CONTRACTING

## Allegations About Trident Submarine Program Matters



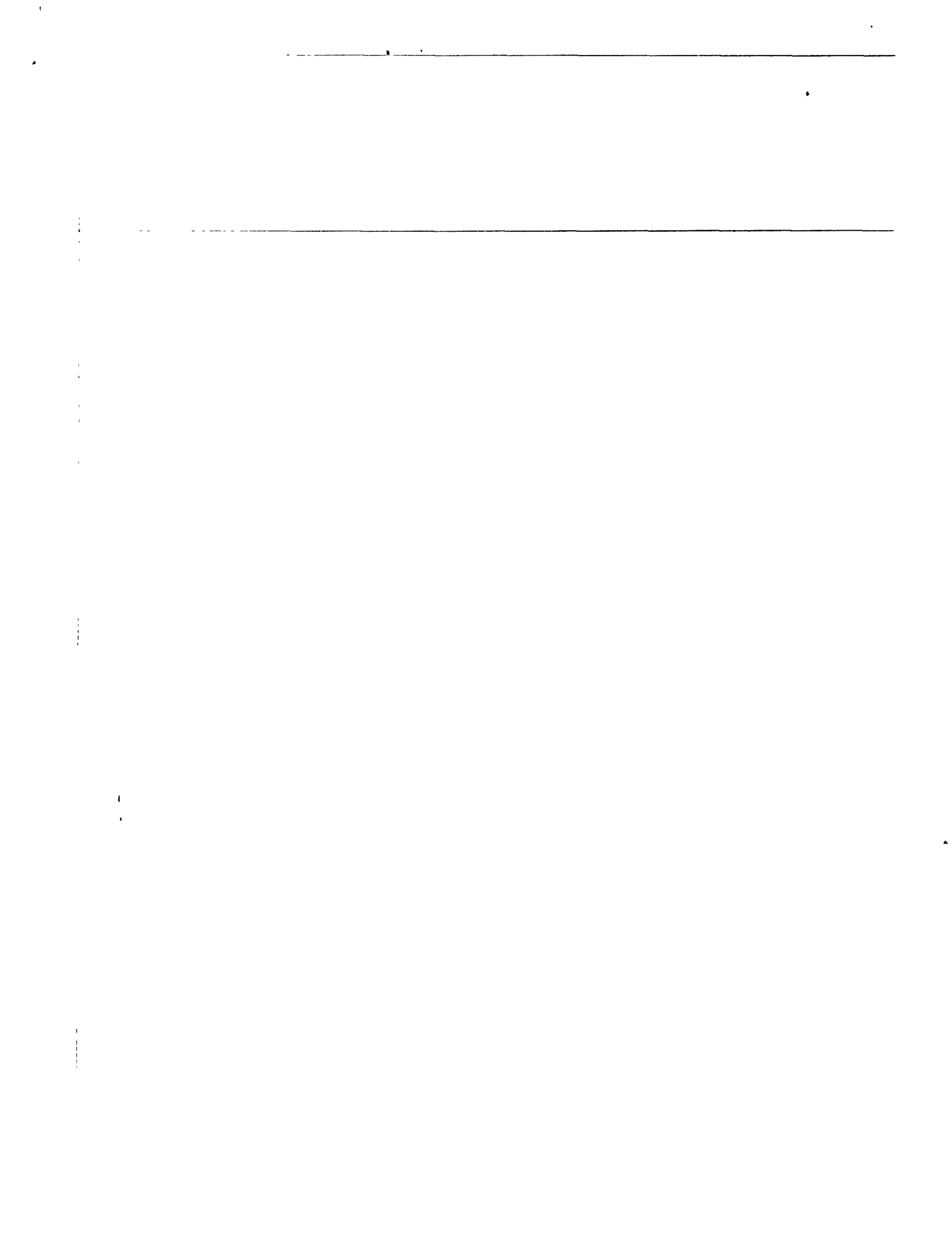
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UNITED STATES GENERAL ACCOUNTING OFFICE  
WASHINGTON, D.C. 20548

NATIONAL SECURITY AND  
INTERNATIONAL AFFAIRS DIVISION

June 13, 1986

B-222051

The Honorable William Proxmire  
Vice Chairman  
Subcommittee on Economic Resources,  
Competitiveness, and Security Economics  
Joint Economic Committee  
Congress of the United States

Dear Mr. Vice Chairman:

In response to your request and subsequent discussions with the Subcommittee, we have reviewed certain allegations made by Mr. Robert Kalmin concerning mismanagement and questionable practices in the Trident submarine construction program. These allegations covered excessive progress payments in submarine construction, advance procurement of long lead time material, unwarranted escalation on the lead Trident, destruction of Navy records, inappropriate task authorization and funding on engineering services contracts, elimination of a financial monitoring procedure, and violations of standards of conduct.

Our review disclosed that overprogressing of submarine construction occurred during the early 1980s at Electric Boat and, according to the Navy, produced progress payments earlier than warranted to that contractor. In addition, our work on the overprogressing allegation led us to other contract payment and related management control issues at Electric Boat. In this regard, we found that (1) contractor budgeting practices raised questions about the accuracy of data and reports submitted to the Navy and (2) a Navy contracting practice provided, and is still providing, through special clauses in some submarine contracts, additional progress payment amounts over that which are normally paid under standard payment clauses.

Secondly, we found that there were increases in funding for advance procurement for long lead time material for Trident submarines. Certain purchases under advance procurement contracts were made for equipment that did not qualify as long lead time material and contributed to this growth.

Concerning the allegation on destruction of Navy records, we found that a general records disposal effort took place in a division (PMS 396P) of the Trident project office at the time that investigations of Trident program matters were ongoing. However, we found no evidence that this effort was done to eliminate specified documentation, nor was there any indication that officials involved in the records disposal effort were contacted by investigative agencies at that time. We were unable to independently determine whether retention standards were followed on the records destroyed because of the absence of subject identification codes on the inventory listing of those documents. Such coding would have facilitated this determination but was not required under Navy policy.

Of the remaining allegations reviewed, we found that:

- An increase in escalation authorization in October 1981 for the lead Trident submarine did not result in any additional payment to Electric Boat.
- The cited task transaction on an engineering services contract that occurred on January 3, 1984, was issued within the contract work scope and appropriate funding was available for this type of work. The official who issued the transaction had the authority to approve and issue task assignments.
- Despite the elimination of the Enclosure 3 form (Reconciliation of Funding Sources) from the Task Assignment Letter, the PMS 396P office utilizes a contract-required cost report to enable it to financially monitor contract tasking.
- When the Director, PMS 396P, purchased a used boat at fair market value from a representative of Electric Boat, he did not appear to have violated the federal antibribery statute (18 U.S.C 201) or any of the policies contained in the Navy's Standards of Conduct.

At the request of the Subcommittee, we did not obtain formal agency or contractor comments on the matters in this report. However, these matters were discussed with Department of the Navy and Electric Boat officials. Their views were considered and incorporated where appropriate in our report.

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this briefing report until 30 days from its issue date. At that time, we will send copies to interested parties and make copies available to others upon request.

B-222051

Should you need additional information on the contents of this document, please call John D'Esopo on 275-4361, or John Potochney on 275-8084.

Sincerely yours,

A handwritten signature in cursive script that reads "Frank C. Conahan".

Frank C. Conahan  
Director

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## ABBREVIATIONS

DOD	Department of Defense
FBI	Federal Bureau of Investigation
LLTM	long lead time material
PMS 396P	Plans, Programs and Financial Management Division
SOP	Standard Operating Procedure
SSIC	standard subject identification code
SUBCOM	Submarine Computer Oriented Management
TAL	Task Assignment Letter

## ALLEGATIONS ABOUT

### TRIDENT SUBMARINE PROGRAM MATTERS

The Trident Submarine Ship Acquisition Program Office (PMS 396) of the Naval Sea Systems Command manages the design and construction of the Trident submarine. The Program Manager exercises broad authority within the scope of the program over planning, direction, control, and utilization of resources. The Director, Plans, Programs and Financial Management Division (PMS 396P), an office within the organizational structure of the acquisition program office, is the principle advisor to the Program Manager and the Deputy Manager on business and financial management matters. In essence, PMS 396P provides control and direction of all areas of program and budget planning, business management, budget execution, and program coordination for all programs assigned to the PMS 396 organization.

Trident submarine design and construction is performed under Navy contracts by the Electric Boat Division of the General Dynamics Corporation, located at Groton, Connecticut. The Supervisor of Shipbuilding, Conversion and Repair (Supship), Groton is responsible for contract administration functions on these contracts.

Our review was conducted at the request of Senator William Proxmire, Vice Chairman of the Subcommittee on Economic Resources, Competitiveness, and Security Economics, Joint Economic Committee. The Vice Chairman requested that we examine certain allegations made by Mr. Robert Kalmin, a civilian employee of the Naval Sea Systems Command, concerning mismanagement and questionable practices in the Trident submarine construction program.

We met with Mr. Kalmin and his attorney to initially discuss and obtain specific information on the allegations presented to the Subcommittee. Subsequent correspondence from Mr. Kalmin's attorney to us clarified and expanded on the allegations.

After an initial analysis of the information provided and meetings with the Subcommittee, we agreed to focus on the following allegations: (1) overprogressing of submarine construction, (2) advance procurement of long lead time material (LLTM), (3) unwarranted escalation on the lead Trident, (4) destruction of Navy records, (5) inappropriate task authorization and funding on engineering services contracts, (6) elimination of a financial monitoring procedure, and (7) violations of standards of conduct.

Although the allegations concerned the Trident program, during the course of our work on overprogressing, we found that the finding also applied to the SSN 688 program. The effect on this program is also included in this report.

Our review was conducted from July 1985 to January 1986, primarily at the Plans, Programs and Financial Management Division (PMS 396P) of the Trident Submarine Ship Acquisition Program; Supervisor of Shipbuilding, Conversion and Repair, Groton, Connecticut; and the Electric Boat Division of General Dynamics Corporation, Groton, Connecticut. Audit work was also conducted at the Comptroller Directorate of the Naval Sea Systems Command, the Naval Data Automation Command, and the Office of the Comptroller of the Navy.

At the Navy offices in the Washington area, we obtained, discussed, and reviewed Secretary of the Navy instructions, policy directives, standard operating procedures, Task Assignment Letters, task statements, internal memoranda, contract data, and cost reports. In addition, we interviewed key Navy officials associated with matters concerning the allegations. We also obtained information from various investigative activities, including the Federal Bureau of Investigation (FBI); Office of Special Counsel, U.S. Merit System Protection Board; Department of Defense Inspector General; Navy Inspector General; Naval Sea Systems Command Inspector General; Naval Investigative Service; and the Naval Audit Service.

At the Supervisor of Shipbuilding, Conversion, and Repair, officials were interviewed and contract, payment, and correspondence files were reviewed in the Contracts, and the Business and Production Review Departments.

At Electric Boat, we discussed and reviewed the allegation on advance procurement funding for LLTM with Trident Program Control officials. We also reviewed cost reports, LLTM listings, and other documentation submitted by the Procurement Office. We asked Electric Boat to respond to our observations on progress payments, and discussed the special provisions on contract retentions with the contractor.

At the request of the Subcommittee, we did not obtain formal agency or contractor comments on the matters in this report. However, these matters were discussed with Department of the Navy and Electric Boat officials and their views on our findings were included in the report where appropriate.

Hearings were held by the Subcommittee on January 14, 1986, during which we presented testimony on the preliminary results of our review.

The specific allegations and our findings are presented in the following sections.



## OVERPROGRESSING OF SUBMARINE CONSTRUCTION

### Allegation

Until at least March 1982, Trident submarines were overprogressed during construction; i.e., the actual percentage of completion was less than the percentage claimed for progress payments, thus allowing Electric Boat to receive early progress payments. An adjustment made by the Navy to the progressing system in March 1982 constitutes proof that the early payments were occurring.

### GAO findings

Navy documents show that Trident and SSN 688 submarine construction contracts at Electric Boat were overprogressed in the early 1980s. According to these documents, certain budgeting practices followed by the contractor--that were contrary to those approved by the Navy for use on these contracts--had the effect of inflating the reported percentage of ship construction completed and thus produced early payment for work progress.

In March 1982, the Navy took action to disapprove Electric Boat's progress payment computation, which was based on the unacceptable practices, when it became clear that the contractor's budget allocation at that time would have resulted in a significantly inflated progress payment.

### Computation of progress

Progress achieved in constructing a submarine is determined by computing separate percentages of completion for labor and for material, and then combining them to compute an overall weighted percentage of completion. Material progress is measured basically by dividing the cost incurred to date for material by the estimated total cost for material. Labor progress is measured by the number of budgeted hours earned (see next page) to date compared to the total number of hours budgeted. The number of hours actually worked to date does not enter directly into the computation of progress. However, there should normally be a close relationship between actual hours worked and budgeted hours earned. If the budgets are accurate, the number of hours actually expended to complete any given task will closely approximate the hours budgeted for that task.

The basic units of measurement for labor progress are the individual tasks, or work authorizations, involved in constructing a submarine. Each submarine has several thousand work authorizations, about one-third of which would be open, or in process, at any given time. Each work authorization has a budgeted number of labor hours to complete the work.

On a biweekly basis, foremen estimate the percentage of each task which has been completed. The larger tasks (i.e., those which budgets of more than 1,000 labor hours) have pre-established milestones or standards which must be achieved in order to earn progress on the task. The hours budgeted for a task are multiplied by the percentage of completion claimed by the foremen to compute the number of budgeted hours which have been earned. The earned budgeted hours for all tasks are added together to determine the total hours earned to date in constructing the submarine. This result is divided by the total hours budgeted for construction in order to compute the percentage of labor progress on the submarine.

#### Practices that cause overprogressing

In March 1980, the Navy validated Electric Boat's Submarine Computer Oriented Management (SUBCOM) system as complying with Department of Defense (DOD) Instruction 7000.2, which establishes criteria for cost and schedule control systems on selected DOD contracts. The criteria serve as standards for measuring the reliability of a contractor's management control system and the data and reports submitted to and used by the Navy that are derived from the system. Compliance with these criteria is usually a requirement of contract awards.

Our review disclosed Navy correspondence with the contractor showing that, beginning in mid-1980 and extending for almost 2 years, Electric Boat's cost and schedule control system was not fully complying either with DOD Instruction 7000.2 or with its own SUBCOM system description. The documentation identified a number of contractor practices associated with the operation of the system that the Navy perceived as deviating from the system as originally approved. Among the problems cited were Electric Boat's practices of making retroactive changes to budgets and schedules and overvaluing the budget allocation for work performed early in the construction cycle. Since labor progress was computed at Electric Boat by estimating the percentage of work completed and then multiplying this percentage by the budgeted hours for the work, an overstated labor hour budget for work to be accomplished early in the contract would result in greater reported progress.

#### Indications that overprogressing may have occurred as early as 1980

Navy documentation reviewed indicates that practices noted above began to appear in mid-1980 and resulted in early payment of work progress from that time until March 1982. For example:

- An internal Navy memorandum in August 1980 referred to the fact that Electric Boat's SUBCOM system overstated the earned value (hours) and reflected unrealistic scheduled earned budgets.

--Supship informed Electric Boat in October 1980 that "the Cost Reports and supporting data indicate many instances of retroactive changes to schedule and budget for TRIDENTS and SSN 688 ships."

--A Navy review of the SUBCOM system in June 1981 showed that Electric Boat had made frequent changes to budget and schedules for completed and in-process work.

--The Navy advised Electric Boat on October 1, 1981, that retroactive changes to budget and schedule should cease and that retroactive changes to data previously reported were excessive.

--An internal Navy memorandum, dated October 21, 1981, stated that "it is evident, at the ship level, based on historical data, that we are making early progress payment because of 'rubber' budget baselining." (According to other Navy documents, continuous revisions to work authorization budgets constituted, in the Navy's view, a "rubber baseline" against which performance measurement was very difficult.)

The Navy attempted to get Electric Boat to correct these problems, but the contractor continued the practices into 1982. In February 1982, the Navy told Electric Boat that it considered the company's answer to the June 1981 review findings "to be generally unresponsive and does not propose satisfactory solutions to the problems."

1982 budget revision causes the Navy to disapprove Electric Boat's progressing system

In March 1982, Electric Boat revised the budgets for its contracts. Approximately 16 million labor hours were added to the work authorization budgets, with the majority of the hours going to tasks that were in process or had already been completed. The increased budgets were then multiplied by the percentages of completion claimed by the foremen. As a result, Electric Boat claimed to have earned 12.6 million hours during a 2-week period in which it had worked 1.8 million hours. As previously discussed, labor progress is based on earned hours. Therefore, the revision would have resulted in increased progress payments if the Navy had not acted.

On April 7, 1982, Supship notified Electric Boat that because of the many problems previously discussed with the company, including the March 1982 budget revision, the Navy could no longer rely on Electric Boat's progressing system to accurately reflect the physical progress of individual submarines. Consequently, the Navy said it would use Supship's calculation of physical labor progress to compute progress payments. The Navy's action, in effect, suspended payments that were based on Electric Boat's progressing system until such time

as revisions to the system acceptable to the Navy were made. These revisions were accomplished in March 1983.

Effect of budget revision  
on progress payments

Of the 12.6 million hours that Electric Boat claimed were earned, 11 million were charged to the SSBN Trident I contract and the SSN 688 II contract, as shown below.

<u>Contract</u>	<u>Claimed hours earned</u>	<u>Actual hours expended</u>
SSBN Trident I	5.9 million	0.6 million
SSN 688 II	5.1 million	0.7 million

Because of payment limitations contained in the Trident I contract, the revision would not have resulted in increased progress payments on that contract at that time. On the other hand, Electric Boat would have received approximately \$11.3 million in increased progress payments on the SSN 688 II contract had Supship not substituted its own calculation of labor progress.

SSBN Trident I contract. Most submarine construction contracts, including the Trident I, contain a provision that states a contractor cannot be paid more than a certain percentage of costs incurred. In the Trident I contract, the limitation is specified as 100 percent of costs incurred. If progress payments computed according to contract terms resulted in tentative payment amounts larger than the amount of costs incurred, then this excess amount is to be deferred and not paid to Electric Boat.

During the period in which its progressing system was suspended, Electric Boat continued to submit progress payment invoices based on the revised budget and Supship continued to calculate its own progress on each invoice. However, under either method, the calculated payment exceeded cost incurred. Consequently, payments made to Electric Boat remained unchanged, with each party calculating different amounts as being deferred. The table below illustrates this difference. The information is based on data contained in the first progress payment invoice Electric Boat submitted after the budget revision and is on a cumulative basis from inception of the contract.

	<u>Progress</u>	<u>Calculated payment</u>	<u>Costs incurred</u>	<u>Actual payment</u>	<u>Amount deferred</u>
		- - -	-(millions)-	- - -	-
Per Electric Boat	89.40%	\$1,607.2	\$1,574.5	\$1,574.5	\$32.7
Per Supship	87.43%	1,582.6	1,574.5	1,574.5	8.1

SSN 688 II contract. The SSN 688 II contract (N00024-74-C-0206) authorized the construction of 11 SSN 688 class submarines (SSN 700-710).

As with the SSBN Trident I contract, from April 1982 to March 1983, Supship recomputed each progress payment invoice based on its own calculation of the percentage of completion. The recomputation resulted in varying reductions. The largest reduction on a single invoice was \$19 million and the smallest was \$3.98 million. The \$19 million was withheld from the first invoice. On that invoice, Electric Boat reported the contract to be 82.58 percent complete and claimed a payment due of \$55.8 million. Supship calculated completion as 81.27 percent, with a resulting payment due of \$36.8 million, or \$19 million less.

#### Supship approval of revised progressing system

During the suspension period, Supship and Electric Boat negotiated changes to the progressing system. Supship, in a letter dated May 20, 1982, pointed out a number of deficiencies that needed correction and stated that any progressing system that relied on a budget that was unequivocally distributed or was changed retroactively would be unacceptable.

On August 4, 1982, a memorandum of agreement was signed in which Electric Boat agreed to a number of conditions. Electric Boat agreed to establish and maintain a performance measurement baseline that was in accordance with its Navy-approved cost and schedule system. It also agreed that reprogramming of effort remaining in the contracts would be restricted to the preparation of new annual Division Operating Plans or to major changes caused by unusual circumstances and that reprogramming results would be reviewed with appropriate Navy personnel. Furthermore, Electric Boat agreed that it would not make retroactive changes to data previously submitted.

On August 30, 1982, Electric Boat submitted to Supship a progressing system description that incorporated changes in response to Supship's stated objections and to the recently signed memorandum of agreement. Further discussions were held between the two parties, with Supship withholding approval of the progressing system until Electric Boat incorporated its 1983 operating plan into the cost and schedule control system. On March 15, 1983, Supship provided some additional comments on the proposed system. Their general comments included requirements that (1) progressing must be consistent, accurate, and auditable to the work authorization level, (2) every other system used in the determination of progress but not submitted directly for approval forms a part of the progressing system and, as such, is subject to audit and subsequent disapproval if found to be deficient, and (3) each change to the system must receive Supship approval before being used for billing purposes.

On March 16, 1983, Electric Boat submitted another system description and, on March 24, 1983, Supship notified Electric Boat that the proposed system was acceptable for use in determining progress payments. In addition, Supship stated it intended to initiate an ongoing program of independent surveillance to assure that the progressing system was consistent, accurate, and auditable and that the system description was complied with.

#### Electric Boat and Supship views

In a letter to us dated December 18, 1985, Electric Boat stated that the March 1982 budget revision was made to reflect the manhour goals for the construction contracts in process, in accordance with the 1982 Operating Plan. Electric Boat stated that the manhour goal for delivered submarines is the actual number of manhours expended. It also stated that the budgets were adjusted to clarify the goals to Electric Boat personnel responsible for achieving them. According to Electric Boat, its intent was not to accelerate progress payments beyond actual construction progress, but to motivate managers to improve construction methods and reduce costs. Electric Boat stated that the 1982 replanning effort provided the baseline the Division required and that a similar major replanning effort has not been done since.

Electric Boat's response did not comment directly on whether or not the budget revision would have accelerated progress payments, except to state that was not its intent. Electric Boat claimed, however, that the payments Supship computed after March 1982 were too low, thus causing the Division to be underpaid. Electric Boat stated that, as time passed, it became clear that Supship's calculations were incorrect and, therefore, Supship began accepting Electric Boat's progress values again in March 1983. Electric Boat contends that any statements, which claim that it has made and continues to make retroactive changes to budget and schedule which impact on progress payments, are without merit.

We asked Supship officials to comment on Electric Boat's letter. The officials disagreed with Electric Boat's assertion that the Navy began accepting Electric Boat's progress values again in March 1983 simply because the Navy's calculations were incorrect. They said that Electric Boat's system was initially disapproved because of deficiencies in its operation, and that it was accepted again in March 1983 only because Electric Boat had made revisions that, in the Navy's opinion, corrected the deficiencies.

Supship officials also stated, however, that there was some validity to Electric Boat's assertion that it was underpaid during the suspension period. During this period, Supship calculated progress based on its own estimate of cost at completion. Subsequent Supship experience showed that its

estimate was slightly high on the SSN 688 II contract. Consequently, the officials stated that the amount withheld from Electric Boat was probably too high. They believed recomputing the correct amount now would be a very time-consuming process, if it could be done at all.

Supship officials stated that Electric Boat's budget revision was the culmination of a long-running dispute with Electric Boat over its noncompliance with DOD Instruction 7000.2. They noted that the revision claimed most of the additional labor hours against work authorizations already completed or submarines already delivered to the Navy, and that this would have inflated progress payments.

When we asked if Supship had considered charging Electric Boat with a violation of the False Statements Act (title 18, U.S.C. 1001),<sup>1</sup> the officials stated that they had not because they were not looking for this type of violation. They noted that there had been an ongoing attempt by Supship to get Electric Boat to improve in a number of areas, such as improving compliance with DOD Instruction 7000.2 and increasing its estimates of construction costs to more realistic levels. The officials stated that Electric Boat had informed the Navy ahead of time that the budgets were being revised. Consequently, while Supship objected to how the hours were charged to contracts, Supship told us that it believed the budget revisions which resulted in increases were a step in the right direction by Electric Boat.

#### Other noncompliance issues

During our review, we found that Navy documentation identified other effects of Electric Boat's noncompliance with DOD Instruction 7000.2. The Navy documents indicated that the contractor's noncompliant budgeting and other practices also may have resulted in suppression of cost and schedule variances and inaccurate or misleading cost reports during the period that overprogressing occurred.

We did not review these matters because they were beyond the scope of this review. However, we did discuss the issues

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<sup>1</sup>Title 18, United States Code 1001 states:

"Whoever, in any matter within the jurisdiction of any department or agency of the United States knowingly and willfully falsifies, conceals or covers up by any trick, scheme, or device a material fact or makes any false, fictitious or fraudulent statement or entry, shall be fined not more than \$10,000 or imprisoned not more than five years, or both."

with the Subcommittee who agreed that the issues were related to those being reviewed by the Department of Justice's Special Task Force, which is investigating shipbuilding activities in the Electric Boat Division of General Dynamics. With the advice and concurrence of the Subcommittee, we discussed and provided the pertinent documentation to members of the task force.

### SPECIAL PROVISION ON CONTRACT RETENTIONS

During our review of the allegation on progress payments, we found the Trident IV and SSN 688 VII contracts contained special retention clauses which allowed Electric Boat to receive progress payments that substantially exceeded the amounts that would have been paid under normal progress payment contract clauses. This occurred because the retention clauses had the effect of deleting the payment limitations associated with the payment clauses.

As of August 1985, we estimated the amount of additional progress payments realized through these provisions totaled \$69.6 million on the Trident IV and \$1.2 million on the SSN 688 VII contracts. We also estimated that the interest cost to the government for these payments was \$9.9 million.

We determined that this particular special retention provision was first used on a sole-source submarine contract awarded in August 1981 to Newport News Shipbuilding Dry Dock Company, but we did not determine whether it was used on other Navy shipbuilding contracts.

### Progress payments

Because of the length of time involved in constructing submarines, contractors are allowed to receive periodic progress payments during the construction period. The payment is the sum of the amount due for construction work accomplished based on the percentage of work completed, plus the amount due for escalation (inflation) at that time. The total payment, however, is normally subject to a payment ceiling that is based on a specified percentage of the allowable costs actually incurred. If the computed progress payment exceeds the specified percentage of costs incurred, the excess is not paid to the contractor.

The standard clauses for progress payments and for escalation payments, including the payment limitation, were included in both the Trident IV and the SSN 688 VII contracts. However, in both contracts, we found that these clauses were superseded by the insertion of a third clause--Special Procedures Concerning Contract Retentions.

### Trident IV

The Trident IV contract (N00024-81-C-2134) was awarded in January 1982 for the construction of the SSBN 734. Two



additional Tridents (SSBN 735 and 736) were subsequently added through the exercise of a contract option. The contract price for these three submarines totaled \$1.6 billion.

The contract contains the standard Progress Payment Clause (Clause H-2) and the Compensation Adjustment Clause (Clause H-5). The latter clause governs the payment of escalation. These clauses contain payment limitations, which vary depending on the percentage of physical completion of each submarine. The clauses state that the combined payments for progress and escalation for each submarine shall not exceed the following:

Up to 25% complete	90% of the payment due; not to exceed 100% of costs incurred.
25% to 50% complete	Payment due less 2.5% of the contract price; not to exceed 105% of costs incurred.
Over 50% complete	Same as preceding category, but not to exceed 107% of costs incurred.

These, or similar, payment restrictions are contained in all the Trident contracts. The Trident IV contract, however, contains a clause entitled Special Procedures Concerning Contract Retentions (Clause H-74) that states both parties recognize that contract retentions specified in the progress payment clause might exceed the amount necessary to accomplish the objectives of such retentions. Consequently, the clause specified an alternative method for computing payments that deleted the requirement to retain 2.5 percent of the contract price and substituted a retention of \$22.5 million per submarine.

Although the stated purpose of the special retention clause was to change the amount of contract retentions, the Navy interpreted the clause as also deleting the payment limitations contained in the contract payment clauses. Therefore, Electric Boat received progress payments calculated through the application of the special retention clause without regard to any ceiling limitation.

As of August 9, 1985, Electric Boat had incurred costs of \$740.4 million and had received payments of \$847 million, or \$106.6 million more than the amount of costs incurred. We estimate that this is \$69.6 million more than the amount that would have been paid under the standard payment clauses. At one point, payments made represented about 115 percent of incurred costs.

#### SSN 688 VII

The SSN 688 VII contract (N00024-82-C-2055) was awarded in February 1982 for the construction of the SSN 724. The SSN 725 was subsequently added to the contract through the exercise of a

contract option. The contract price for these submarines totaled \$471 million.

As in the Trident IV contract, the same payment limitations for this contract were also superseded by a special retention clause for contract retentions. This retention clause was the same as the clause in the Trident IV contract, except that it specified a retention of \$7.5 million a submarine, not \$22.5 million.

As in the case of the Trident IV contract, the Navy interpreted the clause as also deleting the contract payment limitations of the contract payment clauses. Therefore, Electric Boat received the progress payments calculated through the application of the special retention clause without regard to any ceiling limitation.

As of August 16, 1985, Electric Boat had incurred costs of \$358.9 million and had received payments of \$377.5 million, or \$18.6 million more than costs incurred. We estimate that this is \$1.2 million more than would have been paid under the standard payment clauses. At one point, payments represented about 110 percent of incurred costs.

#### Interest cost

As a result of the special retention clauses in these two contracts, the Navy made payments that were substantially in excess of the amount that would otherwise have been paid. We estimate that the interest costs incurred by the government on this difference, from contract inception to August 1985, were \$8.5 million on the Trident IV contract and \$1.4 million on the SSN 688 VII contract.

To evaluate the effect of the special retention clause on each contract, we estimated the amount the progress payments would have been on a monthly basis had payment limitations been in effect, compared this amount to the payments actually made, and computed the interest cost on the difference using the interest rates for 3-month Treasury bills (auction average) in effect at the time.

Because the invoices submitted by Electric Boat disclosed costs incurred on a total contract basis, we estimated the amount of the cumulative payment that would have been made each month. Since the payment limitations had been superseded, there was no requirement for the invoices to show costs incurred for each submarine.

Electric Boat personnel stated that it would be a very time-consuming process to reconstruct the costs incurred for each submarine for each invoice submitted. As an alternative, we computed the payments on a contract basis using the total costs incurred monthly for the contract and the monthly contract

percentage of completion. We believe that the result, when used over a period of time such as this, is a reasonable approximation of the actual amounts involved.

#### Electric Boat views

We discussed the use of the special retention clause with the Electric Boat Division Controller who said that this clause was first used in the SSN 688 VI contract with Newport News Shipbuilding. He believed the clause to be reasonable, given the fact that the Navy had introduced the 50-50 cost sharing concept into the contracts. He said the 50-50 share line significantly increased Electric Boat's risk and the special retention clause may have been intended by the Navy as a means for making the risk more acceptable to the contractor.

#### Previous use of retention clause

We confirmed that a special retention clause identical to the one in the Electric Boat SSN VII contract was used in an earlier contract awarded to Newport News Shipbuilding and Dry Dock Company on August 13, 1981, for three submarines (SSN 721, 722, and 723). According to the Post-Negotiation, Business Clearance Memorandum for the award, this clause was intended to limit the amount of contract retentions under the payments clause to a maximum of \$7.5 million a ship.

It was further stated that:

"It is considered that the contract retentions resulting from the 'Payments' clause are much greater than needed to accomplish the objectives of such retentions. Shipbuilding contracts for SSN 688 Class ships are of a high dollar value with a 6-7 year period of performance. Risk to the Contractor is substantial and thus, Contractor profits should not be unduly eroded by excessive retentions. The Exhibit 26 special retention] clause alleviates this problem by providing for the special release of excessive contract retention amounts. The mechanism of the clause will result in maximum contract retention amounts which are consistent with those of the recently awarded CVN-71 contract.\*\*\*"

The negotiation document also noted that the Naval Sea Systems Command had obtained Assistant Secretary of the Navy (Shipbuilding and Logistics) approval for the special release of contract retentions under this contract.

#### Subsequent use of retention clause

The Trident IV and SSN 688 VII contracts were the only contracts at Electric Boat in which the special retention clause eliminated the payment limitations. Such a clause was not included in the Trident V contract (N00024-85-C-2062) awarded on

August 13, 1985, for the SSBN 737. The Trident V contract incorporates the following payment limitations:

0 to 50% complete 90% of the payment due; not to exceed 100% of costs incurred.

Over 50% complete Payment due less 5% of contract price; not to exceed 105% of costs incurred.

The SSN 688 VIII contract (N00024-83-C-2039) awarded on November 30, 1982, and the SSN 688 IX contract (N00024-84-C-2063) awarded on November 23, 1983, included modified versions of the retention clause. The clauses in these two contracts limit payments to not more than 100 percent of allowable costs incurred, plus applicable profit calculated as a percentage of incurred costs.

We did not determine whether the special retention clause that deleted the payment limitations was used on other Navy shipbuilding contracts.

#### ADVANCE PROCUREMENT OF LONG LEAD TIME MATERIAL

##### Allegation

The amount of funding authorized for advance procurement of long lead time material was excessive on the Trident submarine program.

##### GAO findings

Advance procurement funding for long lead time material (LLTM) associated with Trident submarine construction was similar for each of the first seven, then increased substantially over the next four submarines. According to Navy and Electric Boat officials, the primary reasons for the funding increases were inflation and changes in construction sequencing that required installation of more components earlier in the construction cycle.

We confirmed that construction sequencing changes and inflation were responsible for some of the increase. However, our review disclosed a number of instances where materials purchased under advance procurement contracts did not qualify as LLTM. This situation also contributed to the increase in funding.

We found that the contractor does not benefit financially from early purchases of material because of the procurement approach used on LLTM. However, inclusion of such material in Navy advance procurement budget requests to the Congress could result in premature funding.

### Purpose of advance procurement

Generally, a typical Trident submarine takes 6 years to construct and is built according to a master construction schedule. In order to conform to the schedule, some material and components with long delivery lead times must be purchased before a construction contract is awarded in order to have them available when needed. These long lead time materials are purchased through advance procurement contracts which, on the Trident submarine program, have typically provided funding for a 2-year period prior to award of the construction contract.

### Selection of long lead time material

Electric Boat prepares a master candidate list of LLTM items based on when material must be ordered in order for it to be available when needed. The candidate list is prepared by working backwards from the date the item is required to be in a shipyard. Vendor lead time is deducted from the required-in-yard date to determine the date the purchase order must be placed. Administrative lead time of approximately 6 months is then deducted to account for the time needed to prepare the purchase requisition, obtain bids, and place the purchase order with the vendor. The material is a valid LLTM candidate if this final date occurs before the expected award date of the construction contract.

The Navy reviews the master candidate list and makes the final determination as to which items will be funded for advance procurement. The advance procurement contracts with Electric Boat are cost, no fee contracts, whereby Electric Boat is reimbursed for actual costs incurred but does not receive a profit on these costs until after the construction contract is awarded.

Material and components purchased as LLTM are included in the construction contract at a cost based on the latest information available when the contract is negotiated. When the construction contract is awarded, the funding authorized in the advance procurement contract is reduced to zero.

### Funding for Trident submarine advance procurement

As of December 31, 1985, construction contracts had been awarded for 12 Trident submarines. Contracts for the first seven Tridents (SSBN 726-732) were awarded between July 1974 and March 1978. Advance procurement funding on each of these submarines was similar, with the lead Trident receiving \$40 million and each of the following six submarines approximately \$36 million.

The SSBN 732, however, was the last submarine funded at that level. Advance procurement funding on each of the following four Tridents increased rapidly, rising from \$35.5

million on the SSBN 732 to \$148 million on the SSBN 736. Funding for the SSBN 737 then decreased to \$126.4 million. This amount included \$33 million for two major components previously provided as government-furnished equipment, not as LLTM. Excluding these items, the advance procurement funding for this ship was \$93.4 million, or 37 percent less than the funding for the SSBN 736. The following table illustrates the advance procurement funding which occurred from the SSBN 732 through the SSBN 737.

Advance Procurement Funding

<u>Ship</u>	<u>LLTM funding</u>  (millions)	<u>Percentage increase prev. ship</u>	<u>LLTM period</u>
SSBN 732	\$ 35.5	- 0 -	12/75 to 3/78
SSBN 733	70.5	98.5	9/78 to 1/81
SSBN 734	101.2	43.6	2/80 to 1/82
SSBN 735	129.0	27.5	7/80 to 11/82
SSBN 736	148.0	14.7	2/82 to 11/83
SSBN 737	126.4	(14.6)	11/83 to 8/85

Electric Boat and Navy views on funding increases

Electric Boat officials stated that the need for significant increases in advance procurement funding occurred primarily because of changes in construction sequencing. They stated that Electric Boat has become increasingly capable of installing more detailed component packages earlier in the construction of the hull cylinders, thus requiring earlier receipt of material and components. They also stated that a general overall improvement in the efficiency and effectiveness of building submarines has naturally resulted in the need for more material at an earlier date.

A Navy project office official stated that some of the LLTM funding increases occurring from the SSBN 732 to the SSBN 736 were due to cost escalation and to increased material requirements caused by changes in construction sequencing. He stated that Electric Boat was installing more material in the hull cylinders earlier in the construction cycle as part of its effort to improve the construction process, with a consequent increase in the amount of material required before contract award.

The project office official also stated that there was much turbulence in the Trident program when the rapid funding increases occurred, which made it difficult to estimate the funds needed for LLTM. He cited the following events as being primarily responsible for the turbulence: authorization of ships later than originally planned, breaks in planned yearly

production, delays in ship awards due to changes in procurement approach, major changes in ship configuration after contract award (change from C-4 missile to D-5 missile), and changes in construction sequencing at Electric Boat.

The project office official stated that by 1984 the program had stabilized to the point where an engineering review could be done on the LLTM list. This Navy review found that Electric Boat was being too "conservative" in projecting LLTM requirements and that much of what it wanted to order to protect schedules was not justified as LLTM. According to the Navy, Electric Boat was trying to cover too many contingencies by having material earlier than was demonstrated as being necessary by the construction sequence. As a result, the Navy said it reduced the value of the LLTM list by 37 percent on the SSBN 737. Based on this review, the project office official said that the \$148 million authorized for the SSBN 736 was probably too high and that it should probably have been about \$93 million.

The project office official stated that Electric Boat does not benefit financially by purchasing equipment or material earlier than needed since no fee is paid on items until after a construction contract is awarded. He also stated that the Navy now continually analyzes Electric Boat's performance on obtaining required material under the LLTM contract and systematically reviews construction schedules to verify that they still support LLTM requirements.

#### Examples of items not qualifying as LLTM

We confirmed that construction sequencing changes occurred and, along with inflation, were responsible for some of the LLTM funding increase. However, during our review, we noted a number of instances where equipment purchased under the LLTM contracts for various Tridents did not appear to qualify as LLTM because the purchasing cycle did not need to be started until after the construction contract was awarded. We selected some of these items for follow-up with both Electric Boat and the Navy. Electric Boat officials' comments are discussed below in connection with the individual items.

Examples of items purchased as LLTM that did not qualify as LLTM follow.

#### 1. SSBN 735 - Construction contract awarded 11-19-82

Item B-24; 1200 KW diesel generator; \$950,000

According to an LLTM listing dated September 22, 1981, the purchase requisition for this item needed to be placed December 4, 1982, and the purchase order placed May 21, 1983, in order for the generator to be available August 18, 1984. The actual procurement sequence was as follows:

Mar. 1982: Funds authorized by the Navy.  
Aug. 1982: Purchase requisition prepared.  
Nov. 1982: Purchase order placed.  
Dec. 1983: Generator delivered.

An Electric Boat official stated that the planning schedule called for the purchase requisition to be prepared so close to the actual contract award that it qualified as LLTM. We agree that given the planning dates being used at the time, the generator could be considered a borderline LLTM item. However, we also noted that as of December 1985, the generator had not been used, even though it had been delivered 2 years earlier.

2. SSBN 736 - Construction contract awarded 11-21-83

(A) Item B-70; countermeasure launcher firing valve; \$4 million

Per an LLTM list dated August 20, 1982, the purchase requisition for this item needed to be prepared August 11, 1984, and the purchase order placed February 2, 1985, in order for the item to be available May 3, 1986. The actual procurement sequence was as follows:

Oct. 1982: Funds authorized by the Navy.  
Dec. 1982: Purchase requisition prepared.  
Feb. 1983: Purchase order placed.

An Electric Boat official stated that available planning data did not support procurement as LLTM for schedule reasons. He said that the valve was purchased as LLTM on the SSBN 735 and SSBN 736 because several earlier ships had experienced problems with the valve requiring them to be returned to the vendor.

We found that the budget for this item was \$70,000 on the SSBN 735 and \$4 million on the SSBN 736. Electric Boat officials stated that the \$4 million budget was established in error and that they could document no reason for it. They said the latest information available indicated an actual cost of approximately \$145,000.

(B) Item A-4; main condensate pump; \$870,000

Per an LLTM list dated August 20, 1982, the purchase requisition for this item needed to be prepared March 3, 1984, and the purchase order placed August 18, 1984, in order for the pump to be available October 12, 1985. The actual procurement sequence was as follows:



Oct. 1982: Funds authorized by the Navy.  
Apr. 1983: Purchase requisition prepared.  
Apr. 1983 Bids solicited.  
Nov. 1983: Negotiations completed.  
Mar. 1984: Purchase order placed.

An Electric Boat official stated that the LLTM list we used was not the correct list. He cited an earlier LLTM list, dated September 22, 1981, which states that the purchase requisition should be prepared in September 1983--2 months before the award of the construction contract. He stated that, based on this list, the pump was a qualified LLTM item.

We believe that the LLTM list we used was the proper list since it was available for approximately 2 months before funds were authorized by the Navy. According to this list, procurement did not need to be initiated for at least 3 months after the construction contract was awarded.

A project office official advised us that he did not have the detailed purchasing justifications available and would therefore rely on Electric Boat's response to us for information on these items. He stated, however, that since the Navy had reduced the LLTM list for the SSBN 737 and subsequent hulls, he would not be surprised if some of the items could not be justified as LLTM items. He added, however, that he knew of no additional cost resulting from a limited number of such errors and believed that the current state of the program allows much better judgments to be made today.

#### ESCALATION ON THE LEAD TRIDENT SUBMARINE

##### Allegation

In October 1981, the Naval Sea Systems Command authorized \$50 million for escalation for the lead Trident submarine (U.S.S. Ohio). This amount, if actually paid to Electric Boat, was excessive, given that the submarine was delivered to the Navy that same month.

##### GAO findings

We found that the actual amount of escalation funds made available to Supship, Groton, in October 1981 for the SSBN 726 (U.S.S. Ohio) was \$36.7 million, not \$50 million. The disposition of these funds was

--\$6.7 million was used to repay the escalation accounts of two follow-on Trident submarines (SSBN 727 and 729) for

funds previously borrowed to make normal escalation payments on the U.S.S. Ohio during July, August, and September 1981;

--\$22.6 million was added to the \$159.8 million in escalation previously authorized for the Ohio; and

--\$7.4 million remained in the escalation account at Supship, Groton.

We traced the payments actually made to Electric Boat and determined that because of contract payment limitations, the increase in escalation authorized did not result in any additional payment to Electric Boat.

#### Additional escalation authorized

The first contract for Trident submarines (N00024-75-C-2014), called for the construction of seven Tridents and was split into two groups. The first group (known as Group I) authorized the construction of four submarines. The first, or lead, submarine constructed under Group I was the U.S.S. Ohio (SSBN 726), which was delivered to the Navy on October 28, 1981.

The \$22.6 million authorized by a contract modification as additional escalation in October 1981 for the U.S.S. Ohio was the result of a change in the method used to calculate escalation. The contract contained two clauses (Sub-Articles I and II) for the calculation of escalation. Sub-Article I was to be used during contract performance and contained tables to be used in estimating the monthly labor and material costs. Upon delivery of the last submarine in each group, the escalation due for each submarine was to be recalculated according to the terms of Sub-Article II. This provided for escalation to be calculated based on revised tables that used the actual number of months involved in construction and the percentage of total costs actually incurred during each month.

Although not contractually required to use Sub-Article II until January 1984, when the SSBN 729 (the fourth and final submarine in Group I) was delivered, Supship elected to apply it in October 1981 to recalculate escalation applicable to the SSBN 726 (U.S.S. Ohio) upon its delivery. As a result, escalation authorized for the U.S.S. Ohio increased by \$22.6 million--from \$159.8 million to \$182.4 million.

The Supship Supervisory Contract Specialist for the Trident Program told us that the change was a Supship initiative; i.e., it was not directed by the Naval Sea Systems Command or requested by Electric Boat. He said that the change was discussed with and agreed to by both the Naval Sea Systems Command and Electric Boat.

The Supship official stated that the payments to Electric Boat under this contract are calculated on a group billing base; i.e., based on the total billing base for all submarines in a group. This base is allocated to each submarine in the group based on the relationship of the submarine's projected de-escalated final cost to the total group de-escalated final cost. Accordingly, any fluctuation in the group cost, regardless of cause, would affect each submarine's allocated share of the group billing base, even if that submarine had already been delivered.

The official said these changes would result in the need to continually realign funding on all ships. To avoid these changes on delivered ships, Supship isolated each submarine from the group as it was delivered and attempted to establish the cost as close as possible to the actual final cost. He said this involved using Sub-Article II to determine escalation because the final calculation was to be based on Sub-Article II.

#### Effect on payments

Under the terms of the Trident I contract, Electric Boat could not be paid more than the total of actual costs incurred on the group plus the profit on any delivered submarines.

At the time of delivery of the U.S.S. Ohio, the costs incurred (approximately \$1,443.8 million) on the Group I submarines were less than the computed amount of the progress payments (\$1,492.3 million). Consequently, the increase in authorized escalation did not directly increase progress payments made to Electric Boat. Under either method of computing escalation, progress payments due would have exceeded this amount and the excess would not have been paid.

The changes made by Supship at the time of delivery resulted in a more reasonable allocation of profit under the Trident I contract. Profit is ordinarily computed by comparing actual cost at completion to the contract target cost and applying contract cost-sharing provisions to the resultant cost underrun or overrun to arrive at the amount to be added to or subtracted from the contract target profit. In computing the underrun or overrun, however, actual cost at completion has to be de-escalated to be on a comparable basis with contract target cost, which does not include an amount for inflation. This is accomplished by subtracting authorized escalation from the actual cost at completion. The higher the amount of escalation subtracted, the lower the resulting de-escalated actual costs will be. Under a normal computation of profit such as described above, increasing the amount of escalation authorized would result in a lower de-escalated actual cost at completion and, consequently, a higher profit.

The Trident I contract was unique, however, in that it required computations to be made on a group basis as opposed to

individual ships. Under this approach, the billing base, which includes profit, is allocated to each submarine based on the relationship of its cost at completion to the total group cost at completion. As a result, the submarine with the highest cost at completion is allocated the largest share of the billing base and, consequently, the largest share of the group profit, which at the time of the delivery of the U.S.S. Ohio in October 1981 was calculated as approximately \$94 million. Since the U.S.S. Ohio had the largest cost overrun, it also had the highest cost at completion and accordingly would have been allocated the largest share of profit. In this regard, Supship officials stated that the computed profit on the U.S.S. Ohio would have been approximately \$35 million, or \$12 million more, had they not isolated the submarine upon its delivery.

Supship officials stated that an allocation such as above, although in accordance with contract terms, would have obviously been unrealistic and at odds with economic reality. They noted that the fourth and final submarine in the group (SSBN 729) actually underran target cost and therefore probably earned the highest actual profit for Electric Boat. However, if profit were computed on a group basis and then allocated to each submarine as described above, the SSBN 729 would have been allocated the smallest share. The officials stated that more accurate and realistic results were obtained by isolating each submarine as it was delivered. They believed that the potential effects on contract payments and funding were not recognized at the time the Trident I contract was negotiated, and noted that all subsequent contracts have required payments to be made on the basis of individual submarines, not on a group basis.

## DESTRUCTION OF NAVY RECORDS

### Allegation

In November 1983, a destruction of records took place at PMS 396P during a period when three investigations, one of which was a Federal Bureau of Investigation (FBI) effort, were reportedly ongoing.

The records destruction violated the Navy's policy; potentially obstructed justice with the past and ongoing investigations; and eliminated documentation that could have been used to substantiate allegations being focused at the Trident program.

### GAO findings

Our review showed that PMS 396P conducted a general records disposal effort and that most of the disposal activities

occurred between September 1983 and September 1984. During this effort, many records were destroyed, including files and reports. According to officials responsible for and involved in the effort, the records disposal was conducted because of a need for additional office space and to organize PMS 396P's filing system in accord with the Navy's standard file indexing system.

Secretary of the Navy Instruction P5212.5B provides authority for the periodic destruction of records based on prescribed record retention standards. The Navy process classified the retention standards for the various records according to standard subject identification codes (SSICs). These codes not only identify the subject of the documents but also state how long they should be retained. Although PMS 396P compiled an inventory of documents and decided upon their disposition, we could not independently determine whether retention standards were observed on records earmarked for destruction. We were unable to do this because the subject identification codes, which would have facilitated this determination, had been omitted from a designated column on the inventory listing for most of the documents.

Our review also showed that there were ongoing investigations of Trident program matters during the period in which the records disposal took place. We identified nine ongoing investigations, including three by the FBI. We found no evidence that PMS 396P officials were contacted by the investigative agencies during the period in which the disposal activities occurred.

#### PMS 396P records disposal

According to PMS 396P officials, a records disposal was conducted because of a need for additional office space and to organize a filing system that was in accord with the Navy's standard file indexing system. Most of the disposal activities took place from September 1983 through September 1984. The overall management of the records disposal was assigned to a staff member of PMS 396P and a private contractor--Automation Industries, Inc., Vitro Laboratories Division--provided assistance during the disposal effort.

Beginning in September 1983, an inventory listing of all PMS 396P documents was compiled and distributed to branch heads within that office. According to the PMS 396P staff member, these individuals either decided on the disposition (retain, microfiche, archive, or destroy) for each document maintained within their respective unit or delegated this task to subordinates. This individual further advised that most of the disposition decisions assigned to the documents were executed by September 1984.

### Retention standards

Secretary of the Navy Instruction P5212.5B states that records retention standards are the basis for establishing activities' records disposal programs. Retention standards prescribe how long records are to be kept, whether temporarily or permanently. Retention of temporarily valuable records is expressed in terms of time or the occurrence of a particular event or action.

The instruction classifies standards according to the SSIC, which is a code that stands for the subject of a document. According to Navy policy on identification codes, SSICs are required on all Navy and Marine Corps letters, messages, directives, forms, and reports. However, Navy disposal policy does not require a SSIC on an inventory listing for initially establishing disposal programs or when initially applying the instruction. This policy recommends various steps to establish a records disposal program, such as taking inventory of all records series to be covered in a disposal effort and obtaining information needed to match each record series with the appropriate retention standard. According to the person who managed the PMS 396P disposal effort, a subject code was assigned after a retention decision was made to save time and effort.

### Ongoing investigations

Navy disposal policy also requires that in the event of an ongoing investigation, pertinent records be retained until the investigation is completed.

The former Director advised us that he was not aware of any ongoing investigations during September 1983 through September 1984, but was aware of Mr. Kalmin's internal grievance. Further, the current Director stated he cannot recall being aware of any ongoing investigations during the time of the disposal, but he was aware of charges made by Kalmin. The individual that managed the disposal said she cannot recall being aware of any ongoing investigations.

We established that there were ongoing investigations of Trident program matters during the period in which the records disposal took place. We identified nine ongoing investigations, including three by the FBI. We reviewed closed case files on each of six Navy investigations and discussed the cases with investigative personnel. We also discussed the three FBI investigations with an agency official. We found no evidence that PMS 396P officials were contacted by the investigative agencies during the period in which the disposal activities occurred.

TASK AUTHORIZATION AND FUNDING  
ON ENGINEERING SERVICES CONTRACTS

Allegation

Authorization to begin work on a design contract was given over the telephone before the contract was awarded, and before (fiscal year 1984) funds were available. In this regard, the Director PMS 396P approved new work telephonically even though he was not the approved contracting officer.

New (fiscal year 1984) work was approved that required Operations and Maintenance, Navy (O&MN) appropriation funding in an amount over \$500,000 in January 1984. The only type of funds that were legally available for this work were fiscal year 1984 O&MN funds. The fiscal year 1984 funds had been authorized but, at the time the new work was authorized, the contract had not been modified to add that money and that specific work to the scope of the contract. Only fiscal year 1983 O&MN funds and work scope were present in the contract at the time of the phone call.

GAO findings

In support of this allegation, three documents--a General Dynamics/Electric Boat Telecon/Conference Report, dated January 3, 1984; an internal PMS 396 memorandum, dated January 23, 1984; and a Trident Task Assignment Data Package Action Sheet--were cited. Based solely on the cited documents and funding information contained therein, Mr. Kalmin could reasonably conclude that the task in question was outside the work scope of the contract and that funding for the task was not provided by the identified contract modification. However, our review disclosed that there were additional documents, actions, and information associated with this transaction that, when considered, produce a different conclusion. Thus, we found that the task in question was issued within the contract work scope and appropriate funding was available for this type of work.

Our analysis of standard operating procedures in PMS 396 and related contract information indicated that at the time of the task transaction, the Director, PMS 396P, had the authority to approve such a task and that it is reasonably clear that he had the authority to issue task assignments.

Task issued within contract  
work scope and funding

Our examination of additional Navy documentation showed that the task identified in the cited documents was issued under a completion task-contract line on December 29, 1983. This task

was authorized with an estimated cost of \$550,000. Our analysis showed, and Navy officials agreed, that this issuance was outside the work scope of the contract line because it did not contain a completion task, work statement applicable to this type of work. According to the responsible Navy official, the issuance of this task was "an administrative error." The error was corrected by a telecon held on January 3, 1984 (5 days later).

Our review of information related to this telecon confirmed that the task issuance was modified at that time to apply to an appropriate contract line. This contract line contained a work statement that was applicable to the task issued in error. Moreover, we determined that appropriate fiscal year funding was available for the task at the time of the January 3, 1984, telecon.

#### Authority to approve tasks

The task in question was issued under Naval Sea System Command contract N00024-78-C-2507. A memorandum of understanding applicable to this contract states that clearance must be received from PMS 3960, PMS 396B, or PMS 396P before a direction is implemented that will change any existing task which causes a change in estimated costs or schedule. Thus, we believe PMS 396P had the authority to issue the task in question as a modification to an existing task.

Regarding approval of task packages, the governing Standard Operating Procedure (SOP) during the time frame of the task approval and issuance was PMS 396 SOP No. 5B, dated April 30, 1973. Specifically, it provided that task packages will be submitted to PMS 396P for processing and approval, and cited the Task Assignment Letter (TAL) and task statement among a list of enclosures as forms used in the packages. Further, the current Director, PMS 396P, stated that the processing and approval of task packages denotes that PMS 396P had the authority to issue tasks. This official cited the signature of PMS 396P on the task statement (within a section designated for PMS 396 signature) as further evidence that PMS 396P had the authority to issue tasks. The Data Manager also stated that the task statement can be considered the task "authorizing documents" and that this form is signed by PMS 396P.

In addition, the SOP dated July 7, 1971, which preceded SOP dated April 30, 1973, explicitly states that PMS 396P was one of three designated officials having signature authority for TALs and task modification. The SOP dated April 25, 1984, which superseded SOP dated April 30, 1973, lists the task statement and the TAL as forms to be included in a task assignment package.



## ELIMINATION OF A FINANCIAL MONITORING PROCEDURE

### Allegation

At the request of Electric Boat, PMS 396 eliminated Enclosure 3 "Reconciliation of Funding Source" from the Task Assignment Letter. The eliminated enclosure identified funds and work breakdown structures for each new task and Electric Boat had to agree to the enclosure. It is believed that the elimination of Enclosure 3 permits the contractor to oversee its own contract.

### GAO findings

We found that Enclosure 3 was eliminated. However, there are other mechanisms that allow the Navy to monitor tasking under the contract. The PMS 396P office utilizes a contract-required cost report to identify availability of funds and to monitor tasking. Moreover, the TAL in use identifies the cost of a task and the enclosure to the TAL (a task statement) identifies the work breakdown structure of a task.

### Enclosure 3

The TAL forwards a task to the contractor. The "Reconciliation of Funding Sources" (Enclosure 3) was the third enclosure to the TAL. Data elements of this enclosure covered (1) previously authorized work to be incorporated within current task modifications, (2) new authorizations of unassigned work under a specified contract, and (3) cumulative revised task statements. The sources and uses of funds for each of these categories are identified by manhours, materials, and total dollar values.

According to the former Director, PMS 396P, Enclosure 3 was discontinued during his tenure because it did not contain "real-time" data concerning money availability for tasking. The former Director stated that the enclosure did not allow for cost credits (cost underruns) or task cost debits (cost overruns).

### Cost report

The cost report, a requirement of the contract, is currently used to verify the availability of funds for tasking and to monitor tasking. Our analysis of this report showed that it contains data elements that would enable Navy monitoring of tasking. The cost report contains data that (1) identifies the appropriation source of funding, (2) identifies the type of tasking funded--level-of effort or completion tasks, (3) shows the total funds authorized within the contract modification (obligated dollars), (4) shows the total actual charges incurred to date (expenditures), (5) shows the total dollars used to fund

previously issued tasks, and (6) identifies the dollars available for future tasking.

### Task Assignment Letter

The TAL states that a task is being issued within the scope of the contract. Currently, the TAL states the cost of a task in manhours, material, and total dollar values. In addition, it identifies the contract line under which a task is authorized. An enclosure to the TAL, the task statement, identifies the work breakdown structure of the task that is to be performed.

### STANDARDS OF CONDUCT

#### Allegation

The former Director, PMS 396P in the Trident Project Office--Mr. James Salko--maintained a close contact with Mr. William Tassias, a representative of the Electric Boat Division, General Dynamics Corporation, the contractor on the Trident project, and purchased a boat from the representative. This transaction violated criminal statute 18 U.S.C. 201 and the Navy's Standards of Conduct 32 C.F.R. 721.5 (b), (c), and (d).

#### GAO findings

Based on the information we reviewed, Mr. Salko does not appear to have violated 18 U.S.C. 201 or any of the policies contained in the Navy's Standards of Conduct.

#### Salko's responsibilities

From May 1980 through July 1984, Mr. James Salko was employed as the Director, Plans, Programs and Financial Management (PMS 396P), in the Office of the Trident Submarine Acquisition Project Manager. The Director, PMS 396P, acted as the principle advisor to the Project Manager and the Deputy Manager on business/financial management matters. As such, the Director, PMS 396P, developed program plans and budgets, managed financial resources, and processed and approved task assignments under level-of-effort contracts. Our analysis indicates that major and substantive decisions on the development, design, and construction of the Trident submarines were made by the Project Manager.

#### Boat purchase

According to information obtained from the Navy, Mr. Salko purchased a used boat (sailing dinghy) in 1981, for between \$500 and \$600 from Mr. William Tassias, the representative of the Electric Boat Division, General Dynamics Corporation. In 1980 or 1981, Mr. Tassias advertised the boat for sale on the

Electric Boat Division bulletin board. At the time of the transaction, Mr. Salko was in charge of General Dynamics contracts and authorized, on a daily basis, work for the Navy by General Dynamics. Based on an inquiry at Washington, D.C., marinas, the price paid by Mr. Salko for the boat represented fair market value.

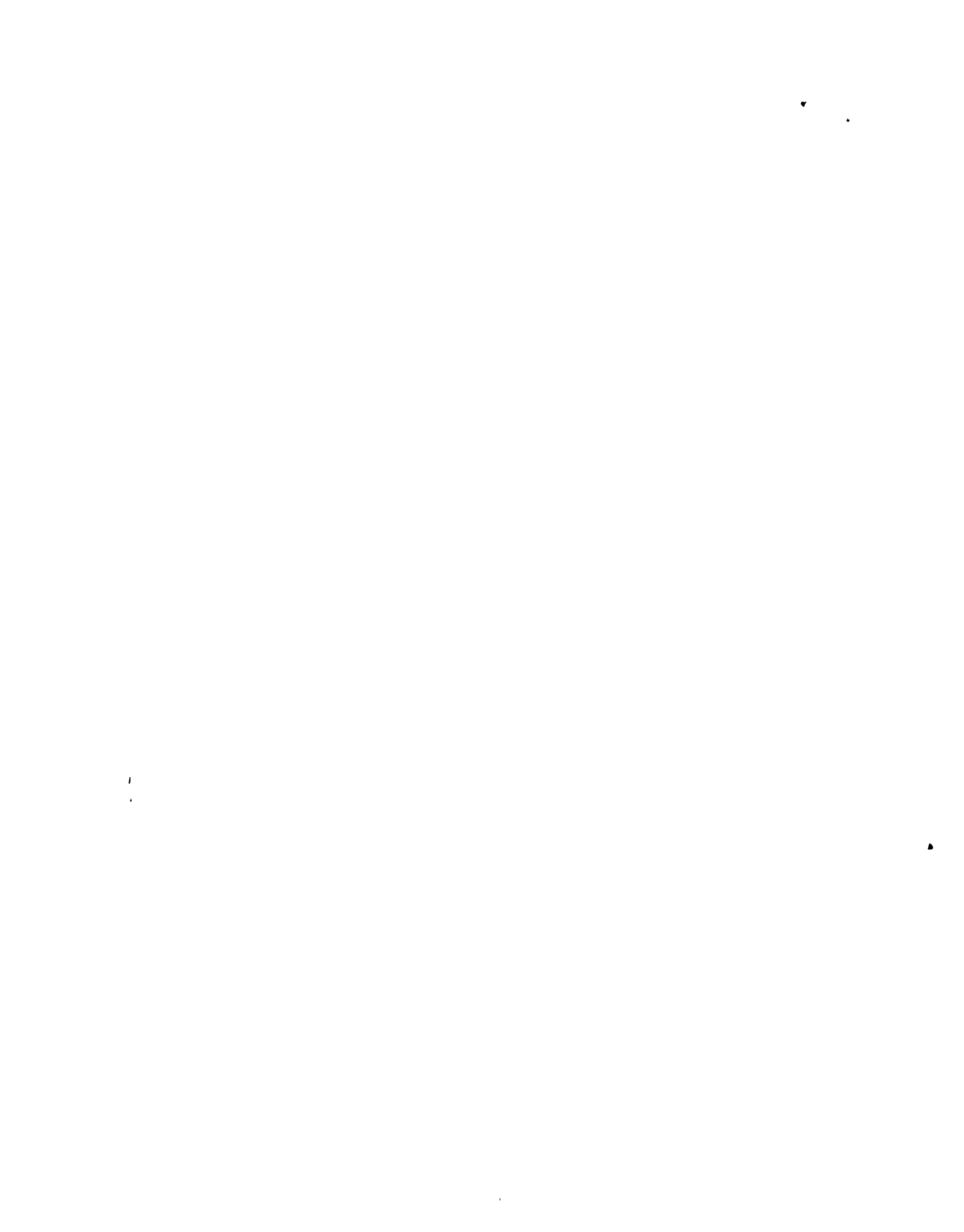
Applicable law and regulations allegedly violated

Mr. Kalmin charges that the transaction violated the federal antibribery statute, 18 U.S.C. 201, because Mr. Salko received something of value from Mr. Tassias. He also charges that the transaction violated several general policies in the Navy Standards of Conduct (32 C.F.R. 721.5 (b), (c), and (d)) and that these violations require disciplinary action. Subsection 721.5(b) admonishes naval personnel to avoid any conduct that is, or may reasonably appear to be, prejudicial to the government. Subsection 721.5(c) requires naval personnel to exercise sound personal judgment and subsection 721.5(d) requires that they avoid any conflicts of interest or the appearance of such conflicts in their dealings with business and industry representatives.

Conflicts of interest may take place, or appear to take place, because naval personnel (1) accept gratuities (a benefit for which fair market value is not paid) or (2) engage in other activities that could affect the impartiality that must exist in the government's relation with business. Prohibited conflicts of interest and apparent conflicts may arise from personal relationships that naval personnel regard as inconsequential.

Although Mr. Salko received something of value (a boat) from Mr. Tassias, Mr. Salko paid a price that reflected the fair market value according to the Navy. Thus, such a transaction does not appear to violate 18 U.S.C. 201 or to be in conflict with the policies set forth in subsections 721.5(b) and (c). In addition, the transaction does not appear to have violated subsection 721.5 (d) because (1) the purchase of the boat was not a "gratuity" and (2) this activity could not reasonably be expected to influence or appear to influence his impartiality.

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General Accounting Office  
Washington, D.C. 20548

Official Business  
Penalty for Private Use \$300

Address Correction Requested

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First-Class Mail Postage & Fees Paid GAO Permit No. G100
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