

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

ACQUISITION PROCESS FOR
METALWORKING MACHINERY

Report No. 96-087

March 26, 1996

Department of Defense

Additional Copies

To obtain additional copies of this audit report, contact the Secondary Reports Distribution Unit of the Analysis, Planning, and Technical Support Directorate at (703) 604-8937 (DSN 664-8937) or FAX (703) 604-8932.

Suggestions for Future Audits

To suggest ideas for or to request future audits, contact the Planning and Coordination Branch of the Analysis, Planning, and Technical Support Directorate, at (703) 604-8939 (DSN 664-8939) or FAX (703) 604-8932. Ideas and requests can also be mailed to:

OAIG-AUD (ATTN: APTS Audit Suggestions)
Inspector General, Department of Defense
400 Army Navy Drive (Room 801)
Arlington, Virginia 22202-2884

Defense Hotline

To report fraud, waste, or abuse, contact the Defense Hotline by calling (800) 424-9098; by sending an electronic message to Hotline@DODIG.OSD.MIL; or by writing to the Defense Hotline, The Pentagon, Washington, D.C. 20301-1900. The identity of each writer and caller is fully protected.

Acronyms

DLA	Defense Logistics Agency
DGSC	Defense General Supply Center
DIPEC	Defense Industrial Plant Equipment Center



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884



March 26, 1996

MEMORANDUM FOR DEPUTY UNDER SECRETARY OF DEFENSE
(LOGISTICS)

SUBJECT: Audit Report on the Acquisition Process for Metalworking Machinery
(Report No. 96-087)

We are providing this audit report for information and use. We conducted the audit in response to a request from the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management). Comments on a draft of this report were considered in preparing the final report.

Comments on the draft of this report conformed to the requirements of DoD Directive 7650.3 and left no unresolved issues. Therefore, no additional comments are required.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Thomas D. Kelly, Audit Project Manager, at (215) 737-3886. See Appendix E for the report distribution. A list of the audit team members is located on the inside back cover of this report.

A handwritten signature in cursive script that reads "Robert J. Lieberman".

Robert J. Lieberman
Assistant Inspector General
for Audit

Office of the Inspector General, DoD

Report No. 96-087
(Project No. 5LD-5036)

March 26, 1996

Acquisition Process for Metalworking Machinery

Executive Summary

Introduction. This audit was performed as a result of a request from the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management). Metalworking machinery includes large, expensive, precision machines and accessories primarily used by air logistics centers, arsenals, and shipyards to change the physical properties of materials in producing and maintaining defense hardware. The acquisition process for metalworking machinery has been centralized with the Defense General Supply Center (DGSC), Defense Logistics Agency since October 1, 1992. In FY 1994, DGSC spent \$2.2 million to operate a centralized procurement office for acquisition of metalworking machinery. It also spent \$10.3 million to operate a rebuild facility and to maintain an inventory of reparable machinery for rebuild. During FY 1994, DoD acquisitions of metalworking machinery totaled about \$53.8 million.

Audit Objectives. The audit objective was to evaluate the economy and efficiency of the acquisition process for metalworking machinery. We also reviewed the adequacy of the management control program as it applied to the stated objective.

Audit Results. Centralized procurement of metalworking machinery was not economical and efficient; however, centralized rebuild services were economical and efficient when used in lieu of new procurement. Specifically:

- o DoD creation of a central procurement office at DGSC to buy reparable metalworking machinery, in addition to the local procurement offices already established by Military Departments, has proven to be an uneconomical decision. As a result, much of the acquisition services that DGSC performed at an annual cost of \$2.8 million in FY 1995 could have been performed by the Military Departments with no degradation in services and at less overall cost to DoD (Finding A).

- o Military Department customers often did not examine the capability of DGSC rebuild services before they bought new metalworking machinery. As a result, Military Department customers procured new metalworking machinery when suitable rebuilt machinery could have been acquired at substantially less cost (Finding B).

Recommendations in this report, if implemented, will help to make the acquisition process for metalworking machinery more economical and efficient. However, the monetary benefits were undeterminable. Appendix C summarizes the potential benefits of the audit.

Summary of Recommendations. We recommend that the Deputy Under Secretary of Defense (Logistics) direct the Military Departments to procure metalworking machinery locally if it is more advantageous to the Government. We also recommend that the Deputy Under Secretary of Defense (Logistics) direct the Defense Logistics Agency to issue procedures for using the rebuild services of DGSC and instruct the Military Departments to use the rebuild services whenever practical.

Management Comments. The Deputy Under Secretary of Defense (Logistics) concurred with the intent of the recommendation to expand the Military Departments' use of local procurement. However, as an alternative, the Deputy Under Secretary requested that the Military Departments change their regulations to remove restrictions to local purchase authority not intended by the Defense Federal Acquisition Regulation Supplement. The Deputy Under Secretary concurred with the recommendation to use rebuild services of DGSC, when practicable; and requested that the Defense Logistics Agency and the Military Departments work together to issue formal procedures for using rebuild services, when practicable. See Part I of the report for a discussion of management comments and Part III for the complete text of management comments.

Table of Contents

Executive Summary	i
Part I - Audit Results	
Audit Background	2
Audit Objectives	2
Finding A. Centralized Acquisition	3
Finding B. Rebuild Services	10
Part II - Additional Information	
Appendix A. Audit Process	16
Scope and Methodology	16
Management Control Program	17
Appendix B. Chronology of Major Events in Establishing a Centralized Acquisition Process for Metalworking Machinery	19
Appendix C. Summary of Potential Benefits Resulting From Audit	22
Appendix D. Organizations Visited or Contacted	23
Appendix E. Report Distribution	25
Part III - Management Comments	
Deputy Under Secretary of Defense (Logistics) Comments	28

Part I - Audit Results

Audit Background

This audit was performed as a result of a request from the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management). Metalworking machinery includes large, expensive precision machines and accessories primarily used by air logistics centers, arsenals, and shipyards to change the physical properties of materials in producing and maintaining defense hardware. The acquisition process for metalworking machinery has been centralized with the Defense General Supply Center (DGSC), Defense Logistics Agency (DLA) since October 1, 1992. In FY 1994, DGSC spent \$2.2 million to operate a centralized procurement office for acquisition of metalworking machinery. It also spent \$10.3 million to operate a rebuild facility and to maintain an inventory of reparable machinery for rebuild. During FY 1994, DoD acquisitions of metalworking machinery totaled about \$53.8 million.

Audit Objectives

The audit objective was to evaluate the economy and efficiency of the acquisition process for metalworking machinery. We also reviewed the adequacy of the management control program as it applied to the stated objective. See findings for a discussion of the material management control weaknesses we identified and Appendix A for the audit scope and methodology and the management control program.

Finding A. Centralized Acquisition

The DoD creation of a central procurement office at DGSC to buy repairable metalworking machinery, in addition to the local procurement offices already established by the Military Departments, has proven to be an uneconomical decision. The central procurement office had not offset its cost of operations with savings from quantity discount buys, even though the Military Departments had often used its services when local procurement was more appropriate. As a result, much of the acquisition services that DGSC performed at an annual cost of about \$2.8 million in FY 1995 could have been performed by the Military Departments with no degradation in services and at less overall cost to DoD.

Basis for Central Procurement

DGSC Designation. In 1991, the then Assistant Secretary of Defense (Production and Logistics) designated DLA and, in turn, DGSC to manage metalworking machinery. With that designation, the Military Departments, which had previously acquired their metalworking machinery locally after first checking with the Defense Industrial Plant Equipment Center (DIPEC) for available equipment in reserve, were now to acquire their metalworking machinery through DGSC. Savings from centralized acquisition were to be realized by an estimated 5-percent quantity buy discount. The Military Departments argued against the change in acquisition processing and have not implemented it uniformly. A chronology of major events pertaining to the metalworking acquisition process, beginning with the establishment of DIPEC in 1962, is in Appendix B.

Acquisition Services. In FY 1994, DGSC spent about \$2.2 million to perform its central acquisition mission. In FY 1995, central acquisition costs rose to \$2.8 million, and DGSC began to convert and maintain technical documents. As shown in Figure 1, central acquisition involves procuring metalworking machinery as well as performing financial services, rendering legal and other management assistance, ensuring the quality of purchased machinery, standardizing technical documents, performing supply services, and preparing technical data.

Finding A. Centralized Acquisition

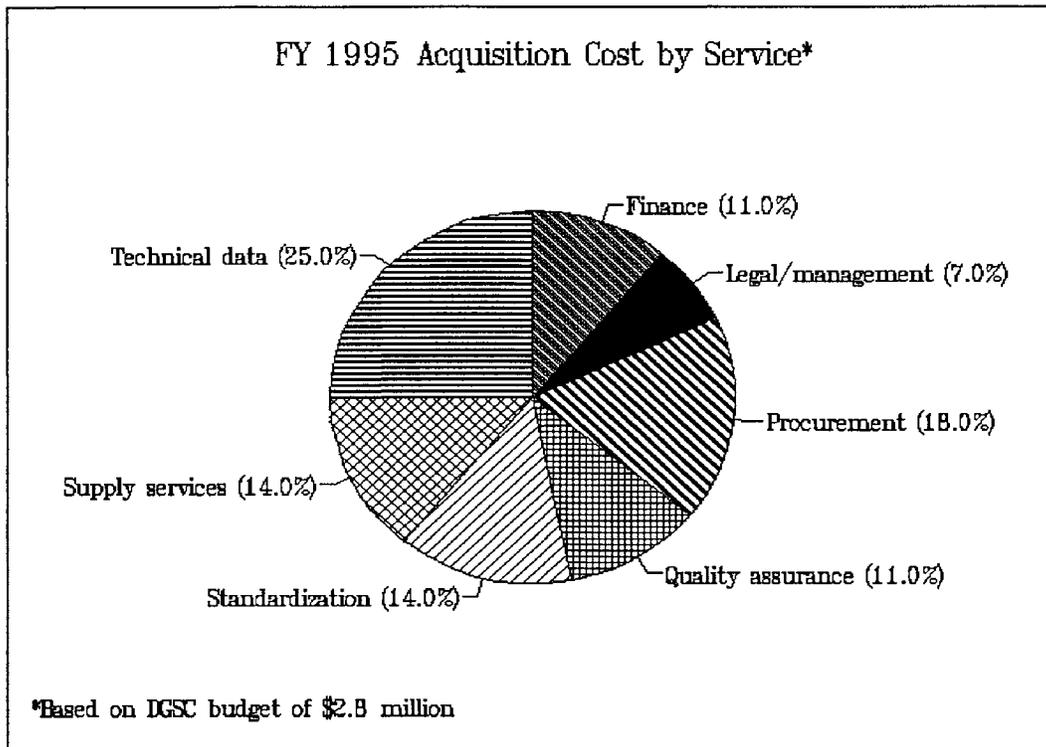


Figure 1. Central Acquisition Costs for Metalworking Machinery

Military Department customers, whether they acquire metalworking machinery centrally or locally, generally perform services comparable to the central procurement office. However, the costs associated with the local procurement services are not captured specifically for metalworking machinery and cannot be directly related to the cost of operations for the central procurement office.

Regulatory Guidance. The Defense Federal Acquisition Regulation Supplement, part 208, establishes required sources for services and supplies. It provides policy and procedures for acquiring commodities used and possibly procured by more than one department or agency or the General Services Administration. Essentially, all such commodities are to be acquired by a single buyer under either the Integrated Materiel Management Program or the Coordinated Acquisition Program. Within DLA, the Integrated Materiel Management Program mostly applies to nationally stock-numbered, consumable items although reparable items are not excluded by definition. Integrated materiel management includes budgeting, cataloging, computing requirements, contracting, funding, issuing, standardizing, and storing. The Coordinated Acquisition Program strictly relates to contracting and primarily applies to items not covered by the Integrated Materiel Management Program. DGSC is the acquiring department for all 37 classes of metalworking machinery under both the Integrated Materiel Management Program and the Coordinated Acquisition Program. Although DGSC is the designated acquiring department, the Defense Federal Acquisition Regulation Supplement provides numerous exceptions to

centralized procurement. In FY 1994, DoD acquisitions of reparable metalworking machinery totaled about \$53.8 million. Of that amount, \$36.8 million (68 percent) was awarded by local procurement offices and \$17 million (32 percent) was awarded by DGSC.

Economy and Efficiency of Centralized Procurement

Decision to Centralize. The DoD creation of a central procurement office at DGSC to buy reparable metalworking machinery, in addition to the local procurement offices already established by the Military Departments, has proven to be an uneconomical decision. Because contracts for metalworking machinery make up only a fraction of workload at a local procurement office, no local procurement offices were eliminated as a result of the creation of the central procurement office. Additionally, because customers must still perform acquisition services even if the award is made centrally, the central procurement office's acquisition services of legal, financial, quality assurance, supply, technical, and other management assistance can become somewhat duplicative or provide additional layers in the acquisition process. In effect, DoD was spending more to acquire reparable metalworking machinery than when only the Military Departments were acquiring it in FY 1992.

Cost-effectiveness Factors. To evaluate the cost-effectiveness of the central procurement decision, we evaluated whether the central procurement office had produced reasonable economies and efficiencies by outperforming the local procurement offices or otherwise achieving dollar savings. We selected for review 37 procurement actions (\$12.2 million) of the central procurement office and 21 procurement actions (\$8 million) of the two local procurement offices acquiring the most metalworking machinery for the Military Departments: Rock Island Arsenal and Warner Robins Air Logistics Center. Our review of DD Form 350, "Individual Contract Action Reports," and contract files showed that the central procurement office performed at least as well as the two local procurement offices but not with a marked increase in economy and efficiency. Specifically:

- o both the central and local procurement offices used a negotiated procurement process. Under that process, an award could be made to the offeror who makes the most favorable proposal if no negotiations are needed. If negotiations are needed, all offerors still within the competitive range are asked to submit best and final offers. Award is made to the offeror who makes the most advantageous offer to the Government.

- o both the central and local procurement offices used firm-fixed-price contracts.

- o the central procurement office had a 69-percent success rate in soliciting competition compared to the local procurement offices' 84-percent success rate. However, compared to the central procurement office sole-source

Finding A. Centralized Acquisition

procurement of about \$64,000, the local procurement offices procured about \$113,000 of machinery sole-source . Because the central and local procurement offices performed similarly, the only economy and efficiency advantage of a central procurement office was its potential for generating quantity discounts by consolidating the requirements of different customers.

Savings from Quantity Discount Buys

The central procurement office at DGSC has not offset its cost of operations with savings from quantity discount buys. DLA, in justifying the establishment of a central procurement office, indicated that at least 5 percent savings could be achieved from quantity discounts. The quantity discounts were to be earned by consolidating the buys of different users of the same metalworking machinery. To offset its cost of operations, the central procurement office would have to consolidate requirements of \$56.7 million a year at the DLA estimated 5-percent savings rate. However, requirements for metalworking machinery declined and were not enough to consolidate centrally and to achieve significant savings through quantity discounts.

Total Requirements. Total requirements for reparable metalworking machinery were below \$56.7 million a year and were decreasing. As with most DoD operations, budget-cutting and force structure reductions have affected metalworking machinery requirements. In FY 1993, 511 procurements of reparable metalworking machinery, valued at \$76.1 million, were made. In FY 1994, procurements had slipped to 291 at a cost of \$53.8 million. For the first half of FY 1995, only 93 procurements for metalworking machinery, valued at \$15.1 million, were made. Because total requirements have decreased to about \$30 million a year, the cost of operating the central procurement office cannot be recovered through quantity discounts of 5 percent. If the central procurement office could consolidate \$30 million of requirements into one buy, the savings would still be \$1.3 million less than the cost of its operations.

Consolidated Requirements. The number of requirements that could be consolidated was very small and unlikely to produce meaningful savings. DGSC information showed that the central procurement office did not consolidate requirements for any purchases of reparable metalworking machinery over the 18-month period we reviewed. The 384 procurement actions awarded during the 18-month period ending March 31, 1995, involved 31 of the 37 Federal supply classes of metalworking machinery. Only 5 of the 31 Federal supply classes averaged more than 1 buy over \$25,000 a month. To determine the potential for consolidated procurement, we assumed that any DoD procurement office could consolidate metalworking requirements. We selected for review two of the five Federal supply classes with the most actions and highest dollar amount of awards, 3416, lathes and 3445, punching machines. Together, lathes and punching machines made up 76 (20 percent) of the 384 procurement actions and \$24.9 million (36 percent) of the \$69 million of

Finding A. Centralized Acquisition

metalworking machinery procured. From these totals, we subtracted \$21.9 million (88 percent) of procurement actions that were not or could not have been consolidated because they were awarded:

- o as delivery orders on general supply contracts,
- o as modifications to existing contracts, or
- o for unique requirements.

Technical information was not readily available to determine whether any of the remaining 25 procurement actions (13 for \$1.9 million of lathes and 12 for \$1.1 million of punching machines) could have or actually had been consolidated. However, the 25 procurement actions were spread over 17 months and ranged in value from \$28,000 to \$457,000. Thus, it was likely that few, if any, of the procurement actions contained consolidated requirements for lathes and punching machines. Unless metalworking machinery requirements increase substantially, the potential for consolidated buys and savings will remain very low.

The benefit of DoD centrally consolidating requirements may be even less in the future as the General Services Administration has expanded its offerings of United States-made metalworking machinery through multiple award schedules. In August 1995, we scanned the Commerce Business Daily for the 3-month period ending March 31, 1995, and identified 75 awards that DoD organizations proposed for metalworking machinery. With the help of personnel from the General Services Administration, we identified 33 (44 percent) of the 75 proposed awards that could be satisfied in August (assuming they were still not awarded by that time) by merely placing delivery orders with the General Services Administration schedule contracts, thus greatly reducing the customers' procurement process. All schedule contracts were awarded on a competitive basis and contained either list price discounts or incentives for quantity discounts. Therefore, DGSC had generated very little, if any, quantity discount savings to offset the cost of its operations and, in view of the General Services Administration expanded supply schedule, will have even less opportunity in the future.

Customer Base

The customer base of the central procurement office has been sustained, in part, by customers who feel compelled to use its services. The customer base would have been lower had the customers freely cited the Defense Federal Acquisition Regulation Supplement before acquiring metalworking machinery. Although the Defense Federal Acquisition Regulation Supplement requires commodities to be acquired by a single manager under either the Integrated Materiel Management Program or the Coordinated Acquisition Program, it provides numerous exceptions. The Integrated Materiel Management Program allows three exceptions to single manager or central procurement. For example, customers do not have to acquire commodities from the single manager:

- o under circumstances of unusual and compelling urgency and

Finding A. Centralized Acquisition

- o when the combination of cost, timeliness, and quality, makes satisfying the requirement locally in the best interest of the Government.

The Coordinated Acquisition Program allows 13 exceptions to central procurement. For example, customers do not have to acquire commodities from the single manager:

- o when requirements do not exceed \$100,000 and local procurement is in the best interest of the Government, and

- o if the acquisition is a one-time buy of a noncataloged item.

Although the exceptions in the Defense Federal Acquisition Regulation Supplement are designed to give customers a wide latitude in selecting the most economical method of acquisition, many customers were restricted from using them.

Latitude in Selecting Method of Acquisition. The exceptions to central procurement give customers a wide latitude in acquiring commodities, especially as waivers are not needed to proceed with local procurement when in the best interest of the Government and requirements do not exceed \$100,000. Nevertheless, customers have been hesitant to cite the exceptions, when applicable, and to acquire metalworking machinery locally. In June 1995, we met with Military Department representatives who had been active in acquiring metalworking machinery. The representatives were from the Army Rock Island and Watervliet Arsenal, the Navy Air and Sea Commands, and the Air Force Warner Robins Air Logistics Center. Only Army customers consistently cited exceptions to acquiring metalworking machinery centrally. Their acquisitions were one-time buys of noncataloged items. Representatives of the Navy and Air Force told us that they had to acquire all metalworking machinery centrally. The representatives provided us with letters from their respective headquarters essentially noting that DGSC had been designated the single manager for metalworking machinery. The letters did not specifically prohibit Navy and Air Force customers from citing exceptions authorized by the Defense Federal Acquisition Regulation Supplement, if applicable. Whether the customers of repairable metalworking machinery could have cited exceptions, they have often gone through the central procurement office when it may have been more economical and efficient to procure locally. Recent DoD studies, changes to the Defense Federal Acquisition Regulation Supplement, and other initiatives are based on the premise that local procurement can often be advantageous and less expensive to the Government.

Representative Claims. Each of the representatives believed that most repairable metalworking machinery should be acquired locally. In support of their positions, the representatives claimed that local procurement:

- o allows for easier technical coordination among customers, procurement personnel, and contractors;

- o costs customers less to award; and
- o results in customers obtaining urgently needed equipment faster.

The claims of the representatives could not be substantiated across the board for all items acquired. For example, the cost of the services from the central procurement office to customers was directly and clearly documented in a surcharge rate -- from 7 to 13 percent for each item bought in FY 1995 up to \$1 million. In contrast, the cost of local procurement was not directly identified to the items bought but was hidden within various activity and expense accounts of the local organization. Nevertheless, the claims of the Military Department representatives often seemed reasonable on an item by item basis but were not used to cite exceptions to central procurement.

Recommendation and Management Comments

A. We recommend that the Deputy Under Secretary of Defense (Logistics) direct the Military Departments to procure metalworking machinery (Federal supply group 34) locally if it is more advantageous to the Government or if the acquisition falls under the umbrella of exceptions to central procurement authorized by the Defense Federal Acquisition Regulation Supplement.

Management Comments. The Deputy Under Secretary concurred with the intent of the recommendation, and proposed an alternate method that would allow the Military Departments more flexibility in the use of local procurement. The alternate action requested that the Military Departments remove their restrictions on local purchase authority, and allow local procurement up to the new threshold of \$100,000 established by the Defense Federal Acquisition Regulations Supplement.

Finding B. Rebuild Services

Military Department customers often did not examine the capability of DGSC rebuild services before they bought new metalworking machinery. Procedures for examining the capability of the rebuild services were not formalized and made known to all Military Department customers. As a result, Military Department customers procured new metalworking machinery when suitable rebuilt machinery could have been acquired at substantially less cost.

Sources of Services

From 1962 to 1992, DIPEC provided rebuild services for reparable machinery. The main purpose of the rebuild services was to give Military Department customers an option of rebuilding industrial plant equipment instead of procuring new machinery. The customers could have DIPEC rebuild either their own machinery or replacement machinery from the general reserve of plant equipment. Procedures for obtaining rebuild services were contained in Defense Logistics Agency Manual 4215.1, "Management of Defense-Owned Industrial Plant Equipment," November 26, 1991. Rebuild is described as:

Restoring a machine to the original or like-new condition meeting or exceeding the original accuracy, performance, life-expectancy and external appearance. During rebuild the machine is disassembled to the basic castings, parts cleaned, repaired, or replaced as required. The machine is also updated electrically to meet all current occupational safety and health administration requirements as they apply to the individual item.

When DGSC assumed the responsibilities of DIPEC in October 1992, DoD had decided to reduce the general reserve to reparable metalworking machinery with expected demands. By the end of FY 1995, the reparable inventory or rebuild machinery candidates consisted of about 900 line items, while the rebuild facilities had a staff of 129 technicians capable of restoring a piece of machinery to its original condition or to a state of the art condition. In FY 1995, the cost of operating the rebuild facilities and maintaining a reparable inventory of rebuild candidates totaled about \$11.2 million. How economically and efficiently these resources are put to use depends on whether Military Department customers consider rebuilding as a alternative to new acquisition.

Economy and Efficiency of Rebuild Services

Military Department customers often did not examine the capability of DGSC rebuild services before buying new metalworking machinery. According to DD Form 350 and information available at DGSC, DoD either purchased or rebuilt 372 metalworking pieces of machinery in FY 1994. The 372 pieces would have cost \$81.3 million if they were all purchased. DGSC satisfied 105 of the requirements through purchases of new machinery at a cost of \$17 million and 81 others through rebuild at a cost of \$14.4 million or \$13.1 million less than if the machinery had been procured. In effect, rebuilding resulted in a saving of 29.5 percent on total potential acquisitions of \$44.5 million processed through central procurement. Military Department customers satisfied the remaining 186 requirements solely through local purchases at a cost of \$36.8 million. Thus, as shown in Figure 2, only the Military Department customers who sought centralized procurement services from DGSC were formally offered an acquisition alternative to new procurement -- that is, rebuild either their own machinery or an available piece from the reparable inventory. In contrast, the Military Department customers who contracted locally did not formally consider using the DoD resources established for reducing acquisition costs.

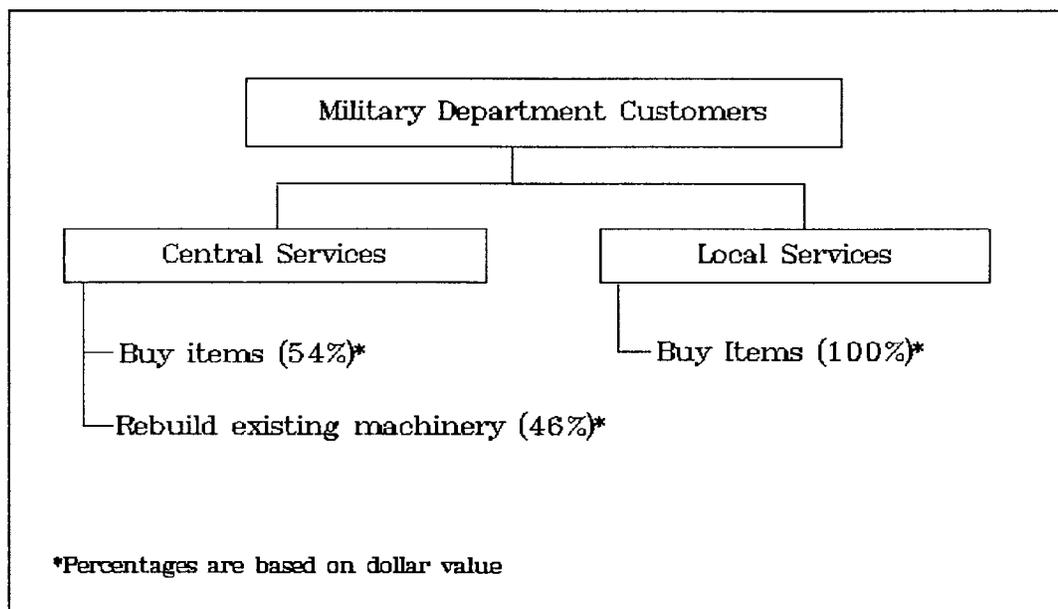


Figure 2. Options for Acquiring Metalworking Machinery

Procedures for Obtaining Rebuild Services

Procedures for examining the capability of DGSC rebuild services were not

Finding B. Rebuild Services

formalized and made known to Military Department customers. DoD materiel management policy is to satisfy reparable machinery requirements by repair first, if economical. This policy, along with related procedures were stated in detail for industrial plant equipment in DLA Manual 4215.1. However, with the disestablishment of DIPEC in 1992, the regulation became inoperative. Consequently, DLA drafted a new manual that again spelled out the procedures for obtaining rebuild services, but the Military Departments had not agreed to the manual. The primary disagreement the Military Departments had with the manual was with the requirement to purchase all metalworking machinery centrally at DGSC (see Appendix B for additional details).

The Military Department customers examined the capability of DGSC rebuild services when they processed their procurement requirements centrally and when DGSC requested formal consideration before contracting for the new machinery. When the Military Department customer contracted for metalworking machinery locally, the rebuild services of DGSC were not formally examined for capability. During the 3-month period ending March 31, 1995, the Commerce Business Daily listed 75 proposed DoD purchases of metalworking machinery, of which 16 Military Department customers were to award 23 locally. We contacted the 16 customers and determined that none had examined the capability of the rebuild services of DGSC. In fact, 8 of the 16 customers were not even aware of the rebuild services of DGSC. For example, the Army Corps of Engineers at Vicksburg, Mississippi, published a proposed buy of an automatic surface grinder in the February 15, 1995, Commerce Business Daily. Responsible personnel at the Corps of Engineers told us they were unaware of the rebuild services of DGSC and would pursue rebuilding rather than disposing of the old machine.

Rebuilding Costs Less

The Military Departments procured new metalworking machinery when restored machinery may have done the job at substantially less cost. According to studies published by the General Accounting Office and private industry, rebuilding costs about 50 percent less than new procurement. The rebuild facilities of DGSC have generated about the same savings as substantiated by DGSC for both machinery provided by the customer and machinery drawn from the reparable reserve.

Customer Machinery. Using customer machinery, in FY 1994, DGSC rebuilt 27 metalworking machines at a cost of \$10.5 million. If purchased, the machines would have cost \$19.3 million or \$8.8 million more. For example, Holloman Air Force Base required a horizontal boring mill. A commercial

supplier quoted a price of \$1.1 million for a new mill. However, instead of contracting with the supplier, Holloman Air Force Base requested the services of DGSC which:

- o disassembled, blocked, and braced the serviceable machine,
- o transported the serviceable machine to the rebuild facility,
- o rebuilt and retrofitted new controls into the serviceable machine,
- o transported the rebuilt machine back to Holloman,
- o reassembled and tested the rebuilt machine, and
- o trained Holloman personnel on the rebuilt machine.

The rebuild service cost about \$0.6 million, thereby saving Holloman about \$0.5 million.

Reparable Reserve. Using machinery drawn from the general reserve, in FY 1994, DGSC rebuilt 54 metalworking machines at a cost of \$3.9 million. If purchased, the machines would cost \$8.2 million or \$4.7 million more. For example, the Warner Robins Air Logistics Center required a toolmaker's grinder. A commercial supplier quoted a price of \$68,900 for a new grinder but it included undesirable special attachments. The Warner Robins Air Logistics Center accepted the DGSC proposal to rebuild a serviceable grinder from its reparable inventory. The rebuild services cost \$42,000, thereby saving Warner Robins Air Logistics Center \$26,900.

If the Military Department customers had achieved the same percentage of rebuilds and savings as those customers who procured centrally through DGSC, we estimated that an additional \$10.9 million could have been saved in FY 1994. Although not all machinery requirements can or should be satisfied by rebuild, rebuild should be considered. Unless customers are required to examine the capability of the DGSC rebuild services, significant savings could be lost and economical and efficient use of dedicated DoD resources will not be made.

Recommendations and Management Comments

B. We recommend that the Deputy Under Secretary of Defense (Logistics):

1. Direct the Defense Logistics Agency, in coordination with the Military Departments, to issue formal procedures for using the rebuild services of the Defense General Supply Center.
2. Direct the Military Departments to formally evaluate the capability of the Defense General Supply Center rebuild services whenever practicable before acquiring new metalworking machinery.

Finding B. Rebuild Services

Management Comments. The Deputy Under Secretary concurred with the recommendations, and stated that a memorandum addressing the recommendations had been sent to the Military Departments. The memorandum requested that the Defense Logistics Agency and the Military Departments work together to issue formal procedures for using the rebuild services of DGSC, when practicable.

Part II - Additional Information

Appendix A. Audit Process

Scope and Methodology

We evaluated the economy and efficiency of the acquisition process for metalworking machinery primarily at DGSC and at selected organizations within the Military Departments.

We obtained all DD Forms 350 for reparable metalworking machinery contracted for in FYs 1993 and 1994 and the first half of FY 1995. DD Forms 350 contain contractual information on acquisitions over \$25,000. During the 18-month period, DoD made 384 separate buys for \$69 million of reparable metalworking machinery. The central procurement office awarded 149 of the buys for \$24.2 million. Local procurement offices within the Military Departments awarded 235 of the buys for \$44.8 million. In using DD Form 350 information, we manually excluded consumable acquisitions over \$25,000. We could not ascertain exact figures on the number of buys and dollar values because metalworking machinery could be acquired for less than \$25,000. However, we do not believe that such additions would be significant enough to materially alter our figures or conclusions.

Using information from DD Form 350 and contract files for the same 18-month period, we determined whether the central procurement office had produced reasonable economies and efficiencies by outperforming the local procurement offices or otherwise achieving dollar savings and whether the Military Departments had adequately considered the rebuild facilities of the Defense General Supply Center. We held discussions with responsible personnel from major logistics commands and users of metalworking machinery within the Military Departments.

For our detailed review of performance, we selected 37 procurement actions (\$12.2 million) of the central procurement office and 21 procurement actions (\$8 million) of the two local procurement offices acquiring the most metalworking machinery for the Military Departments, Rock Island Arsenal and Warner Robins Air Logistics Center. While DD Form 350 and contract files were our primary source of analyzing savings and use of rebuild facilities, we also obtained and reviewed copies of the January through March 1995 issues of the Commerce Business Daily. We reviewed the Commerce Business Daily to determine whether the machinery being procured was also offered on General Services Administration schedule contracts and to determine customer awareness of the rebuild program for metalworking machinery. We held discussions with responsible personnel from the General Services Administration and 16 procurement offices within the Military Departments. In reviewing the rebuild program, we limited our scope to transactions that DGSC completed. We also queried Military Department customers on their satisfaction with the program. We did not use statistical sampling techniques to conduct this audit.

Computer-Processed Data. We verified information sampled from computer-

processed DD Forms 350 to contract files. We identified no significant errors and concluded that the information sampled was reliable.

Prior Audits and Other Reviews. No audits or reviews have been conducted of the acquisition process for metalworking machinery since it was centralized under DGSC on October 1, 1992.

Audit Period, Standards, and Locations. This economy and efficiency audit was made from April through September 1995. The audit was made in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD. Accordingly, we included tests of management controls considered necessary. A complete list of organizations visited or contacted is in Appendix D.

Management Control Program

DoD Directive 5010.38, "Internal Management Control Program," April 14, 1987 requires DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls.

Scope of Review of Management Control Program. We reviewed the adequacy of DGSC management controls over the process used to acquire metalworking machinery. We did not review the adequacy of Military Department management controls over the process used to acquire metalworking machinery because program responsibility had been centralized within DGSC.

Adequacy of Management Controls. The DGSC management control program was not adequate as it related to the acquisition of metalworking machinery. The DGSC management control program did not specifically address the metalworking machinery acquisition process and did not provide procedural controls for ensuring an economical and efficient acquisition process with the Military Departments under a centralized concept. Recommendations in this report, if implemented, will ensure that the process the Military Departments use to procure and rebuild metalworking machinery would be more economical and efficient. We could not determine the amount of potential monetary benefits because of unknown future requirements and other uncertain factors. See Appendix C for all benefits associated with the audit.

Adequacy of Management's Self Evaluation. The DGSC self-evaluation of the centralized acquisition process for metalworking machinery was not adequate. No self-evaluations have been performed and key internal control procedures contained in Defense Logistics Agency Manual 4215.1 have not been updated, since the metalworking machinery acquisition process was centralized under DGSC on October 1, 1992. DGSC performed a risk

Appendix A. Audit Process

assessment of the acquisition process in FY 1994 but it covered only basic procurement duties. Concerns about program results and relationships with the Military Departments were not covered.

Appendix B. Chronology of Major Events in Establishing a Centralized Acquisition Process for Metalworking Machinery

In 1962, DoD established DIPEC in Memphis, Tennessee, to coordinate the purchase and disposal of industrial plant equipment within the Military Departments and to repair, rebuild, and overhaul the equipment for reutilization when appropriate. Under the control and direction of DLA, DIPEC became the central clearinghouse in DoD for plant equipment purchases and disposals by Military Departments. The change to centralizing the acquisition responsibility within DGSC began with the establishment of the Defense Depot Maintenance Council (the Council) in 1990. The Military Departments resisted the change to centralized acquisition, culminating in the Assistant Under Secretary of Defense (Materiel and Distribution Management) requesting the Inspector General, DoD, to review the centralized acquisition process in 1995.

June 30, 1990. The Deputy Secretary of Defense established the Council, chaired by the then Assistant Secretary of Defense (Production and Logistics). The Assistant Secretary included as members representatives from DLA and each of the Military Departments. One of the main purposes of the Council was to improve depot maintenance operations throughout DoD. DLA was designated the lead activity to review the full range of industrial plant equipment management, with team participation from all Military Departments.

November 17, 1990. The Deputy Secretary of Defense approved Defense Management Report Decision 995. It stated that consolidations, proposed by either DLA or the Army, could be accomplished to reduce costs and improve industrial plant equipment management. Costs were to be reduced by implementing one of three alternatives:

- o save \$21 million over 6 years by implementing recommendations anticipated from the Council.

- o save \$18.5 million over 6 years by implementing DLA recommendations to assume management of industrial plant equipment and to close Seneca Army Depot and transfer its work load to DIPEC.

- o save \$20 million over 6 years by implementing the Army's recommendations to allow the Military Departments to manage their own industrial plant equipment and to disestablish DIPEC.

The Deputy Secretary of Defense approved the Army's estimate of savings but referred the issue of which alternative to be selected to the Assistant Secretary, with the advice of the Council.

Appendix B. Chronology of Major Events

January 1 and February 1, 1991. DLA and the Military Departments issued reports representing the results of the Council review of industrial equipment management. Only DLA signed the first report, which identified yearly savings of \$8.8 million based on implementing eight recommendations. The key recommendation involved centralizing the acquisition of industrial plant equipment at DIPEC. Savings from centralized acquisition were estimated at \$4.9 million a year and were to be realized from consolidating buys (5 percent times the FY 1989 procurement program of \$98.6 million). Each of the Military Department signed the second report. It identified yearly savings of \$20.5 million based on disestablishing DIPEC and centralizing the acquisition of industrial plant equipment within the Military Departments.

February 28, 1991. The Assistant Secretary approved the Defense Depot Maintenance Council Joint Service Business Plan to improve depot maintenance operations throughout DoD. The Plan consisted of 21 commodity studies. The study on industrial plant equipment noted that DLA and the Army disagreed on how to manage industrial plant equipment. In those areas where DLA and the Military Departments agreed, the study recommended a reduction in industrial plant equipment to Federal supply group 34 (metalworking machinery), and to:

- o increase the threshold of industrial plant equipment from \$5,000 to \$15,000,
- o phase out plant equipment codes and use national stock numbers to identify industrial plant equipment,
- o use standard commercial specifications to procure industrial plant equipment instead of military specifications, and
- o eliminate manual reporting of the status of industrial plant equipment in the hands of users.

The study recommended additional tests and analyses be performed in areas of disagreement. For example, regarding the general reserve, the Military Departments and DLA were to conduct a scrub of assets to determine those with the potential for future use. Regarding consolidation of depot maintenance, the industrial plant equipment study group was to conduct a cost analysis of supporting six Army items at Seneca Army Depot versus DIPEC facilities. Regarding centralized acquisition, DIPEC and DLA were to conduct a 1-year test of industrial plant equipment acquisitions to determine the potential for consolidating procurement requirements.

June 12, 1991. At a Council meeting, DLA showed that \$22.1 million could be saved from FY 1992 to FY 1997 by consolidating the Seneca Army Depot work load with DLA facilities. DLA also expressed the opinion that without the 1-year test of the potential for consolidating procurement requirements recommended by the Defense Maintenance Council, it should be the integrated material manager for industrial plant equipment.

Appendix B. Chronology of Major Events

July 25, 1991. The Assistant Secretary confirmed that all industrial plant equipment depot maintenance would be consolidated into DLA facilities. Subsequently, on August 1, 1991, the Assistant Secretary designated DLA as the single DoD integrated materiel manager of industrial plant equipment, Federal supply group 34. On May 19, 1992, the Assistant Secretary designated DLA as the single manager or consolidated materiel manager for Federal supply group 34 consumables as well as reparable.

October 1, 1992. DLA integrated the inventory control point and item manager functions for both new procurement of metalworking machinery and management of the general reserve into the DLA supply business area at DGSC. The former headquarters of DIPEC was also functionally realigned under the DGSC and, on a transitional basis, provided on-site technical support.

November 2, 1992. The Assistant Secretary directed DLA to reduce or eliminate the general reserve of industrial plant equipment. On March 10, 1993, DLA informed the Assistant Secretary that it had eliminated the general reserve and had established a demand-based reparable inventory.

March 16, 1995. DLA expressed concern about local purchases of metalworking machinery and requested the assistance of the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management) in getting the Military Departments to furnish their metalworking machinery requirements to DGSC. On March 24, 1995, the Deputy Under Secretary requested the Inspector General, DoD, to review the issue of the Military Departments purchasing metalworking machinery locally.

Appendix C. Summary of Potential Benefits Resulting From Audit

Recommendation Reference	Description of Benefit	Amount and Type of Benefit
A.	Economy and Efficiency. An increase in local procurement of metalworking machinery should result in reduced staffing at the central procurement office and more efficient use of DoD resources.	Undetermined. The large number of local procurement offices and the varying services provided, coupled with unknown metalworking machinery requirements, makes predicting future acquisition work loads and savings highly speculative.
B.1. and B.2.	Program Results. Potential Benefits should result from rebuilding metalworking machinery instead of new procurement. For every acquisition dollar central procurement received, rebuilding resulted in a 29.5 percent savings.	Undetermined. Future metalworking machinery requirements are not summarized within the Military Departments and are largely unpredictable by type, quantity, and dollar value.

Appendix D. Organizations Visited or Contacted

Office of the Secretary of Defense

Deputy Under Secretary of Defense (Materiel and Distribution Management),
Washington, D.C.

Department of the Army

Aviation and Troop Support Command, Saint Louis, MO
Corps of Engineers, Baltimore District, Baltimore, MD
Corps of Engineers, Huntington District, Huntington, WV
Corps of Engineers, Louisville District, Louisville, KY
Corps of Engineers, Nashville District, Nashville, TN
Corps of Engineers, Pittsburgh District, Pittsburgh, PA
Corps of Engineers, Waterways Experiment Station, Vicksburg, MS
Aberdeen Proving Ground, Aberdeen, MD
Fort Bragg, NC
Industrial Operations Command, Rock Island Arsenal, Rock Island, IL
Red River Army Depot, Texarkana, TX
Tobyhanna Army Depot, Tobyhanna, PA
Watervliet Arsenal, Watervliet, NY

Department of the Navy

Naval Air Systems Command, Arlington VA
Naval Sea Systems Command, Arlington, VA
Fleet and Industrial Supply Center, Puget Sound, Bremerton, WA
Naval Industrial Resources Support Office, Philadelphia, PA
Naval Ordnance Station, Louisville, KY
Naval Surface Force, Pacific Fleet, San Diego, CA
Naval Supply Security Office, Arlington, VA
Plant Equipment Support Office, Norfolk, VA
Ships Parts Control Center, Mechanicsburg, PA

Appendix D. Organizations Visited or Contacted

Department of the Air Force

Oklahoma City Air Logistics Center, Tinker Air Force Base (AFB), OK
Sacramento Air Logistics Center, McClellan AFB, CA
Warner Robins Air Logistics Center, Robins AFB, GA
20th Contracting Squadron, Shaw AFB, SC
27th Contracting Squadron, Cannon AFB, NM
30th Contracting Squadron, Vandenberg AFB, CA
47th Contracting Squadron, Laughlin AFB, TX
46th Test Group, Holloman AFB, NM
Air Force Cataloging and Standardization Center, Battle Creek, MI
Hill AFB, UT
Wright-Patterson AFB, OH

Other Defense Organizations

Defense Logistics Agency, Arlington, VA
 Defense Construction Supply Center, Columbus, OH
 Defense General Supply Center, Richmond, VA
 Defense General Supply Center Industrial Plant Equipment Repair Facility,
 Mechanicsburg, PA
Defense Nuclear Agency, Arlington, VA

Non-Defense Federal Organizations

Defense Plant Representative Office, General Dynamics-Lima, Lima, OH (Government
 owned, contractor operated facility)
General Services Administration, Region Seven, Fort Worth, TX

Appendix E. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Acquisition and Technology)
Deputy Under Secretary of Defense (Logistics)
Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management)
Assistant Secretary of Defense (Economic Security)
Director, Defense Logistics Studies Information Exchange
Under Secretary of Defense (Comptroller)
Assistant to the Secretary of Defense (Public Affairs)

Department of the Army

Commander, U.S. Army Materiel Command
Auditor General, Department of the Army

Department of the Navy

Assistant Secretary of the Navy (Financial Management and Comptroller)
Auditor General, Department of the Navy

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)
Auditor General, Department of the Air Force

Other Defense Organizations

Director, Defense Contract Audit Agency
Director, Defense Logistics Agency
Commander, Defense General Supply Center
Director, National Security Agency
Inspector General, National Security Agency

Non-Defense Federal Organizations and Individuals

Office of Management and Budget
General Accounting Office
National Security and International Affairs Division
Technical Information Center

Non-Defense Federal Organizations and Individuals (cont'd)

Chairman and ranking minority member of each of the following congressional committees and subcommittees:

- Senate Committee on Appropriations
- Senate Subcommittee on Defense, Committee on Appropriations
- Senate Committee on Armed Services
- Senate Committee on Governmental Affairs
- House Committee on Appropriations
- House Subcommittee on National Security, Committee on Appropriations
- House Committee on Government Reform and Oversight
- House Subcommittee on National Security, International Affairs, and Criminal Justice, Committee on Government Reform and Oversight
- House Committee on National Security

Part III - Management Comments

Deputy Under Secretary of Defense (Logistics) Comments



ACQUISITION AND
TECHNOLOGY

OFFICE OF THE UNDER SECRETARY OF DEFENSE
3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000



22 FEB 1996

(L/MDM)

MEMORANDUM FOR DOD INSPECTOR GENERAL
THROUGH: CHIEF, CAIR / *AW 23 Feb 96*

SUBJECT: Draft Audit Report, "Acquisition Process for
Metalworking Machinery," Dated December 20, 1995
(Project No. 5LD-5036)

This responds to your memorandum of December 20, 1995, on the subject audit report. This review was conducted at the request of this office, and we appreciate the work done by your staff in performing this review. Two recommendations were addressed to this office. Our detailed comments on those recommendations is included in the attachment.

John F. Phillips
John F. Phillips
Deputy Under Secretary
of Defense (Logistics)

Attachment



"A. We recommend that the Deputy Under Secretary of Defense (Logistics) direct the Military Departments to procure metalworking machinery (Federal supply group 34) locally if it is more advantageous to the Government or if the acquisition falls under the umbrella of exceptions to central procurement authorized by the Defense Acquisition Regulation Supplement."

This office concurs with the intent of this recommendation, and proposes an alternate method to meet the recommendation's goal of seeking expanded benefits from the local procurement authority in the DoD Federal Acquisition Regulation Supplement (DFARS). The increased flexibility to buy centrally managed items locally when such action is in the best interest of the Government took effect on November 30, 1995, with the publication of Defense Acquisition Circular 91-9 in the Federal Register. As a follow-up action to that publication, we have requested the Military Departments to remove restrictions on local purchase authority beyond those in the DFARS coverage from regulations issued by the Military Departments. Full implementation of the new DFARS coverage, which includes the exclusion of requirements up to the simplified acquisition threshold (\$100,000) from those which must be forwarded to the coordinated acquisition assignee (DLA for Federal Supply Group 34), will meet the goal of this recommendation.

"B. We recommend that the Deputy Under Secretary of Defense (Logistics):

1. Direct the Defense Logistics Agency, in coordination with the Military Departments, to issue formal procedures for using the rebuild services of the Defense General Supply Center.

2. Direct the Military Departments to formally evaluate the capability of the Defense General Supply Center rebuild services whenever practicable before acquiring new metalworking machinery."

This office concurs with the recommendation. A memorandum has been sent to the Defense Logistics Agency and the Military Departments requesting that they work together to issue formal procedures for using the rebuild services of the Defense General Supply Center. The same memorandum requests the Military Departments to formally evaluate the capability of the Defense General Supply Center rebuild services whenever practicable before acquiring new metalworking machinery.

ATTACHMENT

Audit Team Members

This report was prepared by the Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, DoD.

Shelton R. Young
Thomas D. Kelly
John B. Patterson
E. David Coyne
Laura A. Rainey
Glen B. Wolff