GAO

United States General Accounting Office

Report to the Chairwoman, Government Activities and Transportation Subcommittee, Committee on Government Operations, House of Representatives

May 1992

GENERAL SERVICES ADMINISTRATION

Distribution Center Modernization Was Mismanaged

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GAO/GGD-92-71

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United States
General Accounting Office
Washington, D.C. 20548

General Government Division

B-247719

May 20, 1992

The Honorable Barbara Boxer
Chairwoman, Government Activities
and Transportation Subcommittee
Committee on Government Operations
House of Representatives

Dear Madam Chairwoman:

This report responds to your request that we examine the General Services Administration's (GSA) efforts to automate and modernize its wholesale supply distribution centers. The Subcommittee was concerned that taxpayer dollars may have been wasted in the modernization of GSA's distribution centers at Palmetto, Georgia, and Burlington, New Jersey.

Results in Brief

GSA has mismanaged its modernization efforts, wasted millions of dollars, and has not, and will not, fully realize the intended benefits of modernization unless critically needed software to automate its distribution centers is developed. GSA has already spent more than $3 million and may spend millions more on its unsuccessful attempt to develop this software, an effort that failed largely because of an inadequate needs assessment and ineffective project oversight. In February 1991, GSA began a second software development project with an estimated completion date of 1995. Although this project is an in-house initiative and seems better planned and managed, GSA had no plans to survey the software market to determine if better alternatives exist to meet its needs. As a result, GSA has no assurance that the time and money it will spend on this project will be cost effective.

GSA also incurred millions in unnecessary costs in acquiring and moving into the Palmetto facility, primarily because of poor planning. First, GSA overestimated its space needs, an error that could cost the government about $9 million over the life of the lease. Second, GSA did not include modernization specifications in the lease solicitation process, but within 12 days after the lease was awarded, GSA began negotiating about $12 million of building modifications with the lessor to reflect modernization. These new modernization requirements were negotiated without the benefit of competition. Third, GSA poorly designed and managed its move to Palmetto from its former facility, which cost an extra $1 million in labor. Finally, the Palmetto lease contains overtime and railcar usage provisions that do not protect the financial interest of the government and, as a result, may increase the cost of the lease by as much as $5 million.

GSA seemed to learn from the Palmetto experience because its acquisition of the second modernized distribution center at Burlington, New Jersey, was better. However, the Burlington center, like Palmetto, cannot fully achieve the modernization benefits until the needed software is successfully developed.

Background

GSA's Federal Supply Service (FSS) maintains a worldwide supply, warehousing, and distribution system to receive, store, and issue products and supplies to federal agencies. GSA operates 5 distribution centers that stock about 18,000 commonly used and commercially available products, such as tools, ladders, paints, pens, batteries, and photocopy paper. In fiscal year 1991, GSA spent about $136 million to operate these distribution centers. GSA recouped its operating costs by adding a markup cost to the products' sale prices. In fiscal year 1991, GSA had a year-end inventory of about $242 million and generated about $1 billion in sales to federal agencies.

In 1986, GSA began efforts to automate and modernize its distribution centers to provide for more efficient operations, increase productivity, and reduce costs. These efforts were based on an approach using material handling equipment along with an automated data processing (ADP) system to improve facility operations and inventory management. State-of-the-art material handling equipment to be used included racks and bins linked with conveyors suspended from the ceiling and towveyors (cart-like vehicles) that travel along preset tracks in the floor. This equipment was to be arranged to allow products to "flow through" the facility. For example, products would be received at a central location at one end of the facility and then rerouted for storage in the facility. As orders were filled, the products would travel, via the towveyors and conveyors, to the outbound shipment area. In essence, products would enter at one end of the facility and leave from the other end.

The proposed ADP system was to (1) monitor the flow of all products in the facility from the time they were received until they were shipped out, (2) generate necessary reports and documentation, and (3) interface with the existing GSA host computer system. Also, the new ADP system was expected to improve many of the deficiencies in the current system. For example, under the current system, a product's location and other data are manually entered into the database and, as a result, are prone to error. The new system would use computer-assigned, dated codes to create storage location information and to maintain first-in/first-out control in order to move the oldest stock out first. The replenishment of products under the current system depends on manually distributed and checked tickets, but the new system would automatically produce a replenishment order when the minimum replenishment point was reached. Replenishment orders would be in priority sequence so that immediate attention would be given those items requiring quick replenishment. Additionally, the inventory surveillance function under the current system is cumbersome, batch oriented, and often incomplete. The new system would allow inventory control specialists to continually verify actual on-hand quantities of all items.

GSA's first modernized distribution center, a 1.3-million-square-foot facility, opened in March 1989 in Palmetto, Georgia. This facility was to be the prototype for modernizing the remaining distribution centers. In January 1991, GSA opened its second modernized distribution center, a 1.1-million-square-foot facility, in Burlington, New Jersey. GSA is currently seeking approval from the Office of Management and Budget to modernize the distribution facility in Fort Worth, Texas.

Objectives, Scope, and Methodology

Our objectives were to examine (1) various suspected problems in GSA's development of the ADP system that is critical to fully achieving modernization benefits and (2) potentially questionable management decisions and procurement practices in the acquisition of the first modernized distribution center in Palmetto, Georgia. To accomplish our objectives, we did work at GSA's central office, two regional offices in Atlanta and Philadelphia, and at the Palmetto and Burlington distribution centers.

To meet our first objective, we reviewed and analyzed various information and documents on GSA's distribution center modernization effort and expected benefits, and the material handling equipment and ADP system contract and related documents. We interviewed responsible GSA officials about the ADP software procurement and modification efforts, including their current plans to develop the needed ADP system. We also interviewed the directors of the distribution centers about operational problems caused by the missing ADP software.

To meet the second objective, we reviewed and analyzed GSA procurement policies and procedures and the leases for the Palmetto and Burlington distribution centers. We interviewed officials responsible for awarding the leases and making acquisition decisions. We discussed the new distribution centers' design concept with regional officials as well as the processes for planning the moves from the former facilities into the new ones. We also contacted officials from GSA's Office of Inspector General and Regional Management Acquisition Staff to obtain copies of their reviews of the leases and supplemental lease agreements for the new facilities. In addition, we reviewed and analyzed Inspector General audit reports on the Palmetto distribution center. We did our work from March 1991 to January 1992 in accordance with generally accepted government auditing standards.

Automation: Ineffective and Costly Software Development Efforts

GSA's efforts to modernize and automate its distribution centers have been costly and are not yet complete. In September 1988, GSA awarded a contract for both the material handling equipment and the ADP system, including software development, for $13.4 million. However, after working about 2-1/2 years and spending more than $3 million, the contractor was unable to develop the software necessary to automate the distribution centers. In February 1991, GSA terminated the computer software portion of the contract. GSA is in the process of settling the contract, which could increase the government's cost well beyond the $3 million already spent. Further, without the software, the $539,000 of associated ADP hardware already purchased cannot be used as planned and, more importantly, the modernization of the distribution centers cannot be fully achieved. According to FSS officials, the ADP software development efforts were unsuccessful because (1) an adequate needs assessment was not done and (2) the project lacked effective oversight.

Inadequate Needs Assessment

An adequate needs assessment is critical to successfully developing and acquiring ADP software. A comprehensive needs assessment identifies all functions that the ADP system must be able to do and clearly and accurately defines information requirements based on the users' needs in relation to the agency's mission, strategic objectives, and long-term ADP plans. FSS' ADP system project managers told us that they did not have time to do an adequate needs assessment because former top GSA officials pressured them to have the system ready when the Palmetto distribution center was expected to open in April 1989. Instead, they developed a general needs assessment with broadly defined functions, and they hoped that, with minor modifications, a readily available commercial software package would meet their needs. GSA awarded a contract that reflected these general needs and broadly defined functional requirements.

This approach did not work. Shortly after the contract was awarded, serious questions arose between FSS and the contractor about the nature of the ADP products, such as computer programs and documentation, that the contractor was to deliver. Due dates were missed, misunderstandings between GSA and the contractor occurred, and the contractor was unable to develop a software package to satisfy GSA's needs. In February 1991, GSA partially terminated the contract for the convenience of the government.

Ineffective Oversight

Compounding the software development problem was the minimal oversight given the project by the former GSA Administrator and the FSS Commissioner and the lack of involvement by GSA's Information Resources Management Service (IRMS). According to FSS program managers, although both the Administrator and the FSS Commissioner approved the project and were informed of problems, their involvement was neither continuous nor supportive. For example, they met with project managers only once a year on this project and, according to the FSS project director, when problems surfaced regarding the timely completion of the contract, the guidance from top management was simply "to proceed." The IRMS supervisory computer systems analyst who later participated in evaluating the software contract said that top management attention was not given to this project because of higher priority projects, including building the distribution center and developing a larger ADP project for another GSA component.

An information technology acquisition model we developed through consultation with government and private industry procurement experts identifies several critical factors for ensuring successful ADP projects.[1] According to this model, one of the critical factors is initial and continuing support by top management.

In addition to the minimal involvement by top GSA officials, IRMS, which is the unit responsible for directing and coordinating governmentwide programs for the management, acquisition, and use of ADP systems, was not involved in this project initially. Since the ADP costs were expected to be a relatively small part of the total acquisition cost, FSS and IRMS officials

[1] Information Technology: A Model to Help Managers Decrease Acquisition Risks (GAO/IMTEC 8.1.6, Aug. 1990).

agreed that FSS would have sole responsibility for the project. However, the actual costs for the system greatly increased, and when the contract was signed in September 1988, roughly half of the $13.4 million total contract price was for the computer hardware and software and the remaining half was for the material handling equipment.

New Software Development Efforts Underway

Beginning in February 1991, GSA initiated an in-house effort to develop the needed ADP software, and this effort seems better planned and managed. GSA has made improvements that should result in a better needs assessment. For example, to better define the needs and help establish system requirements, GSA has involved system users in project reviews and in validating system requirements. In addition, oversight of the project has improved significantly because the FSS Commissioner and other managers now meet regularly with the project director to discuss problems and reach decisions. Further, IRMS has been working closely with FSS staff on the project to ensure that appropriate mechanisms are in place and procedures are followed. GSA estimates the cost of this project at about $8 million and expects it to be completed in 1995.

In spite of these improvements, we have some concerns. GSA had no plans to identify or compare a range of alternatives for developing this software to meet requirements once the system is designed. The Federal Information Resources Management Regulation (41 C.F.R. ch. 201) requires that agencies assess alternative means of meeting their ADP needs and calculate the cost and benefits of each alternative when the cost of the project exceeds $50,000. GSA's guide for federal agencies also points out that market research is an effective way to (1) determine cost information and the availability of technology and (2) assist in identifying feasible alternatives.[2] Nevertheless, according to the project director, GSA did not plan to identify various alternatives to its in-house approach because prior efforts using contractors were unsuccessful.

GSA's project director said that GSA did not plan to identify alternatives for this project because it did a market survey in 1987 as part of the earlier software development effort, and from that experience GSA believes that commercially available software packages would not meet its needs. However, more than 4 years have passed since that study was done, and without a current and complete identification and analysis of available alternatives, GSA has no assurance that the time and money it will spend on this project is cost effective. More importantly, GSA has emphasized to

[2] A Guide for Requirements Analysis and Analysis of Alternatives (GSA IRMS, Jan. 1990).

federal agencies the importance of a market survey that includes both industry and government sources as the cornerstone of any alternatives analysis and being even more so for commercial software because the pace of change is so fast.[3]

In commenting on a draft of this report, GSA agreed with our observation and said that it has recently started doing a market survey to consider alternatives. However, we have not evaluated the adequacy of this recent effort.

Acquisition of the New Distribution Centers: the First Had Problems, but the Second Did Not

GSA's acquisition of and move to its first modernized distribution center at Palmetto, Georgia, was poorly done. As a result, GSA will pay millions in unnecessary costs. GSA appears to have learned from its mistakes at Palmetto, because it did not encounter similar problems in the acquisition of its second center in Burlington, New Jersey.

Several fundamental aspects associated with acquiring and moving to the Palmetto center were poorly planned. First, GSA overestimated its space needs, which could cost the government millions over the life of the lease. Second, GSA did not include modernization specifications in the lease solicitation process, but within 12 days after the lease was awarded, GSA began negotiating about $12 million of building modifications with the lessor to reflect modernization. These new modernization requirements were negotiated without the benefit of competition. Third, GSA poorly designed and managed its move from the former facility at Duluth, Georgia, to the Palmetto center which cost an additional $1 million in labor. Further, the Palmetto lease contains overtime and railcar usage provisions that do not protect the financial interest of the government and, as a result, may increase the cost of the lease by as much as $5 million.

Space Requirements Overestimated

GSA overestimated the space needs at the Palmetto distribution center by 131,000 square feet, and this mistake could cost about $9 million over the life of the lease.[4] The space in question is comprised of 85,000 square feet intended for the National Archives and Records Administration (NARA) and 46,000 square feet intended for GSA's Customer Supply Center (CSC).

[3] A Guide for Acquiring Commercial Software (GSA IRMS, Jan. 1991).

[4] We calculated the $9 million cost for the 131,000 square feet by using the lease rates that were in effect for the first 1-1/2 years and the current rate for the remaining 18-1/2 years of the 20-year lease period.

Even though GSA leased space for NARA in the Palmetto facility, NARA did not move, because a study GSA prepared after the lease was awarded determined that such a move was too expensive. According to GSA officials, 63,000 of the 85,000 square feet set aside for NARA has been absorbed into general warehouse operations, but they could not specifically identify how it is being used. GSA officials said the remaining 22,000 square feet is being used for a number of miscellaneous programs. The major reason GSA overestimated the space requirements is that it did not follow its regulations that require completing a cost-benefit analysis, when relocation plans are being considered, to determine if it is in the government's best interest to relocate. GSA regional officials responsible for the lease could not explain why this analysis was not done.

The CSC did move into the Palmetto facility, but after 13 months it was consolidated into warehouse operations. As a result of the consolidation, CSC operations use only about 5,000 of the 46,000 square feet of space they were originally allocated. The remaining 41,000 square feet will have to be absorbed into general warehouse use. GSA had considered consolidating the CSCs into warehouse operations before the lease solicitation was issued. A 1986 study recommended this consolidation to reduce costs and improve operational efficiency.[5] However, a GSA regional official said that the former FSS Commissioner delayed this consolidation because he could not get all GSA regions to agree.

Modernization Requirements Not Included in Lease Solicitation

Although specific facility requirements were needed for GSA to achieve its modernization objectives, these requirements were not included in the lease solicitation process. As a result, GSA had to negotiate supplemental lease agreements for building modifications with the lessor after the contract was awarded, which added about $12 million to the cost of the original lease. Because these changes were added after the original lease was awarded, they were not subject to full and open competition. While it is not possible to determine how much these changes would have cost if they had been included in the original lease solicitation process, procurement procedures endorse full and open competition as the best means for getting the best price.

Although GSA initiated studies and began planning to modernize its wholesale distribution centers as early as 1985, GSA officials said that these requirements were not included in the solicitation process because they

[5]Distribution Strategy—Federal Supply Service, United States General Services Administration, Insight Incorporated (Dec. 18, 1986).

did not know the extent of the modernization requirements then. However, just 12 days after the lease was awarded, GSA officials initiated the first of 12 supplemental lease agreements to incorporate the modernization requirements. In total, these supplemental agreements increased GSA's leasing costs by about $12 million. For example, one supplemental lease agreement, for about $8 million, called for several alterations, such as changing the ceiling height, installing exterior overhead doors and duct work to improve ventilation, and insulating the roof. Included in this $12 million is $1.8 million that GSA paid in cash for some of these changes. (App. I lists the nature and cost of these 12 supplemental lease agreements.)

Poorly Planned Move

GSA's move into the Palmetto facility was poorly planned and cost the government over $1 million in additional labor costs and an undetermined number of damaged products. One of the significant problems with the move was that GSA officials did not prepare a master move plan. A master move plan establishes dates when shipments into the former facility should stop and designates specific storage locations for products received at the new facility. According to GSA regional officials, the plan was not prepared because the lease at the former facility was about to expire and headquarters management was adamant about not extending the lease.

GSA regional officials said that headquarters' reluctance to extend the lease centered on a potential conflict of interest. The former FSS Commissioner told us that a GSA regional real estate official had the opportunity to buy the former facility but decided not to. Later, this regional official went to work for the lessor of the facility and could have been in a position to influence the prices GSA would have to pay to renew the lease. It is interesting to note, however, that although GSA officials expressed this concern and did not extend the lease for distribution center operations, GSA did negotiate a 10-year lease for NARA at the facility.

Because of its reluctance to extend the lease at the former distribution center, GSA moved into the Palmetto facility before construction was completed. For example, GSA moved products into Palmetto before the roof was completed, and an undetermined number of products were damaged as a result of rain falling through the unfinished roof. Furthermore, the move into the center was so hurried that products were randomly unloaded throughout the warehouse, leaving it in chaos. It took more than 15 months and $1 million of additional labor costs to reorganize the warehouse so products could be located and shipped. GSA headquarters and regional officials as well as distribution center directors agreed that the move to Palmetto was costly, chaotic, poorly designed, and mismanaged.

Lease Provisions Do Not Protect the Government

The Palmetto lease contains provisions on overtime use of the facility and railcar usage that do not protect the financial interest of the government. GSA did not include an overtime pay rate in the lease and allowed a lease provision to be included that was based on erroneous railcar usage information. GSA initially anticipated that only limited overtime use of the facility would be required and the cost of the lease reflected this limited use. However, GSA was wrong and required overtime increased. Because GSA did not specify an overtime rate in the lease, there is a disagreement on the hourly rate. The lessor billed GSA for nearly 2,800 hours at $400 per hour for overtime costs through November 1990. GSA disagreed with this rate and offered to pay the lessor $75 per hour for overtime charges. GSA now estimates that there will be at least 2.5 hours of overtime usage at the Palmetto facility each day. Over the 20-year lease period, if the $75-per-hour rate is accepted, GSA will pay $975,000, but if the $400-per-hour rate prevails, GSA will pay about $5 million. GSA officials told us that they expect the lessor to take this matter to the Board of Contract Appeals to be resolved.

According to GSA regional officials, the lease provision that deals with railcar usage is based on erroneous information. The lease provision requires that the lessor provide rail service and states that usage will be two to three railcars per day. Actual usage, however, may be as low as three railcars per month. GSA regional officials responsible for this lease could not explain how or why the erroneous data were used as a basis for the lease provision. If actual usage is only three railcars per month, then GSA may have to reimburse the lessor $60,000 for expenses incurred because the lessor used GSA's erroneous information as the basis for entering into an agreement with a rail company.

Burlington Acquisition and Move Were Better Planned

GSA's acquisition of the Burlington distribution center was better. GSA did not repeat the problems associated with the Palmetto center. Local management's attention to good planning allowed GSA to more accurately determine the size and design of the facility as well as how and when products would be moved into it. Also, the provisions in the lease for the

Burlington facility for overtime and railcar usage better protect the government's interest.

One of the most dramatic improvements in the Burlington acquisition process was the planning devoted to the move into the facility. The move plan covered a 9-month period so that the number of products at the former facility would be reduced while new product shipments were received only at the new facility. As a result, orders were filled from the former facility, reducing the number of items needing to be moved to the new facility. Also, the move plan identified storage places for inventory, which allowed items to be placed in designated storage areas upon receipt. The Burlington center was fully operational by September 1991 as planned.

Unlike the Palmetto situation, the Burlington lease contained provisions to protect the financial interest of the government. The Burlington lease clearly specified overtime rates depending on the level of building use needed. For example, to keep the building open for administrative or other support functions, the overtime rate is $60 per hour, but the rate is $172 per hour if the material handling equipment is operated. As for railcar provisions, the Burlington lease requires that the lessor provide railcar services but does not specify a usage rate. Furthermore, during its first year of operation, the management of the distribution center did not identify any deficiencies at this center as they did at Palmetto.

Conclusions

GSA has not effectively managed the modernization of its wholesale distribution centers. Its efforts to develop software that is central to the modernization have failed, and millions of dollars have been wasted. While GSA believes it can develop the needed software in-house, the estimated completion date is still over 3 years away, and there is no assurance that the time and money it will spend will be cost effective. Until the software is developed and installed, GSA will not fully achieve the benefits envisioned from its modernized distribution centers. It is also questionable whether GSA should modernize another center before the software is developed, tested, and implemented.

In addition, GSA incurred millions of dollars in unnecessary costs in acquiring and moving to the Palmetto distribution center because of poor planning. Although GSA's poor acquisition planning for the Palmetto distribution center resulted in millions of dollars of unnecessary costs, the planning for its second center in Burlington improved, and GSA avoided the unnecessary costs associated with the Palmetto problems. In large part, the Burlington acquisition planning was better because of local management's attention to following established procedures.

Recommendations

We recommend that the Administrator, GSA, survey the software market, including both private and government sources, after completing the design of the ADP system, to identify the best alternative for meeting software needs. We also recommend that before modernizing any other distribution center, the Administrator, GSA, ensure that existing procedures are effectively implemented to

- develop, test, and implement the critically needed software;
- complete a cost-benefit analysis when relocation plans are being considered;
- incorporate modernization design factors in original lease solicitations to allow full and open competition;
- prepare and follow move plans; and
- include provisions on overtime and railcar usage in leases that adequately protect the financial interests of the government.

Agency Comments and Our Evaluation

In commenting on a draft of this report, GSA generally agreed with our findings and recommendations. (See app. II.) GSA also provided additional information that (1) further explained why the modernization problems occurred and (2) discussed various actions it plans to take to implement our recommendations. The actions outlined by GSA appear to address our concerns, but, as GSA recognized, continued oversight will be needed to help ensure that these recommendations are effectively implemented.

GSA's comments regarding overestimated space requirements at Palmetto merit further discussion because they do not fully discuss this issue. GSA said that 88,000 square feet were intended for NARA, 40,000 of which were allocated to the CSC after NARA decided not to move. Our data show that this is not correct. Our analysis showed that GSA leased 46,000 square feet for the CSC and that this space did not come from NARA's allocation. As discussed in the report, GSA actually leased 131,000 square feet—85,000 square feet for NARA and a separate 46,000 square feet for the CSC.

Additionally, GSA's comments indicated that it will construct a new automated Southwest Distribution Center at Fort Worth before the critically needed software is developed and tested. GSA said that savings in productivity and transportation costs will result from the improved physical layout of the facility irrespective of the availability of a completed software package. While this may be true, these savings may be more than offset by costs incurred to construct a new facility designed for automation if the ADP system does not work. Until the software is available, we question the wisdom of constructing another automated facility.

As agreed with the Subcommittee, we plan no further distribution of this report until 20 days after the date of issuance, unless you publicly announce its contents earlier. At that time, we will send copies to the Administrator of GSA, the Director of the Office of Management and Budget, and other interested parties. We will also make copies available upon request.

If you have any questions or would like further information, please contact me on (202) 275-8676. The major contributors to this report are listed in appendix III.

Sincerely yours,

L. Nye Stevens

L. Nye Stevens
Director, Government Business
Operations Issues

List of 12 Supplemental Lease Agreements Required by Modernization

Date	Description	Cash paid at time of change	Amount to be amortized over lease term
10/27/87	Altered ceiling height and other changes to incorporate modernization needs.	[a]	[a]
11/19/87	Alterations—Ceiling height, exterior overhead doors, roof, insulation, ventilation.		$8,361,540
1/29/88	Alterations—Roof loading requirements.	$661,455	251,400
6/20/88	Alterations—Firewall penetrations and associated fire safety criteria.	66,833	45,400
1/6/89	Alterations—In-rack sprinklers and associated fire safety criteria.	391,540	262,520
1/6/89	Additional 1,300 square feet to accommodate computer room.	267,764	129,780
6/14/89	Installation of four air conditioning units.	38,130	
4/21/89	Alterations—Install temporary electrical power for material handling equipment.	55,968	
4/21/89	Alterations—Install permanent electrical power for material handling equipment.	207,510	
11/8/89	Installation of a new 2500 KVA transformer.	76,172	
9/5/89	Alterations—Towveyor upgrade.	74,294	650,660
9/1/89	Install additional lighting in third level mezzanines for the operation of the material handling system.	44,217	
Total		**$1,883,883**	**$9,701,300**
Total both columns		**$11,585,183**	

[a]The costs for these changes were actually in the supplemental lease agreement dated Nov. 19, 1987.

Source: GSA lease file.

Comments From the General Services Administration

Administrator
General Services Administration
Washington, DC 20405

April 6, 1992

The Honorable Charles A. Bowsher
Comptroller General
of the United States
General Accounting Office
Washington, DC 20548

Dear Mr. Bowsher:

Thank you for the opportunity to comment on the General Accounting Office (GAO) draft audit report entitled "GENERAL SERVICES ADMINISTRATION: Distribution Center Modernization Was Mismanaged." We believe that when examined as a whole GSA's efforts to consolidate and modernize its distribution operations have achieved notable results. These results include well functioning operational depots at Burlington and Palmetto with Burlington having been brought on line essentially devoid of the problems experienced at Palmetto.

In response to a prior GAO report (Consolidation of GSA's Depot Function Can Save Millions in Space Costs and Improve the Use of Depot Resources (GAO/PLRD 82-109 dated August 16, 1982)), GSA's efforts to consolidate its distribution facilities have reduced our warehousing space by 7.3 million square feet. In addition, approximately 70 self-service stores were phased out and replaced by catalog ordering operations. In total these actions have resulted in the reduction of 490 employees.

The events surrounding the Duluth to Palmetto relocation and modernization occurred, in part, because of significant differences of opinion between former GSA Administrator Terrence Golden and the Federal Supply Service (FSS). Among these differences were the type of facility to be acquired, i.e., size and shape, the timing and management control over the move from Duluth to Palmetto and the length of time needed to properly transition to a totally different operating system, namely the so called Keogh Plan.

On October 8, 1987, Administrator Golden was briefed by James R. Keogh and Associates (Keogh and Associates) in Fort Worth, Texas, regarding a proposed design considered for the Southwest Distribution Center. While FSS had not totally embraced the concept put forth by Keogh and Associates and felt the proposal needed additional review, GSA Administrator Golden directed its adoption and incorporation into the replacement facility being

Federal Recycling Program Printed on Recycled Paper sought for the southeast region. The then Commissioner of FSS, Mr. Donald C. J. Gray, was dispatched to Atlanta from Fort Worth subsequent to the Administrator's briefing for the purpose of incorporating the Keogh design into the Southeast Distribution Center requirements. Additionally, FSS wanted to develop the depot automation enhancements to its FSS-19 automated logistics system in-house. This approach was rejected in favor of a contracting-out alternative.

On November 17, 1987, at the direction of Administrator Golden, Commissioner Gray submitted a proposal to: (1) abolish the Distribution Management Division in FSS Headquarters in Crystal City, Virginia, (2) establish a new Office of National Distribution Management in Atlanta, Georgia, and (3) transfer management and operations of all FSS distribution facilities from the Regional Administrators in the various regions containing distribution centers to the new Atlanta office. GSA Order ADM 5440.374 dated December 10, 1987, implemented this direction. The former Regional Administrator of Region 4, Atlanta, Georgia, was put in charge of the new Atlanta office and given the responsibility for FSS modernization efforts in a memorandum from Administrator Golden dated December 4, 1987.

As the Regional Administrator in Region 5, I was aware of these events, and generally did not support them, especially the relocation of the distribution management function to Atlanta. After becoming Acting Administrator, I returned the day-to-day management of the supply distribution centers to the Regional Administrators on December 6, 1988 (GSA Order OHR P 5440.1 CHGE 227). After my confirmation as Administrator, I also reversed the order which established the Office of National Distribution Management in Atlanta and relocated the office to FSS Headquarters in Arlington (Crystal City), Virginia (OHR P 5440.1 CHGE 292, dated November 13, 1990). The Atlanta-based Assistant Commissioner for National Distribution Management and the Assistant Regional Administrator for FSS in Atlanta retired, and the management of the Palmetto Wholesale Distribution Center was replaced.

In January 1989, I approved the transfer of the contract administration of the ADP contract for Palmetto to the Information Resources Management Service (IRMS) because I believed IRMS experience with software procurements would be helpful in addressing certain of the contract administration problems the agency was encountering with the contract.

Unfortunately, despite the best efforts on behalf of all involved in both IRMS and FSS, it became apparent that continuation of the software contract was not in the best interest of the Government and the contract was terminated on February 12, 1991. This decision did not come easily. It was the unanimous view of FSS and IRMS that the extent of the redesign and modification of the "Cullinet" commercial software package had exceeded reasonably acceptable levels and further changes yet required would result in a complex, hybrid product, difficult and costly to maintain, if completed.

See pp. 4, 5, and 8.

It is not clear to whom the comments in the draft report refer in alleging the lack of top GSA management support. However, we clarified with GAO officials that these comments were applicable to the former Administrator and former FSS Commissioner. My own oversight, review and support of this effort has been continuous, significant, and detailed. Updates are included regularly in quarterly Management Council meetings, General Management Reviews and Board of Directors meetings. The Commissioner of FSS regularly provides status reviews to either the Deputy Administrator or myself. This management attention has been steady and will continue.

We agree that the problems created by the decision to vacate the Duluth depot before completion of the new facility, as well as the poor execution of the move plan, resulted in excess labor costs. The lease was expiring at Duluth and a decision was made not to extend the lease arrangement with the lessor, therefore forcing the move to Palmetto even though the building was not complete.

We are aware that the original solicitation for the Palmetto facility did not include a requirement for overtime as a bid line item. Thus, overtime was not initially included in the Palmetto lease as was the case in Burlington. GSA is attempting to arrive at a fair and reasonable maximum hourly rate for overtime with the lessor using audit information and comparisons to the non-MHE (Material Handling Equipment) rate at Burlington.

Also, it is GSA's position that we are paying for the rail siding as a part of the rent, since it was part of the solicitation. The solicitation required rail access to the facility and the lessor provided that service via a side-track agreement between the building owner and the railroad. We take the position that we are not obligated to reimburse the building owner for any shortfalls in railcar refunds from the railroad.

Overall, considering Palmetto has an 11 hour/day lease versus Burlington's 10 hour/day coverage and other differences such as a two-tiered overtime rate for lessor-owned MHE, we believe the overtime cost of the leases at Burlington and Palmetto will be roughly equivalent.

Essentially, the lease rate for Palmetto is not excessive for this type of facility. Factoring in the differences inherent in the respective leases, primarily the inclusion of the cost of MHE and its maintenance in the Burlington lease, Palmetto's costs per square foot are approximately 60 percent of the Burlington costs.

See p. 12.

Regarding statements concerning overestimated space requirements, an integrated wholesale distribution center/customer supply center (CSC) operation was included in the Southeast Distribution Center plan developed by Keogh & Associates. The National Archives Records Administration (NARA) space in question was planned at 48,000 square feet in the Keogh Plan. Further, GSA Inspector General Report No. A80188/P/4/R88076, dated March 18, 1988, identifies 40,000 square feet of additional space for NARA under supplemental Lease Agreement No. 1. After NARA decided not to relocate, FSS did determine that the 40,000 square feet of space would be used for the Atlanta Customer Supply Center. The GSA IG Report also attributed the NARA withdrawal from the lease as due to lack of NARA funding and indicates confirmation of this by the NARA Director. FSS was not ready to integrate the CSC into the wholesale warehouse at that time and it remained a separate entity until integrated in July 1990.

The former CSC space has been used for hazardous material packaging to comply with the regulation to perform Performance Oriented Packaging; a requirement not anticipated in 1987. In addition, FSS added several high volume, fast moving items to the stock system, including xerographic copier paper, due to opportunities available in the marketplace. The facility has also added a new program for the Navy to test a "Just-in-Time" program intended to reduce inventories and space at the Jacksonville Naval Supply Center. The availability of space from the CSC/wholesale merger facilitated these actions within existing depot space. With these additional programs, all available space at the Palmetto facility is being fully utilized.

In conclusion, we did learn from our initial experiences with depot modernization at Palmetto and have taken actions to improve our process as evidenced by the comments in your draft report concerning the Burlington Depot.

With respect to your recommendations, GSA proposes the following:

1. Survey the software market, including both private and Government sources, after completing the design of the ADP system, to identify the best alternative for meeting software needs.

   Our previous experience with an off-the-shelf commercially available software package demonstrated that the degree of modification required to adapt one to Government-unique requirements is cost and time prohibitive. We have therefore decided to develop the software in-house.

As your draft report points out, the in-house effort is well planned and managed. A major advantage to the in-house approach is that completed modules can be implemented in phases and we do not have to wait until total software completion to achieve benefits and efficiency. Over the next several months GSA will be implementing enhancements to existing software to produce greater efficiency in warehouse selection processes. We will also be programming and testing the first major automated module, "Receiving and Storage". These in-house designs are comparable to current industry practices for modernization of receiving and storage functions while meeting Government-specific requirements.

See p. 7.

Your recommendation that we consider alternatives and survey recently developed distribution software is already underway. The Depot Automation Project Team has reviewed several commercial software packages including the Navy's NISTARS system. We have reviewed these systems to search for alternative solutions to several of the proposed functions in conjunction with in-house efforts. We are particularly desirous of obtaining a commercial "Mechanization Control System" to control movement of conveyable cartons throughout the warehouse or, in the alternative, the use of a contractor to develop and implement this function. Where current FSS systems are adaptable for modification, we plan to develop the software in-house. It is our desire to allow FSS to continue its in-house efforts over the next several months as they begin to implement the automation systems rather than divert their attention in a totally new direction.

2. Before modernizing any other distribution center, the Administrator, GSA, ensure that existing procedures are effectively implemented to:

   Recommendation:

   o develop, test, and implement the critically needed software.

See pp. 12-13.

Comment:

GSA plans to develop, test, and implement the critically needed software beginning with:

-- redesign of shipment order consolidations within 30 days at Palmetto, and
-- programming and testing the "Receiving and Storage" module starting June 1, 1992.

As these modules are tested, debugged, and implemented, they will be installed at Palmetto, Burlington and, as appropriate, in Fort Worth and Stockton where existing facilities can accommodate automated functions.

Regarding the Southwest Distribution Center (Fort Worth, Texas) savings in productivity and transportation costs will result from the improved physical layout of the facility irrespective of the availability of a completed software package. Current projections indicate the majority of the automation package will be complete prior to completion of an upgraded facility.

Our Plans at the Western Distribution Center in Stockton, California, are largely dependent on our future status as a tenant of the Navy at Rough and Ready Island.

Recommendation:

o Complete a cost-benefit analysis when relocation plans are being considered.

Comment:

A cost-benefit analysis was developed for Fort Worth and basically shows that the savings from improved physical layout and freight consolidation offset the net annual increase in rental cost. This procedure will be followed when considering future moves.

Recommendation:

o Incorporate modernization design factors in original lease solicitations to allow full and open competition.

Comment:

As demonstrated and pointed out in your draft report, the Burlington project implemented this recommendation by incorporating modernization design factors. In the future, we will continue to incorporate modernization design factors in the original lease or Government-owned solicitation, to allow for full and open competition.

Recommendation:

o Prepare and follow move plans.

Comment:

We agree with the recommendation. Again, as demonstrated with the move from Belle Mead to Burlington, managed by the reestablished Office of Distribution Management in Crystal City, relocation plans were prepared and followed and similar controls will be applied in future moves.

Recommendation:

o Include provisions on overtime and railcar usage in leases that adequately protect the financial interests of the Government.

Comment:

We agree. This recommendation regarding overtime and railcar usage was addressed at the Burlington facility and will be implemented similarly in the future.

We appreciate the time and effort you and your staff have expended in developing this draft report. We look forward to working with you in the future.

Sincerely,

Richard G. Austin
Administrator

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