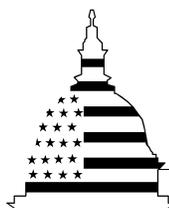


October 2002

INFORMATION
TECHNOLOGY

Issues Affecting Cost
Impact of Navy Marine
Corps Intranet Need to
Be Resolved



G A O

Accountability * Integrity * Reliability



Highlights of [GAO-03-33](#), a report to the Committee on Armed Services, United States Senate, and the Committee on Armed Services, House of Representatives

Why GAO Did This Study

Under the Navy Marine Corps Intranet (NMCI) contract, the Department of the Navy is obtaining information technology (IT) services that are to allow it to replace thousands of independent networks, applications, hardware, and software with one secure network. The National Defense Authorization Act of 2002 directed GAO to review the impact on IT costs of NMCI at Navy shipyards and air depots, which are predominantly working capital funded activities. Because this funding model requires these activities to recover all costs through charges to customers, GAO also reviewed NMCI's impact on shipyard and depot rates.

What GAO Recommends

GAO is recommending that the Navy establish a departmentwide means for systematically capturing and resolving NMCI implementation issues that affect the ability of shipyards and air depots to plan and budget.

The Department of Defense concurred with the report.

www.gao.gov/cgi-bin/getrpt?GAO-03-33.

To view the full report, including the scope and methodology, click on the link above. For more information, contact Randolph Hite, (202) 512-3439 (hiter@gao.gov), or Gregory Kutz, (202) 512-9095 (kutzg@gao.gov).

INFORMATION TECHNOLOGY

Issues Affecting Cost Impact of Navy Marine Corps Intranet Need to Be Resolved

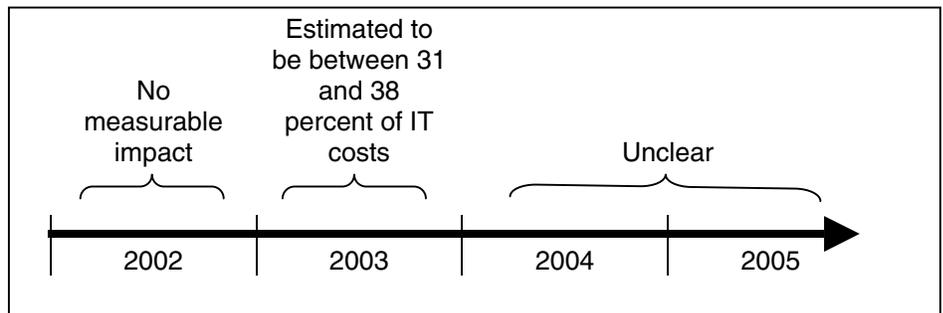
What GAO Found

To date, NMCI has not measurably affected either IT costs at shipyards and air depots or the rates they charge customers. This is because the network, while originally planned to be in place at these activities in fiscal year 2002, is now not to be implemented at them until the latter part of fiscal year 2003.

For fiscal year 2003, budget estimates show that NMCI will represent about 2 percent of total costs at shipyards and air depots. As a percentage of IT costs, NMCI costs will be more significant: about 38 percent at shipyards and 31 percent at air depots. According to shipyard and depot officials, estimated NMCI costs (which are a component of overhead costs) will not affect the rates charged to customers in fiscal year 2003 because they will be offset by cost reductions in other overhead areas, such as travel, training, and real property maintenance.

Beyond fiscal year 2003, the impact of NMCI on IT costs and rates is unclear, because several issues peculiar to shipyards and air depots are unresolved, such as how the costs of some transition items will be funded and whether these costs will be included in the rates. Also uncertain is when these issues will be resolved, because no specific plans for doing so exist, and no explicit issue management process has been established. As a result, the shipyards' and depots' ability to effectively plan and budget is being impaired.

Impact of NMCI on IT Costs at Shipyards and Air Depots



Source: GAO analysis based on data provided by the Department of the Navy.



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

October 31, 2002

The Honorable Carl Levin
Chairman
The Honorable John Warner
Ranking Minority Member
Committee on Armed Services
United States Senate

The Honorable Bob Stump
Chairman
The Honorable Ike Skelton
Ranking Minority Member
Committee on Armed Services
House of Representatives

The National Defense Authorization Act for fiscal year 2002 (Public Law 107-107) directed us to review the impact of the Navy Marine Corps Intranet (NMCI) program on the information technology (IT) costs of Navy working capital funded industrial facilities. As agreed with your offices, our work focused on naval shipyards and air depots that operate under the Navy's working capital fund. Because working capital funded facilities are required to set rates to recover all costs through charges to customers, our work also included NMCI's impact on rates.

NMCI is a multiyear program to outsource the vast majority of Navy and Marine Corps desktop, server, infrastructure, and communications asset and service needs. Through the NMCI services contract, the Navy plans to replace thousands of independent networks, applications, and other hardware and software with one secure network for all Navy and Marine Corps civilian and military personnel, including deployed forces. The Navy expects that significant benefits will accrue from NMCI over the life of the contract, including (1) an uninterrupted flow of information; (2) improvements to interoperability, security, information assurance, knowledge sharing, productivity, and operational performance; and (3) reduced costs. The Navy awarded the NMCI contract in October 2000 to Electronic Data Systems Corporation, for an estimated 412,000 to 416,000

workstations/seats¹ and an estimated minimum value of \$6.9 billion over 8 years.

On August 30 and September 6, 2002, we provided your offices a briefing on the results of this review, including our scope and methodology. This report transmits the briefing, which is reprinted as appendix I.

In summary, NMCI has not to date measurably affected either IT costs at shipyards and air depots or the rates they charge customers, because NMCI implementation at these facilities has slipped from fiscal year 2002 to the latter part of fiscal year 2003. However, shipyard and depot officials stated that NMCI transition activities during fiscal year 2002, such as site readiness and preparation, have had a minor effect on costs. We could not quantify their impact on IT costs because these costs were not separately identified.

For fiscal year 2003, budget estimates show that NMCI will make up about 2 percent of total shipyard and depot costs and about 38 and 31 percent of shipyard and depot IT costs, respectively. Shipyard and depot officials told us that these NMCI cost estimates, which are a component of overhead costs, will not affect the rates charged to customers in fiscal year 2003 because they plan to reduce budgeted costs in other overhead accounts, such as travel, training, and real property maintenance, to offset budgeted NMCI costs. However, if activities are not successful in implementing plans or in offsetting unexpected costs that may arise during the year, they could operate at a loss and thus be required to increase rates in subsequent fiscal years.

The impact of NMCI on IT costs and rates beyond fiscal year 2003 is unclear because, as we reported in our briefing, several issues peculiar to shipyards and depots were unresolved, such as how the costs of some transition items would be funded and whether these costs would be included in the rates. Moreover, NMCI implementation plans did not provide for resolving them because responsibility for doing so had not been clearly assigned and the Navy did not have an explicit issue identification and resolution process. This exacerbates the uncertainty surrounding NMCI's future impact on shipyard and depot costs and rates, and limits

¹Seat management generally refers to service provision arrangements in which contractor-owned desktop and other computing hardware, software, and related services are bundled and provided to a client (e.g., government agency) at a fixed price per unit (or seat).

these activities' ability to plan and budget. DOD subsequently told us these issues have been resolved, but did not provide supporting evidence and did not specify its process for issue identification and resolution and who is responsible for the process.

To ensure that existing and future issues are effectively and efficiently resolved, and thereby allow the shipyards and depots to make more informed planning and budgeting decisions, we recommend that the Secretary of Defense have the Secretary of the Navy direct the NMCI program manager, in collaboration with the Commanders of the Naval Sea Systems Command and the Naval Air Systems Command, to develop and execute an issue management process that resolves existing and future issues and includes

- participation by Navy shipyard and air depot officials,
- continuous identification of relevant and material NMCI implementation issues,
- shipyard and air depot implementation plans that include strategies for resolving these issues, and
- tracking of and reporting on issue resolution.

In response to a draft of this report, DOD provided what it termed "official oral comments" from the Acting Deputy Assistant Secretary of Defense for Command, Control, Communications, and Intelligence. In its comments DOD stated that it agreed with the report. DOD also provided updated information on the unresolved issues discussed in the briefing (app. I). We have incorporated the information as appropriate.

We are sending copies of this report to the Chairmen and Ranking Minority Members of other Senate and House committees and subcommittees that have jurisdiction and oversight responsibilities for the Departments of Defense and the Navy. We are also sending copies to the Secretary of Defense; the Secretary of the Navy; the Commandant of the Marine Corps; the Assistant Secretary of Defense for Command, Control, Communications, and Intelligence; and the Director of the Office of Management and Budget. Copies will also be available at no charge on our Web site at www.gao.gov.

Should you or your staff have any questions on matters discussed in this report, please contact Randolph Hite at (202) 512-3439 or Gregory Kutz at (202) 512-9095. They can also be reached by E-mail at hiter@gao.gov and kutzg@gao.gov. Key contributors to this report were Barbara Collier, William Hill, Greg Pugnetti, Ronnie Tobias, Carl Urie, and Robert Williams, Jr.



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Briefing Presented to Subcommittees



Impact of the Navy Marine Corps Intranet (NMCI) on Information Technology Costs at Naval Shipyards and Air Depots

Briefing for

Senate Armed Services Committee,
Subcommittee on Readiness and Management Support

and

House Armed Services Committee,
Subcommittee on Military Readiness

August 2002



Outline of Briefing

- Introduction
- Objective
- Scope and Methodology
- Results in Brief
- Background
- Results
 - Near-Term Impact on Costs
 - Near-Term Impact on Rates
 - Longer Term Impacts on Costs and Rates
- Conclusions
- Recommendations



Introduction

The Navy-Marine Corps Intranet (NMCI) is a departmentwide, multiyear information technology (IT) services contract to provide and manage the vast majority of Navy and Marine Corps desktop, server, infrastructure, and communications assets and services.

This type of contract is commonly referred to as “seat management” [1], because it involves a number of distinct workstations or “seats” that will be transitioned to a contractor (or contractors), who takes responsibility for operating and maintaining the workstations, including applications and supporting infrastructure, and for providing administrative and operations support, such as help desk support.

[1] Seat management generally refers to service provision arrangements in which contractor-owned desktop and other computing hardware, software, and related services are bundled and provided to a client (e.g., government agency) at a fixed price per unit (or seat). See our report, *Desktop Outsourcing: Positive Results Reported, but Analyses Could Be Strengthened*, GAO-02-329 (Mar. 23, 2002), for additional information on seat management contracts.



Introduction (cont'd)

NMCI is to replace thousands of independent networks, applications, and other hardware and software with one secure network for all Navy and Marine Corps civilian and military personnel, including deployed forces. Expected benefits include (1) an uninterrupted flow of information; (2) improvements to interoperability, security, information assurance, knowledge sharing, productivity, and operational performance; and (3) reduced costs.

The Navy awarded the NMCI contract in October 2000 to Electronic Data Systems Corporation, for an estimated 412,000 to 416,000 workstations/seats and an estimated minimum value of \$6.9 billion over 8 years.



Objective

In the National Defense Authorization Act for Fiscal Year 2002 (Public Law 107-107), the Congress directed us to review the impact that participation in NMCI has on IT costs of Navy working capital funded industrial facilities.

As agreed with the House and Senate Armed Services Committees, our work focused on Navy shipyards and air depots that operate under the Navy's working capital fund [1]. Because working capital funded facilities must set rates to recover all costs through charges to customers, our work also included NMCI's impact on rates.

[1] Three of the shipyards and all the air depots operate under the Navy Working Capital Fund; the Pearl Harbor shipyard operates under an annual appropriation. When we refer in this briefing to the shipyards, we do not include Pearl Harbor.



Scope and Methodology

We obtained and analyzed information from the following sites:

- NMCI Program Office, Arlington, Virginia [1]
- Navy Headquarters Budget Office, Arlington, Virginia [1]
- Naval Sea Systems Command, Washington, D.C. [1]
- Naval Air Systems Command, Patuxent, Maryland [1]
- Naval Air Depot, Cherry Point, North Carolina [1]
- Naval Air Depot, Jacksonville, Florida [1]
- Naval Air Depot, North Island, California
- Naval Shipyard, Portsmouth, New Hampshire [1]
- Naval Shipyard, Norfolk, Virginia
- Naval Shipyard, Puget Sound, Washington
- Office of the Assistant Secretary of Defense for Command, Control, Communications, and Intelligence, Arlington, Virginia [1]

[1] Sites visited.



Scope and Methodology (cont'd)

We obtained and analyzed the following types of information:

- Budgeted information on overhead costs, IT costs, and NMCI costs for fiscal years 2000 through 2003. At the time of our review, Navy had not prepared its fiscal year 2004 budget estimates.
- Rates (prices that the shipyards and air depots charge their customers) and that portion of the rates that was budgeted to cover NMCI costs.
- Information on NMCI-like services and unresolved NMCI implementation issues and perspectives on these issues from officials at the shipyards and air depots and the NMCI program office.

We did not independently verify the accuracy or completeness of certain information provided by the Navy, such as budgeted costs and rates.

We performed our work from March through August 2002 in accordance with generally accepted government auditing standards.



Results in Brief

To date, NMCI has not measurably affected either IT costs at shipyards and air depots or the rates they charge customers, because NMCI has not been implemented at these facilities and is not expected to be in place until the latter part of fiscal year 2003. However, shipyard and depot officials stated that NMCI transition activities during fiscal year 2002, such as site readiness and preparation, have had an effect on costs that cannot be quantified because these costs were not separately identified.

For fiscal year 2003, budget estimates show that NMCI will make up about 2 percent of total shipyard and depot costs and about 38 and 31 percent of shipyard and depot IT costs, respectively. Shipyard and depot officials told us that these NMCI cost estimates, which are a component of overhead costs, will not affect the rates charged to customers in fiscal year 2003 because they plan to reduce budgeted costs in other overhead accounts, such as travel, training, and real property maintenance, to offset budgeted NMCI costs.



Results in Brief (cont'd)

The impact of NMCI on IT costs and rates beyond fiscal year 2003 is unclear because several issues peculiar to shipyards and depots are unresolved, such as how the costs of some transition items will be funded and whether these costs will be included in the rates. Moreover, when they will be resolved is uncertain, because NMCI implementation plans do not specifically provide time frames or procedures for doing so. The absence of an explicit issue management process exacerbates the uncertainty surrounding NMCI's future impact on shipyard and depot costs and rates.

To reduce this uncertainty and allow the shipyards and depots to make more informed planning and budgeting decisions, we are making recommendations aimed at resolving these issues.

In its oral comments on a draft of this briefing, Defense officials agreed with our findings, conclusions, and recommendations.



Background

NMCI is to replace thousands of independent networks, applications, and other hardware and software with one secure network for all Navy and Marine Corps civilian and military personnel, including deployed forces. Expected benefits include

- uninterrupted flow of information;
- improvements to interoperability, security, information assurance, knowledge sharing, productivity, and operational performance; and
- reduced costs.



Background (cont'd)

NMCI contract

NMCI is being accomplished through a multiyear IT services contract that has a base period of 5 years plus a 3-year option period [1]. The contract is a firm fixed-price, indefinite-delivery/indefinite-quantity contract with performance incentives. Awarded on October 6, 2000, the contract covers

- delivery and maintenance of workstations and desktop applications;
- transmission of voice, video, and data; and
- infrastructure improvements.

[1] The contract was awarded to Electronic Data Systems (EDS) Corporation.



Background (cont'd)

Roles and responsibilities

Several organizations share responsibility for managing NMCI.

Organization	NMCI roles and responsibilities
Office of the Assistant Secretary of Defense for Command, Control, Communications and Intelligence (OASD C3I)	Provides guidance, assesses compliance with the Clinger-Cohen Act, and oversees program management activities related to major milestone approvals for NMCI; is the milestone decision authority for the program.
Navy Chief Information Officer	Coordinates NMCI policy, planning, and interoperability issues.
NMCI program office	Manages the NMCI contract; creates and manages implementation of a Navywide NMCI execution plan.
Parent commands [1]	Manage implementation of NMCI at their facilities.
Shipyards and air depots	Carry out NMCI implementation, receive respective contracted services, and respond to customer satisfaction questionnaire related to services provided.

[1] The parent command for the Naval shipyards is the Naval Sea Systems Command, and the parent command for Navy air depots is the Naval Air Systems Command.



Background (cont'd)

Legislative requirements

Public Law 106-398 (2001 National Defense Authorization Act) and Public Law 107-107 (2002 National Defense Authorization Act) mandated that NMCI be implemented in phases and that NMCI program management controls comply with the Clinger-Cohen Act and DOD acquisition regulations.

Key features of implementation phases

Phase I:

- Beginning with contract award in October 2000, phase I covered about 15 percent or about 62,000 of the expected total of 412,000 to 416,000 seats.
- This phase excluded shipyards and air depots.



Background (cont'd)

Phase II:

- In phase II, tests and evaluations were required to demonstrate the operational effectiveness of the network (whether the equipment, operating software, and applications software performed as intended); this phase did not require evaluations to determine whether expected costs and benefits were being realized.
- On the basis of April 2002 test and evaluation results, which the OASD C3I approved in May 2002, the Navy was allowed to order an additional 100,000 seats and proceed with the remainder of the program, subject to key improvements to management controls and satisfaction of specific testing requirements (e.g., an updated test and evaluation plan, a plan and schedule for migrating legacy applications to NMCI, updates to the business case, and DOD senior-level review of program results).
- Within phase II are 20,301 seats designated for shipyards and air depots that operate under the Navy Working Capital Fund.



Background (cont'd)

Shipyards and air depots

Navy shipyards and air depots overhaul and repair ships, planes, and engines and provide engineering, technical, and professional services on maintenance and logistic problems to the Navy, DOD, and other federal government customers. The locations of the Navy's three shipyards and three air depots are shown on the following slide.

The shipyards and depots that are under the Navy Working Capital Fund operate similarly to commercial entities. That is, they do not receive an annual appropriation, but receive their funding from customer orders, for which they charge rates that must capture all costs of operations.

Rates charged customers in a given year are based on estimates of direct, indirect (e.g., materials used for more than one project or purpose), and overhead (e.g., IT support) costs for that year. If actual costs exceed estimates, the shipyards and depots would operate at a loss for that year and thus be required to increase rates in the subsequent year(s).



Background

Shipyard and depot locations





Background (cont'd)

NMCI status/plans

Navywide:

- As of July 31, 2002, the Navy reports that EDS had assumed responsibility for operating and maintaining 57,674 seats, and 19,536 of these seats had reached “cutover” (the point at which the NMCI operating environment is to function in full support of contracted service level agreements [1]).

Shipyards and air depots:

- A total of 20,301 NMCI workstations are planned for the three shipyards and three air depots that operate using Navy working capital funds—12,336 workstations are planned for shipyards, and 7,965 workstations are planned for depots, with cutover projected during June and July of 2003, respectively [2]. (See table on next slide for more detailed breakout.)

[1] Service level agreements define the agency’s expectations (e.g., requirements in terms of system performance objectives and customer satisfaction, often defined as specific agency mission outcome goals) and are used to track and measure a contractor’s performance.

[2] According to shipyard and depot officials, the number of workstations actually implemented may be different from what the table on the next slide indicates as they further review their workstation fiscal year 2003 requirements.



Background (cont'd)

NMCI status/plans (cont'd)

Shipyards	Seats	Start cutover
Portsmouth	2,526	June 2003
Norfolk	4,610	June 2003
Puget Sound	5,200	June 2003
<i>Subtotal</i>	<i>12,336</i>	
Air depots		
Cherry Point	2,630	July 2003
Jacksonville	2,935	July 2003
North Island	2,400	July 2003
<i>Subtotal</i>	<i>7,965</i>	
Total	20,301	



Results: Near-Term Impact on Costs

No measurable impact to date

NMCI is not scheduled to be implemented at the shipyards and air depots until the latter part of fiscal year 2003. Thus, through fiscal year 2002, NMCI has had no quantifiable impact on IT costs or the rates that these activities charged customers.

Unquantifiable impact may have occurred

According to shipyard and depot officials, delays in implementing NMCI have resulted in shipyards and air depots performing activities multiple times, resulting in increases in IT overhead costs in fiscal years 2001 and 2002.



Results: Near-Term Impact on Costs (cont'd)

Examples of activities that were performed multiple times include

- temporarily extending existing IT services contracts that NMCI is to eventually supplant,
- revising the numbers and types of NMCI workstations to be ordered in response to contractor updates of hardware and software available since contract award,
- identifying legacy hardware and software applications that NMCI cannot currently support, and
- inventorying existing IT assets in response to multiple program office “data calls,” each governed by different rules and formats.



Results: Near-Term Impact on Costs (cont'd)

Our analysis of available documentation, such as the NMCI demand models for the shipyards and depots, budget reports, NMCI-related planning documents, and project team meetings, confirmed that these activities have been performed. However, because the shipyards and depots have not separately accounted for these costs, we could not quantify their impact on IT costs. Shipyard and depot officials stated that these costs were minimal.



Results: Near-Term Impact on Costs (cont'd)

Estimated impact on 2003 costs

The following charts show budget estimates developed by the shipyards and air depots for fiscal years 2000 through 2003, assuming NMCI implementation in fiscal year 2002. These estimates can be viewed as indicators of NMCI's quantifiable cost impact, with one key qualification:

Qualification: The shipyards' and depots' respective parent commands decided that NMCI's implementation at shipyards and depots in fiscal year 2002 and 2003 should not impact the rates charged customers during this time. These budget estimates do not reflect the adjustments that would have to be made to other overhead accounts, such as other IT costs, indirect labor, real property maintenance, travel, and training, to offset the costs associated with NMCI and thereby not affect rates.

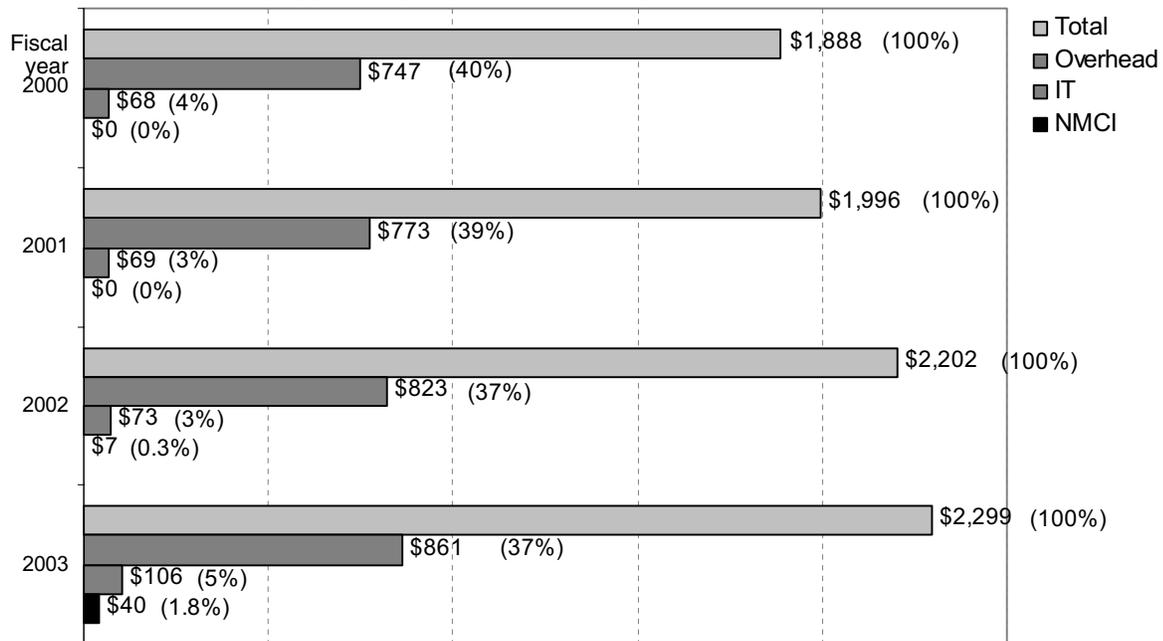
Based on the estimates and assuming that NMCI is implemented in fiscal year 2003, NMCI does not represent a significant portion of estimated total shipyard and depot costs (1.8 percent for shipyards and 1.6 percent for depots), but it does represent 38 percent and 31 percent of shipyard and depot IT costs, respectively [1].

[1] The costs and resultant percentages shown on all the charts in this briefing are rounded amounts.



Results: Near-Term Impact on Costs (cont'd)

Cost estimates for shipyards (millions of dollars)



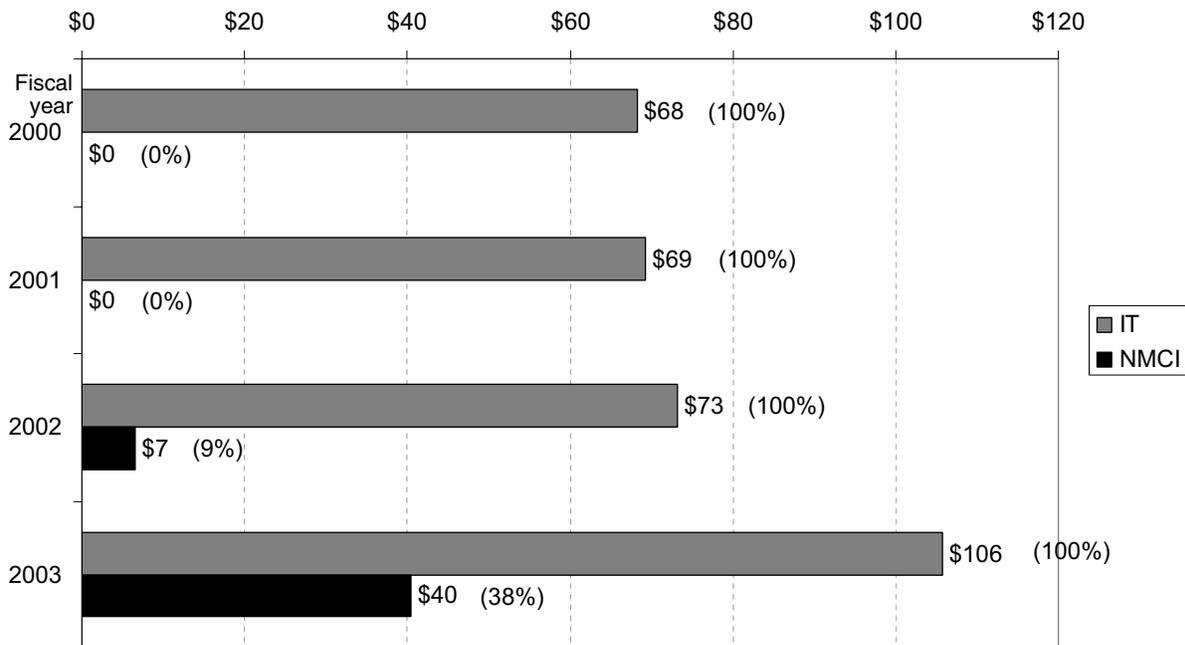
Note: Fiscal year 2002 estimates were developed in fiscal year 2001, assuming implementation in fiscal year 2002. Fiscal year 2003 estimates were developed in fiscal year 2002, assuming implementation in fiscal year 2003.

Source: GAO analysis based on Navy data.



Results: Near-Term Impact on Costs (cont'd)

NMCI and IT cost estimates for shipyards (millions of dollars)



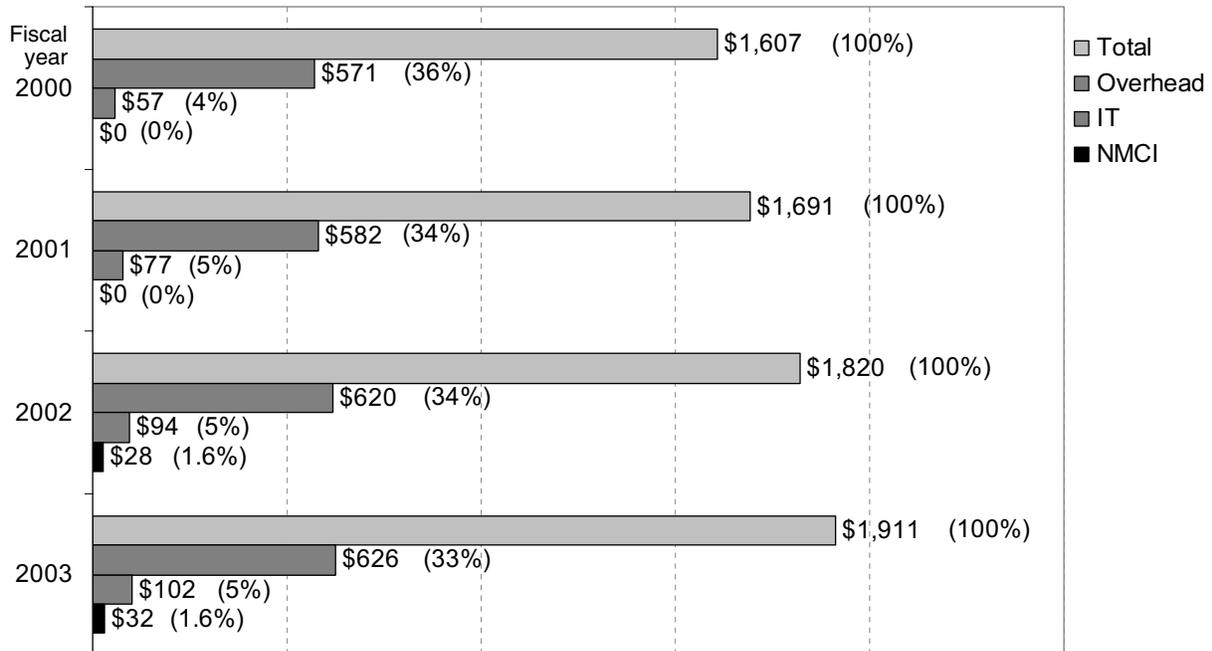
Note: Fiscal year 2002 estimates were developed in fiscal year 2001, assuming implementation in fiscal year 2002. Fiscal year 2003 estimates were developed in fiscal year 2002, assuming implementation in fiscal year 2003.

Source: GAO analysis based on Navy data.



Results: Near-Term Impact on Costs (cont'd)

Cost estimates for air depots (millions of dollars)



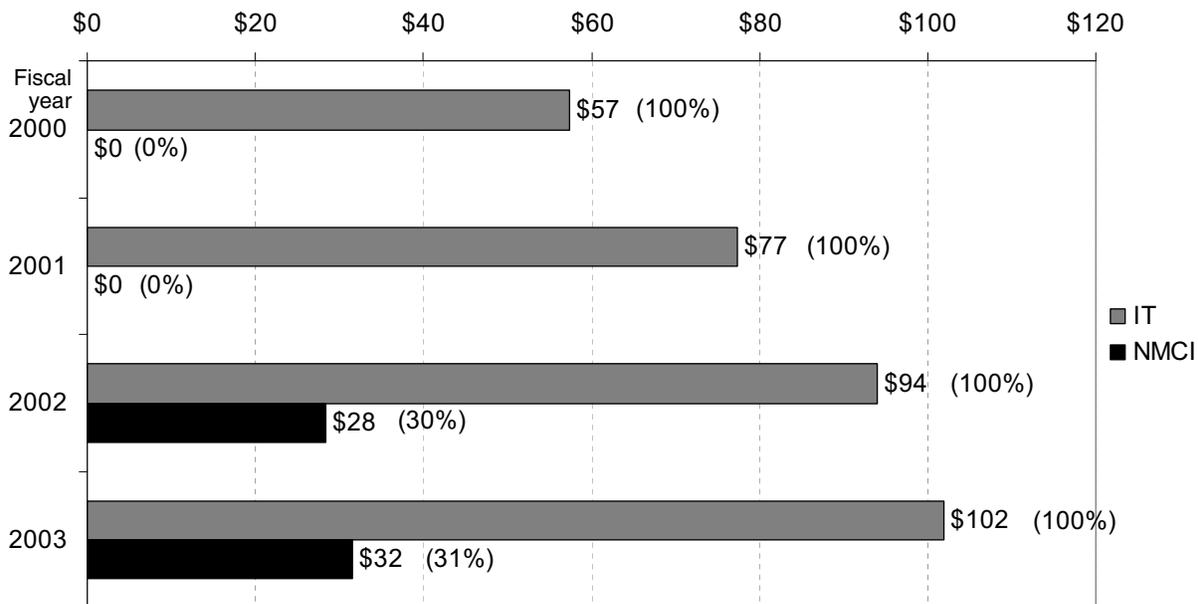
Note: Fiscal year 2002 estimates were developed in fiscal year 2001, assuming implementation in fiscal year 2002. Fiscal year 2003 estimates were developed in fiscal year 2002, assuming implementation in fiscal year 2003.

Source: GAO analysis based on Navy data.



Results: Near-Term Impact on Costs (cont'd)

NMCI and IT cost estimates for air depots (millions of dollars)



Note: Fiscal year 2002 estimates were developed in fiscal year 2001, assuming implementation in fiscal year 2002. Fiscal year 2003 estimates were developed in fiscal year 2002, assuming implementation in fiscal year 2003.

Source: GAO analysis based on Navy data.



Results: Near-Term Impact on Rates

NCMI costs have not affected the total rate charged customers, but they have affected the content of the overhead portion of the rate.

Both shipyards and air depots included estimated NMCI costs in the rates they charge customers in fiscal years 2002 and 2003. However, as previously mentioned, their respective parent commands directed that any increase in budgeted IT costs caused by NMCI be offset by reductions in other budgeted overhead accounts.

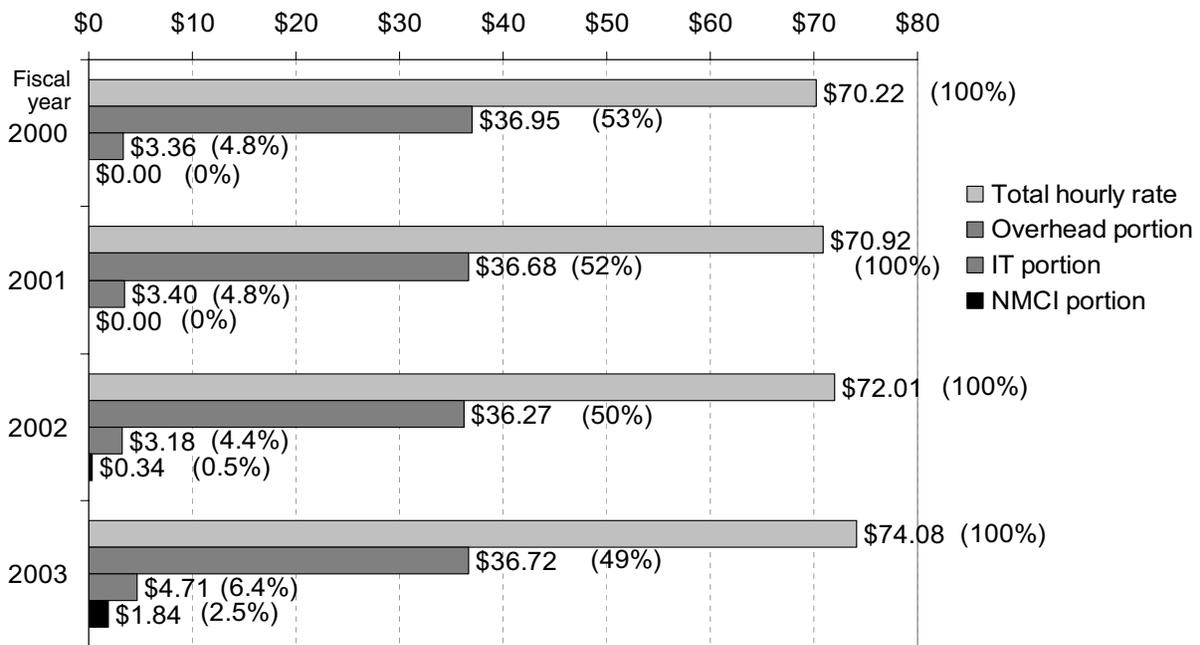
The following two charts show the allocation of budgeted costs within the hourly rate structure for fiscal years 2000 to 2003. The budgeted costs of the overhead accounts for fiscal years 2002 and 2003 were adjusted for NMCI cost impact (i.e., NMCI costs are shown with the planned offset adjustments in other overhead accounts).

Note: Activities have plans for reducing actual overhead costs during fiscal year 2003. If activities are not successful in implementing plans or in offsetting unexpected costs that may arise during the year, they could operate at a loss and thus be required to increase rates in subsequent fiscal years.



Results: Near-Term Impact on Rates (cont'd)

Hourly rate data for shipyards



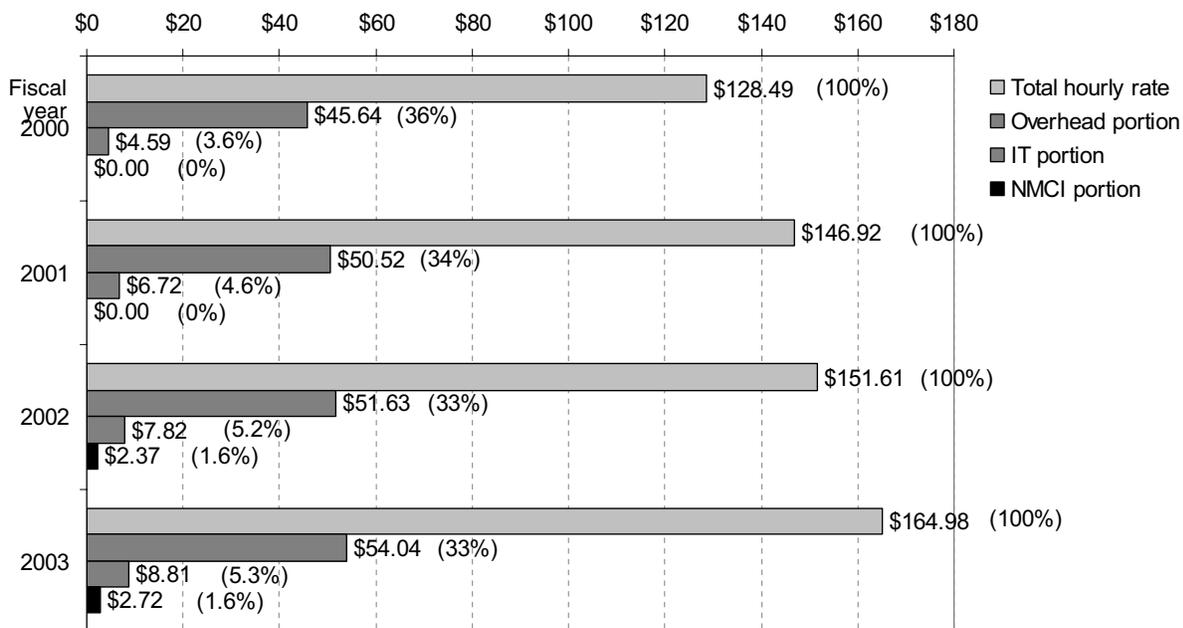
Note: Fiscal year 2002 estimates were developed in fiscal year 2001, assuming implementation in fiscal year 2002. Fiscal year 2003 estimates were developed in fiscal year 2002, assuming implementation in fiscal year 2003.

Source: GAO analysis based on Navy data.



Results: Near-Term Impact on Rates (cont'd)

Hourly rate data for air depots



Note: Fiscal year 2002 estimates were developed in fiscal year 2001, assuming implementation in fiscal year 2002. Fiscal year 2003 estimates were developed in fiscal year 2002, assuming implementation in fiscal year 2003.

Source: GAO analysis based on Navy data.



Results: Longer Term Impacts on Costs and Rates

Navy is not taking steps to resolve uncertainties surrounding NMCI implementation at shipyards and air depots.

Working capital fund management policy advocates taking adequate steps to avoid disruptive cost fluctuations and unforeseen cost changes [1]. This policy recognizes that such steps allow for more accurate planning and budgeting and more effective use of resources. One way to implement this policy is to have a process for identifying those issues that could contribute to cost fluctuations and changes and systematically plan for resolving them.

[1] DOD Financial Management Regulation 7000.14R, Chapter 50, Defense Working Capital Fund General Policies and Requirements, page 50-2, paragraph h.



Results: Longer Term Impacts on Costs and Rates

Beyond fiscal year 2003, shipyards and depots face potential cost fluctuations and changes because important issues concerning NMCI's implementation have not been resolved.

- The NMCI program office has designated the time frame for implementing NMCI at shipyards and air depots as "targeted" and "proposed," and program officials characterized the time frame as tentative. Further, shipyard and depot officials told us that they expect further delays in NMCI's implementation.



**Results: Longer Term Impacts on Costs and Rates
(cont'd)**

- The NMCI program office has not decided who will pay for unique requirements of shipyard and depot operations that may require changes to the NMCI contract. Such requirements include
 - arranging for workstations to accompany personnel as they change locations (e.g., as ships move from dry dock to pier);
 - securing unclassified naval nuclear propulsion information; and
 - establishing and maintaining connections between NMCI and existing networks (including classified networks) and certain legacy applications and databases.



**Results: Longer Term Impacts on Costs and Rates
(cont'd)**

- The NMCI program office has not decided who will pay newly identified and increased NMCI transition costs, such as the increased costs associated with short-term contract actions to maintain existing services until NMCI is implemented.



Results: Longer Term Impacts on Costs and Rates (cont'd)

According to the NMCI program officials, these issues have not been resolved but are being addressed in coordination with the Navy commands as they implement NMCI.

Additionally, program officials said they have undertaken other actions to mitigate NMCI's impact such as

- using appropriated funds to pay for certain NMCI contract costs, such as fees awarded the contractor for meeting performance incentives, facility support costs (e.g., equipment to facilitate transition to NMCI), and physical space costs;
- waiving the requirement for shipyards and depots to expense prior investments, such as recently purchased computer equipment and other capital assets that will be transferred to the contractor when NMCI is implemented [1];
- working with the contractor to develop lower cost workstation (i.e., seat) alternatives; and
- not distributing network connection and telecommunications costs to activities like shipyards and air depots.

[1] We did not determine if the planned approach for accomplishing this was consistent with relevant accounting principles.



**Results: Longer Term Impacts on Costs and Rates
(cont'd)**

These plans do not provide shipyard- and depot-specific actions and time frames for addressing each of the issues raised by shipyards and depots. Moreover, issues facing shipyards and depots in implementing NMCI are not governed by an explicit Navywide process that would identify, document, and track resolution of these issues. According to shipyard and depot officials, the lack of a process is due to uncertainty surrounding roles and responsibilities for resolving these issues.



Conclusions

NMCI has yet to impact costs at shipyards and air depots or the rates they charge customers in any quantifiable way. Looking toward fiscal year 2003, NMCI costs will likely have a minor impact on the allocation of shipyard and depot overhead costs and the rates each activity charges, but total costs and hourly rates should not change as a result of NMCI, because these activities' parent commands have decided to offset NMCI costs with reductions in other overhead costs [1].

Looking beyond fiscal year 2003, NMCI's impact on costs and rates is less clear, because important implementation issues have not been resolved, and the Navy is not systematically providing for their resolution. Such uncertainty surrounding NMCI, and thus the costs that shipyards and depots will incur, hampers these activities' ability to effectively and efficiently plan, budget, and use resources. Thus, it is important that the Navy systematically plan for and resolve these issues.

[1] Activities have plans for reducing actual overhead costs during the year of execution—fiscal year 2003. If they are not successful in implementing these plans or in offsetting unexpected costs that may arise during the year, they could operate at a loss and thus be required to increase rates in subsequent fiscal years.



Recommendations for Executive Action

To assist Navy shipyards and air depots in preparing for NMCI's impact on their respective costs and rates, we recommend that the Secretary of Defense have the Secretary of the Navy direct the NMCI program manager, in collaboration with the Commanders of the Naval Sea Systems Command and the Naval Air Systems Command, to systematically and expeditiously resolve NMCI implementation issues that affect the ability of shipyards and depots to plan and budget. In particular, we recommend that the NMCI program manager work with these commanders to develop and execute an issue management process that resolves each of the issues discussed in this briefing and includes

- participation by Navy shipyard and air depot officials,
- continuous identification of relevant and material NMCI implementation issues,
- shipyard and air depot implementation plans that include strategies for resolving these issues, and
- tracking of and reporting on issue resolution.



Agency Comments and Our Evaluation

In the department's oral comments on a draft of this briefing, officials from the OASD(C3I), Office of the Navy Chief Information Officer, Naval Air Systems Command, and Naval Sea Systems Command agreed with our findings, conclusions, and recommendations. They also provided updated and clarifying information, which we have incorporated as appropriate in the briefing.

In addition to obtaining the department's oral comments on a draft of this briefing, we shared the contents of the briefing with NMCI program officials, including the deputy program manager, when we completed our audit work. These officials also agreed with our findings and conclusions, but stated that our recommendations should be directed to the shipyard and depot parent commands, rather than the NMCI program office. According to the officials, the parent commands, along with the Comptroller of the Navy, have all the information and authority necessary to resolve the issues discussed in this briefing.



Agency Comments and Our Evaluation

The difference of opinion within the department on who the recommendations should be directed to points to the need for the various NMCI players to work collaboratively to resolve key issues and for one entity to take the lead in doing so, as noted in our recommendations. Given the program office's defined role under the NMCI governance structure, as well as the fact that resolving some of these issues requires interpretations of NMCI contract provisions and interactions with the contractor (which only the program office is positioned to do), our recommendations provide for the program office, rather than the parent commands, to take this lead role.

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