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More Direction Needed To Establish a Uniform Depot Maintenance Accounting System. FGMSD-78-35; E-159797. May 22, 1978. 2 pp. + 3 appendices (10 pp.).

Report to Secretary, Department of Defense; by D. L. Scantlebury, Director, Financial and General Management Studies Div.

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Over the past 15 years, the Department of Defense (DOD) has made several unsuccessful attempts to establish a uniform depot maintenance cost accounting system. Findings/Conclusions: The most recent attempt to establish such a system, begun in 1975, has met with substantial difficulties in its implementation stage. The scheduled startup date, October 1976 at Air Force depots, has been delayed, and an interim system does not provide for the allocation of actual direct labor. Implementation of this part of the system may take 3 more years. The new system as now used at Army and Navy maintenance depots is not producing uniform cost accounting data because these services are continuing to use diversified approaches in developing such data. A uniform system would enable DOD management officials to assess the effectiveness of depot maintenance operations which cost several billion dollars in fiscal year 1976. Problems identified in implementing a uniform cost accounting system were: lack of sufficiently comprehensive guidelines to preclude the use of widely varying methods of computing and reporting costs, lack of leadership to insure that managers knew the objectives and uses of the system, and failure of depots to follow the DOD handbook. Recommendations: The Secretary of Defense should have Assistant Secretaries: establish a focal point to oversee system implementation and respond decisively to problems which might compromise the comparability of the cost system at different depots; and provide more complete instructions to depots and limit interpretations of the instructions so that services will follow the same cost accounting procedures. (HTW)

REPORT BY THE U.S.

General Accounting Office

More Direction Needed To Establish A Uniform Depot Maintenance Accounting System

The Department of Defense is trying to implement a uniform depot maintenance cost accounting system to assist its management officials in assessing the effectiveness of the military services' depot maintenance operations.

Over the past 15 years Defense's attempts to establish such a system have not been successful. The most recent attempt begun in 1975 is incurring great difficulties.

GAO recommends ways which will help effect a useful uniform system.



FGMSD-78-35
MAY 22, 1978



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-159797

The Honorable
The Secretary of Defense

Dear Mr. Secretary:

We have reviewed the Defense Department's current effort to establish a uniform depot maintenance cost accounting system. Over the past 15 years Defense has attempted several times to establish a uniform system and each attempt has been unsuccessful.

The most recent attempt begun in 1975 is incurring substantial difficulties in its implementation stage. The scheduled startup date (October 1976) at Air Force depots has been delayed. The Air Force is using an interim system which does not provide for the allocation of actual direct labor. As a result data is not comparable with data from the systems of the Army and Navy. The Assistant Secretary of the Air Force (Financial Management) has stated that the implementation of the direct labor hours part of the system may take 3 more years.

Moreover, the new system as now used at Army and Navy maintenance depots is not producing uniform cost accounting data because these services are continuing to use diversified approaches in developing such data.

Depot maintenance is the major overhaul and/or rebuilding of equipment at military facilities or commercial contractor plants. Complete cost data on military depot maintenance operations is not available; however, fiscal year 1976 (the latest available data) depot level maintenance cost several billion dollars.

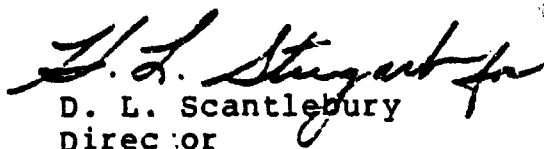
With a uniform accounting system, Defense Department management officials could assess the effectiveness of military services' depot maintenance operations. However, if the system is to be a useful tool, the Secretary of Defense must exercise strong, central direction and oversight over the systems implementation and operation by the military services to assure that the data from each of the services is compiled consistently.

We and the Defense Audit Service identified the military services' problems in implementing the uniform cost accounting system. These problems and our recommendations to you are included in appendix I. Appendix II details the scope of our review. A glossary of accounting terms used in this report is included as appendix III. We have informally discussed our findings with Defense Department officials and their comments have been considered.

As you know section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House Committee on Government Operations and the Senate Committee on Governmental Affairs not later than 60 days after the date of this report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of this report. We would appreciate receiving copies of these.

We are sending copies of this report to the Chairmen, House Committee on Government Operations, Senate Committee on Governmental Affairs, and the House and Senate Committees on Appropriations and Armed Services; the Director, Office of Management and Budget; and the Secretaries of the Army, Navy, and Air Force.

Sincerely yours,


D. L. Scantlebury
Director

FINDINGS AND RECOMMENDATIONS ON DEFENSE EFFORTS
TO ESTABLISH A UNIFORM DEPOT MAINTENANCE
COST ACCOUNTING SYSTEM

LACK OF UNIFORMITY--A LONGSTANDING PROBLEM

The Department of Defense attempted to establish a uniform cost accounting system in 1963 and 1968. But, as we noted in a February 2, 1971, report (B-159797) cost accounting practices varied so widely among services and among activities within a single service that no meaningful comparisons of activities performing similar work could be made.

Specifically:

- DOD had not provided adequate control or sufficiently detailed instruction to accomplish its objective.
- Inconsistent methods and procedures and questionable practices were used in the then current (1971) cost accounting system.

To correct previously identified weaknesses, the Assistant Secretary of Defense (Installation and Logistics) established in November 1972 a Joint Logistics Commanders panel to create a uniform depot maintenance cost accounting manual. In October 1975 the Department of Defense published the "Department of Defense Depot Maintenance and Maintenance Support Cost Accounting and Production Reporting Handbook" (DOD 7220.29-H). The new system was to have been implemented by October 1, 1976.

The objectives of the newly designed system are:

- To establish a uniform cost accounting system for use in accumulating the costs of depot maintenance activities as they relate to the weapon systems supported or items maintained. This information would enable managers to compare unit repair costs with replacement cost.
- To assure uniform recording, accumulating, and reporting on depot maintenance operations and maintenance support activities so that comparison of repair costs can be made between depots and between depots and contract sources performing similar maintenance functions.

- To assist in measuring productivity, developing performance and cost standards, and determining areas for management emphasis, which would enable managers to evaluate depot maintenance and maintenance support activities for efficient resource use.
- To provide a means of identifying maintenance capability and duplication of capacity and indicating both actual and potential areas for interservice support of maintenance workload.

LACK OF UNIFORMITY CONTINUES AS NEW SYSTEM ENCOUNTERS OLD PROBLEMS

The uniform cost accounting system that the Defense Department is currently trying to implement is falling short of its objectives. The shortfall, we believe, can be attributed to the following deficiencies:

- The guidelines for the system were not sufficiently comprehensive to preclude the use of widely varying methods of computing and reporting costs.
- The Office of the Secretary of Defense (Manpower, Reserve Affairs and Logistics) did not provide necessary leadership to insure that managers knew the objectives and uses of the cost accounting system.
- The implementing depots did not always follow the Department of Defense handbook and in some cases followed interpretations of the handbook which were contradictory.

The new system, now well past scheduled startup, is not fully implemented. The Defense Audit Service, in a report dated August 2, 1977, stated that of 11 activities reviewed, none had fully implemented the system. The report also states that the Air Force is experiencing difficulties in converting to a job order cost system required by the Department of Defense handbook. Current Air Force plans show the system will not be implemented until 1981.

To facilitate timely implementation, the Defense Audit Service recommended that the Assistant Secretary of Defense (Comptroller) coordinate with the Assistant Secretary of Defense (Manpower, Reserve Affairs and Logistics) to direct the services to develop a monitoring and reporting system to insure that proscribed cost accounting procedures are implemented in a timely and cost-effective manner. The

Defense Audit Service report shows that substantial additional work is required on the uniform cost accounting system before the system will produce uniform data which will be useful in comparing costs incurred by depots and private contractors. The Defense Audit Service recommended that the Assistant Secretary of Defense (Comptroller) coordinate with the Assistant Secretary of Defense (Manpower, Reserve Affairs and Logistics) to:

- Review the implementing guidance on depot maintenance cost accounting and direct the services to rescind conflicting implementing instructions. Issue more specific guidance when inconsistencies between the services are identified. The services should also review their implementing guidance to assure it is uniform and consistent with the handbook.
- Require the services to accumulate and compare work measurement data with data generated by the depot cost accounting system to identify areas needing management attention.
- Develop more specific instructions for costing military labor, such as ships' crews at shipyards, and for establishing job orders. The services also need to improve their systems for accumulating and distributing depreciation, base support expenditures, and command costs.

Implementing procedures not comprehensive

The Department of Defense handbook contains guidance for determining various cost elements, some of which were not readily available in past Department of Defense cost accounting systems. This included the costing of depreciation, military labor, and associated base support costs. Although the guidance provided for costing these and other elements of cost, it did not provide sufficiently specific guidelines to insure use of uniform cost accounting procedures. As a result, implementing activities used differing methods for such things as determining residual value for real property, costing material exchanges, and charging military labor at shipyards. As a result, significant differences for costs incurred are reported. For example, we noted that the method used to depreciate real property at the Corpus Christi Army Depot is not the same as that in use at the Jacksonville Naval Air Rework Facility. At Corpus Christi residual value is considered in determining depreciation costs of plant and equipment; however, at

Jacksonville residual value is not used. To illustrate the effect of these differing methods, we computed depreciation of the main plant at Corpus Christi and found that depreciation costs over the remaining useful life of the plant using the Corpus Christi method would be about \$838,000, whereas, using the Jacksonville method, the depreciation costs would be \$7.5 million.

Oversight not provided

The Offices of the Assistant Secretaries of Defense (Comptroller) and (Manpower, Reserve Affairs and Logistics) participated in formulating the cost accounting policies outlined in the Defense Department's cost accounting handbook. However, neither office provided the necessary leadership or management emphasis to insure uniform implementation of the system. Instead, the Comptroller of each military service was required to implement the system prescribed by the Department of Defense handbook, but the Comptrollers were not required to report to the Secretary of Defense the status of implementation. Moreover, our review disclosed that depot managers were not always aware of the importance of implementing these policies to insure the establishment of a uniform cost system.

For example, the Department of Defense handbook states that uniform costing requires that support services be recognized as part of indirect expense of the benefiting activity regardless of funding arrangements. However, the Comptroller at one installation decided that the costs of an associated supply operation should not be included in the cost system since funding for the supply operation was not included as part of the industrial fund. At the same time, the Comptroller acknowledged that 91 percent of the items stored by the supply operation were there to support the maintenance activity. The inclusion of supply costs would increase the installation's overhead cost by \$4.8 million or 16.9 percent.

There also is a need to make the services fully aware of the uses of the cost system. For example, the Defense Audit Service reported that:

"In most instances, the Services were not accumulating and/or comparing work measurement data with data generated by the depot cost accounting system."

The report went on to emphasize that "measuring productivity against realistic standards is one of the main objectives of the system."

Instructions not followed

Both the Corpus Christi Army Depot and the Jacksonville Naval Air Rework Facility established costing procedures which contradicted the Department of Defense handbook and resulted in differing cost methods. For example, the Department of Defense handbook states that adjustments to an asset's estimated service life should be made as long as the asset is in use. Good accounting practice requires that depreciation rates on assets be reviewed periodically so that corrections in the asset's useful life may be reflected in revised rates of depreciation. However, the Corpus Christi Army Depot followed the Army's Letter of Instruction, number one, and the Joint Logistics Commanders Joint Interpretive Issue, number eleven. The Joint Issue excludes assets from further depreciation after they have been fully depreciated. The Army Instruction did not specifically address this subject but was interpreted to also exclude further depreciation. As a result, the Corpus Christi Army Depot had assets valued at \$33 million which were fully depreciated but still in use. Similarly, the Jacksonville Naval Air Rework Facility did not adjust useful lives for fully depreciated assets and reported assets valued at \$4.7 million as fully depreciated, although still in use. Depreciation at both installations was understated because of these actions.

Further, the Defense Audit Service reported a lack of uniformity in cost accounting within the Army. According to its report two of the three Army maintenance facilities visited had not adhered to longstanding Army maintenance policies on controlling material and labor costs.

The following table shows other examples where the depots did not follow the Department of Defense handbook

Comparison of Handbook with Practices Found

<u>Handbook</u>	<u>Corpus Christi Army Depot</u>	<u>Jacksonville Naval Air Rework Facility</u>
	<u>Higher Headquarters Expense</u>	
Should be included	Not included	To be included at end of year
	<u>Military Labor</u>	
Should include acceleration factors for leave, retirement, and other benefits	Acceleration factors are not included in military labor	Acceleration factors are not included in military labor
	<u>Quality Assurance</u>	
Final and operational testing should be charged as direct labor	Final and operational testing is charged as an indirect expense	Final and operational testing is charged as an indirect expense
	<u>Manufacturing</u>	
Should be charged to separate job orders	Costs are normally charged to a separate job order	Costs are not normally charged to separate job orders
	<u>Defective Work</u>	
Should be charged as indirect when defect levels are exceeded	Charged as direct	Charged as direct.

CONCLUSIONS AND RECOMMENDATIONS

Repeated efforts to establish a uniform depot maintenance cost accounting system have been unsuccessful. Problems of a longstanding nature continue to thwart effective implementation of cost uniformity. Specifically, (1) each service continues to resist uniformity and (2) the Defense Department has not provided the necessary management action to overcome this resistance.

In order to implement a useful uniform cost accounting system, we recommend that the Secretary of Defense have the Assistant Secretaries of Defense (Comptroller and Manpower, Reserve Affairs and Logistics):

- Establish a focal point to oversee system implementation and respond decisively to problems which might compromise the comparability of the cost system at different depots.
- Provide more complete instructions to depots and limit interpretations of the instructions so that services will follow the same cost accounting procedures.

We plan to continue monitoring the Defense Department efforts in implementing the uniform depot maintenance accounting system because we believe the system can be useful in assisting Defense Department management officials assess the effectiveness of the military services' depot maintenance operations.

SCOPE OF REVIEW

We reviewed how the Corpus Christi Army Depot, Corpus Christi, Texas; the Jacksonville Naval Air Rework Facility, Jacksonville, Florida; and the Oklahoma City Air Logistics Center, Oklahoma City, Oklahoma were implementing the cost accounting system. We also obtained information from the Air Force Logistics Command, the Office of the Assistant Secretary of Defense (Manpower, Reserve Affairs and Logistics), and the Office of the Assistant Secretary of Defense (Comptroller).

In addition, we reviewed the Defense Audit Service audit report (and supporting workpapers) of its recent review of the implementation of the Department of Defense uniform cost accounting system. Because it reviewed three Army depots, six Navy and Marine activities, and two Air Force activities, we limited the scope of our survey.

GLOSSARY

The following definitions are included in the Defense cost accounting handbook.

Base operations cost	Costs incurred at installations at which the depot maintenance activities are located. Such costs relate to depot maintenance as indirect cost for either operations overhead or general and administrative expenses.
Cost accounting system	A subsystem of the accounting system designed to show the detailed costs of operations and the accumulated costs by types of products.
Defective work	Maintenance work performed that does not meet the work specifications or quality control tests.
Direct cost	Any cost which is identified specifically with a particular final cost objective. Direct costs are not limited to items which are incorporated in the end product as material or labor.
Indirect costs	Any cost not directly identified with a single final cost objective, but identified with two or more final cost objectives or with at least one intermediate cost objective.
Job order costing	The method of cost accounting whereby cost is compiled for a specific quantity of product, equipment, repair, or other service that moves through the production process as a continually identifiable unit. The applicable material, direct labor, other direct costs, and the allocated portions of overheads are charged to specific job orders.

Residual value

The proceeds (less removal and disposable costs, if any) realized upon disposition of a tangible capital asset. It usually is measured by the net proceeds from the sale or other disposition of the asset or its fair value if the asset is traded in on another asset. The estimated residual value is a current forecast of the residual value.

Service life

The period of usefulness of a tangible capital asset (or group of assets) to its current owner. The period may be expressed in units of time or output. The estimated service life of a tangible capital asset is a current forecast of its service life and is the period over which depreciation cost is to be assigned.