

Audit



Report

LOGISTICS RESPONSE TIME FOR THE DIRECT VENDOR
DELIVERY PROCESS, DEFENSE SUPPLY CENTER, RICHMOND

Report Number 99-108

March 17, 1999

Office of the Inspector General
Department of Defense

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Acronyms

BPA	Blanket Purchase Agreement
DFARS	Defense Federal Acquisition Regulation Supplement
DLA	Defense Logistics Agency
DSCR	Defense Supply Center, Richmond
DVD	Direct Vendor Delivery
LRT	Logistics Response Time
NSN	National Stock Number
RDD	Required Delivery Date
SAMMS	Standard Automated Materiel Management System
UMMIPS	Uniform Materiel Movement and Issue Priority System



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

March 17, 1999

MEMORANDUM FOR ASSISTANT DEPUTY UNDER SECRETARY OF DEFENSE
(MATERIEL AND DISTRIBUTION MANAGEMENT)
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Audit Report on the Logistics Response Time for the Direct Vendor
Delivery Process, Defense Supply Center, Richmond (Report No. 99-108)

We are providing this report for information and use. This is the second in a series of reports on logistics response time. We performed this audit in response to a concern by the Office of the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management) about whether the direct vendor delivery process is unfavorably affecting the logistics response time. We considered management comments on a draft of this report in preparing the final report.

Management 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. Raymond D. Kidd at (703) 604-8828 (DSN 664-8828) (rkidd@dodig.osd.mil) or Mr. Hassan A. Soliman at (703) 604-8868 (DSN 664-8868) (hsoliman@dodig.osd.mil). See Appendix D for the report distribution. The audit team members are listed inside the back cover.

David K. Steensma

David K. Steensma
Deputy Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. 99-108

March 17, 1999

(Project No. 8LH-0012.01)

Logistics Response Time for the Direct Vendor Delivery Process, Defense Supply Center, Richmond

Executive Summary

Introduction. This is the second in a series of reports on logistics response time. This report covers the logistics response time for direct vendor delivery at the Defense Supply Center, Richmond, Virginia. A previous report, Report No. 99-101, "Logistics Response Time for the Direct Vendor Delivery Process, Defense Supply Center, Columbus," March 4, 1999, addressed the same issue for the Defense Supply Center, Columbus, Ohio, and subsequent reports will cover various other topics impacting logistics response time. The audit was requested by the Office of the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management).

DoD corporate goals in response to the Government Performance and Results Act included goals to reduce inventories through adopting commercial practices and to reduce logistics response time by 50 percent by the year 2000. Those goals were reflected in the 1996/1997 and 1998 DoD Logistics Strategic Plans. Direct vendor delivery emulates a commercial practice by procuring materiel with direct delivery to customers of the DoD supply system. There are three types of direct vendor delivery. Planned direct vendor delivery is usually used for items that the Defense Logistics Agency knows in advance will be needed in sufficient quantities to warrant establishing long-term contracts. Unplanned direct vendor delivery may be used when Defense Logistics Agency depots run out of stock for the requisitioned items. Non-stocked direct vendor delivery is used when supply centers do not receive enough requests to justify stocking a supply item.

The Defense Logistics Agency is the primary manager for procuring consumable hardware items. From FY 1996 through the first 5 months of FY 1998, the Defense Logistics Agency used direct vendor delivery for about 17 percent of its total consumable hardware procurements. In FY 1997, Defense Supply Center, Richmond, direct vendor delivery sales were \$187.4 million for 259,407 requisitions. This audit addressed supply center requisition processing time, which is a subset of logistics response time.

Objectives. The overall audit objective was to evaluate the effectiveness and efficiency of direct vendor delivery in improving logistics response time. We also reviewed the management control program as it applied to the audit objective.

Results. Although Defense Supply Center, Richmond, requisition processing time for planned direct vendor delivery was better than that for direct vendor delivery for unplanned and for non-stocked items, requisition processing time for all direct vendor delivery types at the Defense Supply Center, Richmond, could be improved.

- Direct vendor delivery was effective in reducing consumable hardware inventory; but, as implemented by the Defense Supply Center, Richmond, it did not optimize

logistics response time. As a result, the Defense Supply Center, Richmond, prolonged logistics response time for 25 direct vendor delivery purchase requests in two of our samples by an average of 60 days (Finding A).

- Although DoD established a corporate goal to reduce logistics response time, subordinate and supporting goals were not established at Defense Supply Center, Richmond. As a result, there was no assurance that direct vendor delivery would contribute to achieving the DoD goal to reduce logistics response time (Finding B).

See Appendix A for details on the management control program.

Summary of Recommendations. We recommend that the Director, Defense Logistics Agency, provide guidance to the hardware Defense Supply Centers to maximize the use of post-award price analyses while minimizing unnecessary pre-award price analyses for automated small purchases. We also recommend that the Commander, Defense Supply Center, Richmond, establish procedures that consider the negative effect on logistics response time and that ensure optimum price variance dollar thresholds are used by buyers for pre-award and post-award price variance analyses for automated small purchases of \$2,500 or less; emphasize consolidation and followup procedures for purchase requests referred to technical and supply operations personnel; establish goals to improve logistics response time for direct vendor delivery; and use an appropriate method to ensure use of direct vendor delivery when it is cost-effective and responsive to customers' requirements.

Management Comments. The Defense Logistics Agency agreed to consider the trade-offs associated with price analyses on small purchases, evaluate potential lapses in implementing its procedures, and implement changes to reduce LRT. Those changes include the evaluation of Automated Small Purchase System Phase I purchases that are referred to buyers for pricing review and awarded manually and the implementation of streamlining guidance where appropriate. The Defense Logistics Agency also concurred with improving management of the referral of hard-to-fill items to the technical and supply operations personnel, stating that the Defense Supply Center, Richmond, will issue policy emphasizing the requirement to combine purchase requests for items with the same national stock number, expand acquisition guidance to require buyers to follow up on purchase requests in referral to the technical and supply operations personnel, and clarify policy on consolidating purchase requests for direct vendor delivery, stock, and foreign military sales. The Defense Logistics Agency did not agree to make software changes to automatically notify buyers of opportunities for purchase request consolidation, stating such changes would not reduce logistics response time, but that its planned actions to improve management of the referral process will emphasize purchase request consolidation. The Defense Logistics Agency concurred with establishing goals for logistics response time of direct vendor delivery and using models that optimize direct vendor delivery cost-effectiveness and responsiveness to customer needs. The Defense Supply Center, Richmond, had provided training on using the Corporate Contract Decision Tool, which was being fielded. See Part I for a discussion of management comments and Part III for the complete text of management comments.

Audit Response. The Defense Logistics Agency actions were responsive; its proposed actions meet the intent of the recommendations.

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Part I - Audit Results

Introduction

This audit was performed because the Office of the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management) expressed concern about the impact of direct vendor delivery (DVD) on logistics response time¹ (LRT) in response to a General Accounting Office audit report.² The General Accounting Office reported that Defense Logistics Agency (DLA) records disclosed that the average LRT for DVD in FY 1996 was 54 days, compared to 25 days when DLA used its own stock to fill customer orders. DVD is a method to fill a customer's order for supplies by delivering them directly from the vendor to the customer, without DoD having to stock them. This is the second in a series of reports on DoD efforts to shorten LRT. This report covers LRT for DVD at the Defense Supply Center, Richmond (DSCR), Virginia. A previous report, Report No. 99-101, "Logistics Response Time for the Direct Vendor Delivery Process, Defense Supply Center, Columbus," March 4, 1999, covered LRT for DVD at the Defense Supply Center, Columbus, Ohio, and subsequent reports will cover various other topics impacting LRT. This audit addressed supply center requisition processing time, which is a subset of LRT. LRT also includes requisition processing at the requisitioning installation and shipping times.

Background

DLA uses three types of DVD processes: planned, unplanned, and for items not stocked by DLA. DLA stated that all three types were incorporated in the 54-day average included in the General Accounting Office report. Of the total DVD shipments completed in FY 1997, planned DVD was used for 38 percent, and unplanned DVD and DVD for non-stocked items were each used for 31 percent. The planned DVD process has a shorter processing time than the other two DVD processes.

Planned DVD Process. Planned DVD usually is used for items that DLA knows in advance will be needed in sufficient quantities to warrant establishing long-term contracts. When a DLA supply center receives requisitions for such items, the center fills the requisition using existing long-term contracts that have been pre-negotiated by DLA. Other types of contracts are also used for planned DVD. The average DLA supply center processing time was 8.3 days for shipments completed in FY 1997 using the planned DVD process.

Unplanned DVD Process. Unplanned DVD may be used when DLA depots run out of stock for requisitioned items. When depots run out of stock, supply centers may use the unplanned DVD process to fill the requisition or hold the requisition in a backorder status until the stock is replenished. To fill requisitions through unplanned DVD, DLA supply centers usually order against a blanket purchase agreement (BPA). Because terms for BPAs are not fully negotiated, supply centers must issue an order, receive and evaluate vendors'

¹LRT is the total elapsed time between the date of the customer requisition and the closeout of the requisition. Closeout of the requisition means the item is delivered to the requisitioner.

²Report No. NSIAD-98-47, "Defense Inventory Management--Expanding Use of Best Practices for Hardware Items Can Reduce Logistics Costs," January 20, 1998.

offers, and award a purchase order. The average supply center processing times for unplanned DVD are longer than processing times for planned DVD. Additionally, supply centers often do not immediately begin the unplanned DVD process because the requisitioned item is already on backorder, which further increases processing time. The average DLA supply center processing time was 94.3 days for shipments completed in FY 1997 using the unplanned DVD process.

DVD Process for Non-Stocked Items. When DLA supply centers do not receive enough requests to justify stocking a supply item, they intentionally do not stock it and fill requisitions for such items through the DVD process for non-stocked items. Generally, no contracts or purchase agreements are in place for non-stocked items, so when a supply center receives a requisition for such an item, the center must issue a solicitation, receive and evaluate vendors' proposals, and award a contract. Like unplanned DVD procurements, DVD procurements for non-stocked items usually take longer to process than planned DVD procurements. The average DLA supply center processing time was 67.9 days for shipments completed in FY 1997 using the DVD process for non-stocked items.

The 1996/1997 DoD Logistics Strategic Plan. Two guiding principles in the 1996/1997 DoD Logistics Strategic Plan were that performance will be measured in relation to the impact on customers and that not only performance metrics, but also performance measurement methods must be sharpened. One goal was to reduce average LRT from 24 days experienced in the first quarter FY 1996 to 16 days by September 1997. The goal applied to all sources of supply, whether from DoD stock or DVD procurements. The plan included separate goals for each of the Services.

The 1998 DoD Logistics Strategic Plan. The 1998 DoD Logistics Strategic Plan emphasizes the need to maintain optimum inventory levels that will rapidly meet customer support objectives, to improve the logistics process, and to adopt best business practices. In the plan, the LRT baseline is 36 days in February 1997, and the goals are:

30 days	February 1998
24 days	February 1999
18 days	February 2000

According to the Office of the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management), the baseline in the 1998 plan was increased to 36 days because consumable and reparable³ supply items from all DoD sources were included, not just DLA supply items, as was the case in the 1996/1997 plan. Additionally, the information provided by the Logistics Metric

³Consumable items of supply are those that are normally expended or used up beyond recovery in the use for which they were designed or intended. Categories of consumable items include hardware such as automotive, electrical and construction items (bolts, brake shoes, wires, etc.), and non-hardware items such as clothing and food. Repairable inventory items are subject to economical repair.

Analysis Reporting System was more comprehensive and accurate than the initial data provided by the Military Supply and Transportation Evaluation Procedures.⁴

Objectives

The overall audit objective was to evaluate the effectiveness and efficiency of DVD in improving LRT. The specific audit objectives were to evaluate factors that might limit achieving the goal of optimum LRT for DVD and to evaluate the effectiveness of the DVD process in supporting the goal of improved LRT at DSCR. We also reviewed the management control program as it applied to the audit objectives. See Appendix A for a discussion of the audit scope and methodology and the review of the management control program. See Appendix B for a summary of prior coverage and Appendix C for additional audit coverage related to LRT.

⁴LRT statistics were reported by the Military Supply and Transportation Evaluation Procedures before the introduction of the Logistics Metric Analysis Reporting System.

Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time

DVD was effective in reducing consumable hardware inventory; but, as implemented by DSCR, it did not optimize LRT. LRT for DVD was not optimized because DSCR did not use its successful post-award price analyses for automated small purchases to reduce its pre-award analyses of those purchases, and did not properly consolidate or sufficiently monitor purchase requests for hard-to-fill items. As a result, DSCR prolonged LRT for 25 purchase requests for unplanned DVD and DVD for non-stocked items in two of our samples by an average of 60 days. DoD goals were to achieve an average LRT of 30 days by February 1998 and 24 days by February 1999.

Use of DVD

Using DVD to fill customer requisitions for materiel is discussed in the National Defense Authorization Act for FY 1996 and DoD Regulation 4140.1-R, "DoD Materiel Management Regulation" (DoD Regulation 4140.1-R), January 1993. The National Defense Authorization Act for FY 1996 (Public Law 104-106, Section 352) requires DoD to implement a system under which, to the maximum extent possible, vendors deliver consumable hardware inventory items directly to military installations throughout the United States. Additionally, DoD Regulation 4140.1-R states that DoD should use DVD whenever it is cost-effective and responsive to user requirements. In May 1998, DoD Regulation 4140.1-R was reissued and extended supply alternatives to other commercial practices in addition to DVD.

Effectiveness and Efficiency of DVD

Review of Selection Criteria. To review the effectiveness and efficiency of DVD in improving LRT, we judgmentally selected the Defense Supply Center, Columbus, and DSCR to perform the audit work. Of the three DLA supply centers, the Defense Supply Center, Columbus, and DSCR reported the largest number of consumable hardware requisitions filled through DVD processes in FY 1997.

We selected the DLA supply centers for our review because DLA is the main buyer of consumable hardware items for DoD, and the DLA supply centers significantly impact LRT. We focused our review on consumable hardware items because, in FY 1996, those items accounted for 3.9 million, or 97 percent, of the

Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time

4 million items managed by DLA.⁵ Also, consumable hardware items accounted for \$2.6 billion of the \$5.5 billion worth of materiel⁵ purchased by DLA in FY 1996.

Table 1 shows the distribution of requisitions filled in FY 1997 using the DVD process.

	<u>Total</u>	<u>Planned</u>	<u>Unplanned</u>	<u>Non-Stocked</u>
Columbus	234,942	141,123	44,729	49,090
Philadelphia	150,733	76,523	25,001	49,209
Richmond	<u>259,407</u>	<u>199,825</u>	<u>20,041</u>	<u>39,541</u>
Total	645,082	417,471	89,771	137,840

Table 2 shows the sales distribution, by center and DVD process, of consumable hardware items that were shipped in FY 1997.

	<u>DVD Sales</u>	<u>Planned</u>	<u>Unplanned</u>	<u>Non-Stocked</u>
Columbus	\$185.8	\$ 47.1	\$ 89.2	\$ 49.5
Philadelphia	151.0	67.2	34.5	49.3
Richmond	<u>187.4</u>	<u>86.4</u>	<u>38.1</u>	<u>62.9</u>
Total	\$524.2	\$200.7	\$161.8	\$161.7

Implementation of DVD Processes by DSCR. DVD was effective in reducing consumable hardware inventory; but, as implemented by DLA and DSCR, it did not optimize LRT. Using DVD, supplies are delivered directly from the vendor to the user, bypassing the DLA warehousing and distribution system and eliminating the need to stock inventory. However, unless the DLA supply centers executed a DVD process in an efficient manner, the supply centers' processing time for consumable hardware requisitions filled through DVD processes lagged behind the processing time for requisitions filled from DLA stock. Table 3 compares the supply centers' average processing time for filling a requisition from DLA stock with average processing times for filling a requisition through DVD processes,

⁵Excluding fuels.

Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time

based on information captured by the Virtual Logistics Information Processing System. Those DVD processing times include both manual and automated processing.

Table 3. Comparison of Average Processing Times for FY 1997 Consumable Hardware Requisitions (in days)

	<u>DLA Stock</u>	<u>All DVD</u>	<u>Planned</u>	<u>Unplanned</u>	<u>Non-Stocked</u>
Columbus	2.2	39.5	8.1	98.9	75.5
Philadelphia	2.0	42.8	12.9	91.5	64.6
Richmond	2.4	21.4	6.6	87.5	62.7
All centers	2.2	33.0	8.3	94.3	67.9

To evaluate DSCR management of LRT for its DVD process, we selected and evaluated four judgmental samples from different universes. We evaluated the need to perform pre-award price variance analyses, their effect on LRT, and the use of post-award analyses instead of pre-award analyses. We also conducted analyses and interviews to evaluate the cause and effect of delaying purchase requests for hard-to-fill items. Additionally, we evaluated DSCR optimization of DVD cost-effectiveness and responsiveness to customer requirements through a review of the existence and use of appropriate models such as the Method of Support Model.

Analysis of the procurement process identified two areas where the processing time for all DVD procurements could be reduced. DSCR did not use its successful post-award price analyses for automated small purchases to reduce its time-consuming pre-award analyses that extended LRT by a range of 4 to 6 days for five purchase requests reviewed. Also, DSCR did not have sufficient controls for consolidating and monitoring hard-to-fill items, which extended LRT by a median of 64 days for 20 purchase requests reviewed. As a result, DSCR prolonged LRT for all DVD purchase requests in two of our samples, a total of 25 purchase requests, by an average of 60 days. See Appendix A for details on our samples.

Inclusion of national stock numbers (NSNs) on the Exception File, which enables a requisition to bypass automated processing, is another factor that could extend LRT. However, DSCR had made significant progress in reducing the number of NSNs on the Exception File by thoroughly reviewing the Exception File and establishing management controls that would prevent unnecessary additions to the Exception File. For details on the Exception File, see Appendix C.

Review of Small Purchases for Price Reasonableness

LRT for DVD was not optimized because DSCR did not use its successful post-award price analyses for automated small purchases to reduce its pre-award

Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time

analyses for those purchases. DSCR post-award analyses resulted in voluntary refunds to the Government. However, its pre-award analyses were conducted without considering whether they were cost-effective when compared with the price variance, and without considering their impact on LRT. As a result, the cost to manually process those procurements exceeded the potential savings, and LRT was prolonged by a median of 5 days for five purchase requests reviewed. DSCR uses an automated system for processing small purchases. If certain parameters are not met, the system refers the purchase request to procurement personnel (buyers) for review, which includes price analyses and possibly manual processing.

The Standard Automated Materiel Management System (SAMMS) Automated Small Purchase System Phase I automatically issues orders of \$2,500 or less against BPAs and up to \$25,000 against indefinite-delivery contracts. After vendors respond to orders, SAMMS generates purchase requests that are sent to the subsystem known as the SAMMS Procurement by Electronic Data Exchange for evaluation. If the vendors' offers meet all purchase requirements, including acceptable price variances, the SAMMS Procurement by Electronic Data Exchange electronically awards the contract. If the offers do not meet purchase requirements, SAMMS Procurement by Electronic Data Exchange will refer the purchase requests to buyers for review.

Requirements for Buyer Review. DSCR conducts post-award and pre-award price reasonableness analyses for small purchases of \$2,500 or less. After contract award, unreasonable prices are automatically calculated by SAMMS using variance parameters of 25 percent for awards of \$1,000 or less and 10 percent for awards of more than \$1,000 to \$2,500. That information, provided in the SAMMS Vendor Price Variance Report (F-106 Report), is used by the Competition and Pricing Branch to conduct post-award price variance analyses and to support efforts to recoup funding from vendors on overpriced contracts. The DSCR practice for automated procurements requires the referral of purchase requests to buyers for pre-award review when vendor price offers exceed Government-expected prices by a given percentage, which is 25 percent for procurements of \$2,500 or less.

The Defense Federal Acquisition Regulation Supplement (DFARS) Subpart 217.7504, "Limitation on Price Increase," states:

- (a) The contracting officer shall not award, on a sole source basis, a contract for any centrally managed replenishment part when the price of the part has increased by 25 percent or more over the most recent 12-month period.

It further states:

- (a)(2) Departments and agencies may specify an alternate percentage or percentages for contracts within the small purchase limitations in FAR [Federal Acquisition Regulation] Part 13.

**Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving
Logistics Response Time**

The Federal Acquisition Regulation Subpart 13.202, "Purchase Guidelines," for actions at or below the micro-purchase threshold (\$2,500) states:

(3) The administrative cost of verifying the reasonableness of the price for purchase may more than offset potential savings from detecting instances of overpricing. Therefore, action to verify price reasonableness need only be taken if--

(i) The contracting officer or individual appointed in accordance with 1.603-3(b) suspects or has information to indicate that the price may not be reasonable (e.g., comparison to the previous price paid or personal knowledge of the supply or service); or

(ii) Purchasing a supply or service for which no comparable pricing information is readily available (e.g., a supply or service that is not the same as, or is not similar to, other supplies or services that have recently been purchased on a competitive basis).

We believe that the acquisition regulations provide contracting officers the flexibility to avoid price analyses that are not cost-effective.

Conducting Post-Award Price Analyses. DSCR performed post-award price analyses that resulted in voluntary refunds to the Government. After contract award, unreasonable prices are automatically calculated by SAMMS using variance parameters and provided in the F-106 Report. The DSCR Competition and Pricing Branch uses the F-106 Report information to generate price justification letters to vendors. The letters request that the vendors either justify the prices charged or reimburse the Government for the unreasonable prices charged.

Cost-Effectiveness of Post-Award Price Analyses. In FY 1998, DSCR awarded 5,769 procurements to vendors at unit prices that varied more than 10 percent from historical costs of the items being procured. The difference between the prices paid and historical costs totaled \$910,925. In FY 1998, the DSCR post-award analysis program recouped about \$357,000, or 39 percent, of unreasonable BPA contractor charges. Under the conditions used by DSCR to award BPA contracts, failure to either reimburse the Government or to justify prices with cost information can result in cancellation of the BPA. One of the attributes of the program that contributed most to its success, according to Competition and Pricing Branch personnel, is that the program has been run consistently with dedicated personnel over a number of years. Vendors are knowledgeable of the program and expect letters questioning unreasonable charges. We commend DSCR for an effective BPA cost control that does not slow LRT.

Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time

Consideration of Responsiveness to Customer Requirements. The post-award price variance analysis process at DSCR fully supports the objective of LRT reduction. Since those price variance analyses occur after contract award, there is no impact on LRT. The post-award price variance analyses should be maximized in lieu of the pre-award price variance analyses to optimize the balance between cost-effectiveness and customer responsiveness.

Conducting Pre-Award Price Analyses. DSCR conducted pre-award price analyses that were not cost-effective and prolonged LRT for all five purchase requests in our sample. To determine whether price analyses resulted in cost-effective and responsive procurement decisions, we selected a judgmental sample of five vendor offers made in response to orders against BPAs. Our sample consisted of DVD purchase requests that the SAMMS Procurement by Electronic Data Exchange had referred to buyers as requiring review because of price variances. During the initial review, the buyer researches the records of past procurements and then decides whether to accept the vendor's price or have the procurement processed manually. Manual processing involves competing a procurement among vendors and may increase both the cost of processing the procurement and its LRT. The five vendor offers in our sample represented the approximate number of vendor offers that a buyer would review in one day due to price variance, excluding those items with no standard price that are first-time buys and stock buys. The purchase requests in our sample had been referred to buyers from September 29 through October 1, 1998. More than one day of referrals was included in the sample because of the small number of purchase requests that were being received by DSCR in the first days of the new fiscal year. In FY 1998, DSCR issued an average of 67 orders against BPAs per day.

Cost-Effectiveness of Pre-Award Price Analyses. DSCR pre-award price variance analyses were not cost-effective. The 25 percent cost control threshold for unit price variance had been built into the DSCR procurement system without regard for the materiality of the total variance and the effect of pre-award price analysis on LRT. DSCR did not have sufficient activity-based cost records to determine the cost of a single manual procurement of \$2,500 or less; however, management at DSCR informed us that the threshold of \$250 was used to refer procurements to manual processing. At the Defense Supply Center, Columbus, the cost to manually process a procurement of \$2,500 or less was about \$345. Table 4 identifies the price variances of all offers in our sample. The price variances on four purchase requests did not exceed the \$250 threshold for DSCR manual processing of procurements. Of the five purchase requests in the sample, none of the total price variances of offers exceeded the cost of manual processing at Defense Supply Center, Columbus. DSCR needed to consider the financial cost and benefit of performing pre-award price analyses and the potential benefits of performing post-award analyses in lieu of performing pre-award price analyses. Maximizing post-award price analyses for automated small purchases while minimizing corresponding pre-award analyses assists in optimizing cost-effectiveness and responsiveness to customer delivery requirements.

Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time

Table 4. Pre-Award Price Variances of Offers in Sample

<u>Sample No.</u>	<u>Purchase Request No.</u>	<u>Government-Expected Price*</u>	<u>Offer Price*</u>	<u>Variance</u>
1	YPG98271000088	\$ 1.32	\$ 6.62	\$ 5.30
2	YPG98246000307	54.00	77.90	23.90
3	YPG98267000079	55.16	104.31	49.15
4	YPG98271000124	41.50	198.00	156.50
5	YPG98257000183	281.99	571.50	289.51

*Government-expected and offer prices listed are for the entire purchase request, not price per unit.

The following are examples for which pre-award price analyses were performed.

- An order for two electrical conduits (sample no. 1) were requested as Uniform Materiel Movement and Issue Priority System (UMMIPS) priority three, issue priority group one.⁶ The vendor offer price was \$3.31 per unit for a total of \$6.62. The Government-expected price was \$0.66 per unit or \$1.32 for the two units. The Government-expected price was based on an earlier order for a quantity of 50 units. While the price variance was 400 percent of the Government-expected price, the variance was only \$5.30. Not only was this priority item delayed from getting to the customer by approximately 6 days, but also the cost of manual processing far exceeded the variance amount.
- An order for one pressure gauge (sample no. 2) was requested as UMMIPS priority five, issue priority group two. The purchase request was identified by the automated system for manual review because the vendor offered a price of \$77.90 per unit compared to the Government-expected price of \$54. Although the price variance was 44 percent of the Government-expected price, the total variance amount was only \$23.90.

Consideration of Responsiveness to Customer Requirements. There was no indication that buyers considered the impact of price analyses or manual processing on meeting customers' required delivery dates (RDDs). Review and manual processing increased the time to process purchase requests. In FY 1997,

⁶UMMIPS is a structure which establishes time standards, based on the mission and urgency of need of the requestor, for the supply of materiel from the time of origination of the requirement (date of the requisition) to the time that the acknowledgment of physical receipt is posted to the requisitioner's inventory record. The UMMIPS has 15 priority designators that define the priority to fill customer requisitions. Issue priority group one includes UMMIPS priorities one, two, and three and requires delivery in 8 days (12 to 13 days for overseas). Issue priority group two includes priorities four through eight and requires delivery in 12 days (16 to 17 days for overseas). Issue priority group three includes priorities 9 through 15 and requires delivery in 31 days (69 to 84 days for overseas). In May 1998, DoD Regulation 4140.1-R recognized UMMIPS standards by transportation priority, instead of issue priority group.

Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time

DSCR processing time for orders against BPAs⁷ that were automatically processed averaged 7.6 days whereas all types of orders that were manually processed averaged 99.3 days. Four purchase requests in our sample passed their RDDs while being processed. As a result of purchase requests being referred to buyers because of price variances, LRT for the five purchase requests in our sample was increased by a range of 4 to 6 days.

Consolidating Buys of Hard-to-Fill Items with Current Buys

LRT for DVD was not optimized because DSCR did not properly consolidate and sufficiently monitor purchase requests for hard-to-fill items. Buyers at DSCR allowed purchase requests for DVD items to remain in referral to technical and supply operations personnel past their RDDs while subsequent purchase requests for the same items were successfully placed on contract. Buyers did not use resources available to optimize procurement consolidation. Also, buyers and supply and technical operations personnel did not use resources available to properly manage purchase requests aging in referral. As a result, LRT was prolonged by a range of 6 to 182 days, with a median of 64 days, for the sample of 20 purchase requests. None of the purchase requests met the customers' RDDs.

Referral to Technical or Supply Operations Personnel. Purchase requests for hard-to-fill items are placed in suspension or referral status to technical or supply operations personnel for a number of reasons. Common reasons for referral include evaluation of alternative offers, such as vendors offering substitute or surplus items; the item requested is an obsolete part number; or there is no vendor available for an item. Under some circumstances, one purchase request may be suspended while another purchase request for the same item is not. For example, a vendor may offer a surplus item that must be validated by technical operations personnel for acceptability, while another vendor for a subsequent purchase request offers an exact item that does not require technical review. The purchase request in the second case will be processed and placed on contract, while the first purchase request remains in referral.

Management Controls and Existing Guidance. DLA and DSCR have a system of controls that, when followed, should ensure purchase requests remaining in referral for extended periods are minimized and that consolidation is maximized. Buyers, item managers, and technical and supply operations personnel can track referrals through a reporting system in SAMMS and through the DLA Pre-Award Contracting System. When the DLA Pre-Award Contracting System is used, it automatically updates SAMMS. Additionally, DSCR developed a stand-alone Workload Tracking System to monitor the forms generated when purchase requests are referred to technical and supply operations personnel. The DSCR

⁷BPAs are primarily used for unplanned DVD and DVD for non-stocked items. The time for processing BPAs includes time for SAMMS to prepare a purchase request, transmit the requirement to a vendor, receive and evaluate the vendor offer, obtain funding, and award the purchase order. Also, because items procured through unplanned DVD were often on backorder, DSCR did not immediately begin the DVD process.

Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time

Form 353, Purchase Request Suspension/Cancellation Form, is the vehicle for documenting purchase request referrals and actions taken. The DLA and DSCR systems can produce reports that allow continuous monitoring of purchase requests in referral. Also, the following guidance applies to managing consolidations and the referral process.

- DLA Manual 4715.1, "SAMMS Contracting Subsystem Operating Procedures," January 1998, addresses options for increasing a quantity on a purchase request to support multiple requisitions for the same item, control procedures for referral of purchase requests, and the role of the purchase request trailer⁸ in supporting consolidation decisions.
- The DLA Internal Procedures Memorandum No. 97-0029, "Requirements Guidance and Recommended Buy Policy" (DLA Memorandum 97-0029), November 13, 1997, Attachments 13 and 14, direct buyers and item managers to assess other open purchase requests for the same item and to consolidate the requisition with an open purchase request and direct item managers to contact buyers on aging open purchase requests.
- Defense Supply Center Acquisition Procedures, Part 13, "Simplified Acquisition Procedures," revised October 2, 1998, Section 13.106, directs buyers to combine purchase requests for the same NSN whenever practical, provides guidance for adding a stock line to a DVD purchase request, and directs buyers to annotate why purchase requests are not combined if they are unable to do so.
- Defense General Supply Center Regulation 4105.9, Section II, "Policy," specifies that the buyer will be responsible to follow up on referral purchase requests within a reasonable time and provides criteria for establishing suspenses to ensure timely review of referred purchase requests.
- The DLA Pre-Award Contracting System Users Manual, January 25, 1993, identifies "smart fields" for open contracts and purchase requests that prompt buyers to combine open acquisitions. It also provides procedures to identify open purchase requests and contracts for an NSN as well as instructions for both referring purchase requests to technical and supply operations personnel via the DLA Pre-Award Contracting System and for producing management reports to monitor referred purchase requests.

Management of the Referral Process. Buyers at DSCR allowed purchase requests for DVD items to remain in referral status past their RDDs while subsequent purchase requests for the same items were successfully placed on contract. To review management of the referral process, we requested personnel at DSCR to identify purchase requests that remained in referral while subsequent purchase requests for the same items were placed on contract. DSCR personnel identified 127 DVD purchase requests for items that had been sent to referral from January 1 through August 31, 1998, and were still in referral as of

⁸The purchase request trailer is an addendum to the purchase request that provides, among other things, a listing of other open purchase requests for the same item, sources of supply, and information on previous contracts.

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August 31, 1998, for which contracts had been awarded for later purchase requests for the same items. While those later purchase requests had contracts successfully awarded from January 1 through August 31, 1998, the earlier purchase requests for the same items were not consolidated and remained in referral. We judgmentally selected 20 of the 127 for further review. In a separate effort to review the status and average age of all purchase requests in referral, we requested an aging report of all purchase requests in referral. As of September 21, 1998, 3,118 purchase requests, of which 48 percent were DVD, were aging in referral at DSCR. We examined the status of all purchase requests listed on the aging report in issue priority group one that had been in referral for over 180 days. That sample consisted of 52 purchase requests.

Consolidation of Purchase Requests in Referral. DSCR missed opportunities to consolidate purchase requests in referral with other purchase requests that were successfully placed on contract. Although consolidation of purchase requests could reduce average LRT, reduce unit cost, or motivate a vendor to bid for a larger order, none of the buyers interviewed considered consolidation of the 20 purchase requests we examined. Buyers stated the DSCR policy is to combine purchase requests whenever possible, yet our review of the purchase requests in our sample did not reveal any documentation, as required in Defense Supply Center Acquisition Procedures, Part 13, to specify why consolidation did not occur. Some buyers stated they did not have visibility of other open purchase requests, yet the DLA Pre-Award Contracting System has features that identify open purchase requests and open contracts for the same NSN. Additionally, the purchase request trailer identifies other purchase requests that are open at the time a purchase request is generated.

Although resources were available to provide a prompt for consolidation, that did not occur in some cases. For example, purchase request YPG97323000669, received on November 19, 1997, was referred to technical operations personnel in February 1998 with a request to identify additional sources of supply after a solicitation resulted in no offers. While that purchase request remained in referral, three other purchase requests for the same item were received, on January 22, May 4, and May 29, 1998, and were all successfully placed on contract. As of October 13, 1998, the initial purchase request was not placed on contract.

Some of the buyers stated they did not consider consolidation of their purchase requests with other purchase requests handled by buyers outside of their section, such as the Emergency Supply Operations Center. That resulted in some Emergency Supply Operations Center purchase requests remaining in referral while contracts were successfully awarded for purchase requests for the same items being handled in the product centers. Additionally, most buyers were under the false impression that they were specifically precluded from combining purchase requests for unplanned DVD with purchase requests for stock or with DVD purchase requests supporting foreign military sales customers. Although guidance does not preclude combining requirements for DVD and stock or foreign military sales on one purchase request, guidance for accomplishing that type of consolidation is not clear. The buyers' false impression resulted in the cancellation of some DVD purchase requests to support the customer with a stock

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purchase request that extended LRT. As a result, LRT was prolonged by a range of 6 to 182 days, with a median of 64 days, for the sample of 20 purchase requests.

Monitoring of Purchase Requests in Referral. Although buyers and item managers were assigned responsibility to follow up on open purchase requests for items assigned to them, and DSCR guidance specified time frames for the review of referred purchase requests, buyers conducted limited followup on 32 purchase requests in our sample of 52. Buyers with aging purchase requests who we interviewed cited excessive work load as the primary reason they did not follow up on referrals. They also stated that if the customer inquired or increased the priority of the item, then they followed up. In addition to prolonging LRTs for referred purchase requests, the lack of followup allowed purchase requests to be lost, misplaced, or neglected. Of the 52 aging purchase requests we reviewed, 10 purchase requests from the 1994 and 1996 time frames were canceled but SAMMS was not properly updated. Of the remaining 42 purchase requests, 32 either had a lapse in accountability or had been neglected for periods of up to 10 months. None of the purchase requests in this sample met the customers' RDDs. Although sufficient guidance was available directing followup on purchase requests in referral, buyers did not always comply with that guidance, as illustrated in the following examples.

- Purchase request YPG97227000209, an issue priority group one, UMMIPS priority three order for a cable assembly was received on August 15, 1997. In response to the solicitation, the vendor identified that some of the cable components were obsolete. The purchase request was referred to technical operations personnel where, after being reassigned three times to different technicians, no action had been taken as of October 15, 1998. The buyer for the item had not followed up until our inquiry and was unaware that no work was being accomplished on the item.
- Purchase request YPG97246000506, an issue priority group one, UMMIPS priority two order for a junction box was received on September 3, 1997, and then referred to technical operations personnel in October 1997 because the vendor required special tooling to make the item. The purchase request was further referred to another office that handles all tooling related issues in January 1998. Although the purchase request was still identified as open in their files, the special tooling office had not yet taken action on the item as of October 15, 1998. The buyer for the item had not followed up until our inquiry and was unaware that no work was being accomplished on the item.
- Purchase request YPG98036000200, an issue priority group one, UMMIPS priority two order for a KC-135 structural plate, received on February 5, 1998, was referred to technical operations personnel that same month for development of a technical data package. The buyer for the item had not followed up until our inquiry and was unaware that no work was being accomplished on the item as of October 15, 1998.

Compliance with Existing Management Controls. DSCR management needed to emphasize compliance with the existing system of management controls, including guidance and system tools. DLA Memorandum 97-0029 and Defense Supply Center Acquisition Procedures provide sufficient consolidation

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guidance. Additionally, tools such as the SAMMS GPL005 “Buyer Workload Report” and the DLA Pre-Award Contracting System provide buyers with the necessary visibility of open purchase requests to support consolidation decisions and monitoring of purchase requests aging in referral. However, those tools do not automatically notify buyers when another purchase request for the same item is generated. DSCR personnel did not use the DLA Pre-Award Contracting System to refer purchase requests to technical or supply operations personnel and, as a result, a valuable resource was not available to properly manage referred purchase requests. Emphasizing compliance with the existing controls and expanding DSCR use of the DLA Pre-Award Contracting System would assist DSCR management in improving LRT for both DVD and non-DVD procurements.

Improvements to Existing Management Controls. The Workload Tracking System could be improved. Although the creation of the Workload Tracking System enabled technical operations personnel to monitor purchase requests in referral to them, that stand-alone system does not interface with SAMMS or the DLA Pre-Award Contracting System. The lack of interface resulted in duplication of effort to maintain both the Workload Tracking System and SAMMS, created unneeded reconciliation challenges, and did not enhance buyer visibility of technical operations personnel actions on referred purchase requests. Additionally, the Workload Tracking System duplicated processes for tracking referred purchase request work load that were already available in the DLA Pre-Award Contracting System when it is used to refer purchase requests. Modifications to the Workload Tracking System would allow it to automatically update the DLA Pre-Award Contracting System and SAMMS to ensure proper visibility of referred purchase requests.

Summary

Decisions to perform price analyses when total vendor offer prices exceeded the allowed variance from target prices should consider the cost of manual processing and the effect on LRT. We believe that minimizing manual processing of orders against BPAs, through minimizing pre-award price variance analyses that are not cost-effective, while maximizing post-award analyses would improve cost-effectiveness and LRT. DSCR should issue guidance to buyers that includes guidelines on the trade-off between the potential savings to be gained by conducting pre-award price variance analyses and the associated administrative cost and effect on LRT. Additionally, LRT could be reduced by maximizing consolidation opportunities and making better use of existing resources to manage purchase requests aging in referral.

Recommendations, Management Comments, and Audit Response

A.1. We recommend that the Director, Defense Logistics Agency, provide guidance to the hardware Defense Supply Centers to maximize the use of post-award price analyses, while minimizing unnecessary pre-award price analyses for automated small purchases.

Management Comments. DLA only partially concurred, stating that it will consider the trade-offs associated with price analyses on small purchases; evaluate potential lapses in implementing its procedures; and implement effective changes to reduce LRT, including the evaluation of SAMMS Automated Small Purchase System Phase I purchases that are referred to buyers for pricing review and awarded manually and the implementation of streamlining guidance where appropriate. DLA also cited the need to avoid criticism from other Inspector General, DoD, reports for paying higher prices than previously paid. DLA stated that the procedures in place were to avoid “price creep” in its automated system and delaying a few of the many thousands of automated acquisitions it processed was not a material weakness. The estimated completion date for the planned actions is March 31, 1999.

DLA stated that its 25 percent threshold for performing pre-award price variance analyses is a management control consistent with the Federal Acquisition Regulation Subpart 13.202 and the DFARS Subpart 217.7504. DLA further stated that the audit finding was based on a small sample and an incorrect assumption that procurements referred to a buyer for price analyses must always be awarded manually, and added that reviewing offers and then awarding contracts automatically has a negligible effect on LRT. DLA also stated that having its contracting officers forego price reasonableness determination in favor of post-award reviews is contrary to the guiding principles of the Federal Acquisition Regulation because the post-award process is considerably more expensive and time-consuming compared to pre-award price analyses.

Audit Response. Although DLA only partially concurred, the alternative actions it plans to take satisfy the intent of the recommendation. No further comments are required. However, the issues raised by DLA in its comments warrant clarification of our position.

Although the sample was non-statistical, it was indicative of a need to improve LRT through faster processing of small purchases under BPAs. Also, we understood that purchase requests referred to buyers for price analyses would possibly, but not always, be manually processed. The data collected showed increased LRT for all referred purchase requests, whether they were returned to automated processing after analyses or were manually processed.

Our recommendation that the DLA supply centers minimize pre-award analyses (not forego all such analyses) was made with the Federal Acquisition Regulation guiding principles in mind.

Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time

A.2. We recommend that the Commander, Defense Supply Center, Richmond:

a. Establish procedures that consider the negative effect on logistics response time and that ensure optimum price variance dollar thresholds are used by buyers for pre-award and post-award price variance analyses for automated small purchases of \$2,500 or less.

Management Comments. DLA partially concurred and referenced its response to Recommendation A.1., stating that the sample reviewed does not indicate a systemic problem of increased LRT due to pre-award pricing reviews. However, DLA stated that it would evaluate those buys that are referred to buyers for pricing review and awarded manually and that it would implement streamlining guidance where appropriate. The estimated completion date for corrective actions is March 31, 1999.

Audit Response. DLA actions that it will take in response to Recommendation A.1. and this recommendation are responsive to the intent of the recommendation. No further comments are required.

b. Emphasize the requirement for buyers to assess and maximize opportunities to consolidate purchase requests for the same item and for buyers to follow up with technical or supply operations personnel at periodic intervals to determine status and disposition of referred purchase requests.

Management Comments. DLA concurred, stating that DSCR will issue policy emphasizing the requirement to combine purchase requests for the same NSN when feasible and when it makes proper business sense to do so. Additionally, DSCR acquisition guidance will be expanded to require buyers to follow up on purchase requests referred to technical and supply operations personnel. The estimated completion date for corrective actions is March 31, 1999.

c. Clarify guidance to address consolidation of purchase requests for unplanned direct vendor delivery and stock or foreign military sales requirements.

Management Comments. DLA concurred, stating that DSCR will issue guidance to clarify the policy on consolidating purchase requests for direct vendor delivery, stock, and foreign military sales, taking into account the varying requirements regarding fast payment, inspection, and acceptance procedures for each procurement type. The estimated completion date for corrective actions is March 31, 1999.

d. Make software changes to ensure that buyers with purchase requests aging in referral are automatically notified if an order is issued for the same item.

Management Comments. DLA nonconcurred, stating that buyers currently have visibility of open purchase requests through the DLA Pre-Award Contracting System. The "Open Purchase Requests" data field on the purchase request summary screen identifies additional purchase requests for that item and, if selected, can provide the details on those purchase requests. That information

Finding A. Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time

allows the buyer to effect consolidation when appropriate to potentially reduce LRT and the price paid. However, DSCR will emphasize consolidation of purchase requests aging in referral through the changes to guidance in response to Recommendations A.2.b. and A.2.c. The estimated completion date for corrective actions is March 31, 1999.

Audit Response. Although a software change to notify buyers would communicate the necessary information with much less work for the buyers, the DSCR policy changes regarding consolidation satisfy the intent of the recommendation. No further comments are required.

e. Direct buyers to either use the Defense Logistics Agency Pre-Award Contracting System to refer and monitor purchase requests referred to technical or supply operations personnel or modify the Workload Tracking System to interface with and update the Standard Automated Materiel Management System and the Defense Logistics Agency Pre-Award Contracting System.

Management Comments. DLA concurred, stating that with the DSCR transition from the current version of the DLA Pre-Award Contracting System to the DLA Pre-Award Contracting System Graphical User Interface (the DLA User Interface), the technical operations specialists will begin using that system to manage purchase request referrals. The DLA User Interface will eliminate the need for the current Workload Tracking System for purchase request referrals. The estimated completion date for corrective actions is 90 days after the March 31, 1999, deployment date for the DLA User Interface.

Finding B. Logistics Response Time Goals and Performance Measurement

Although DoD established a corporate goal to reduce LRT, subordinate and supporting goals were not established at DSCR. Specifically, DSCR did not establish goals to reduce LRT for DVD and did not use the Method of Support Model or an alternative method to optimize cost-effectiveness and responsiveness to customer requirements of DVD processes. As a result, there was no assurance that DVD would contribute to achieving the DoD goal to reduce LRT.

Corporate Goals and Performance Reporting

Corporate and Functional Goals. In response to the Government Performance and Results Act, DoD established corporate goals to reduce LRT and supply inventory. To support the DoD corporate goals, the DoD Logistics Strategic Plans included two objectives: reduce logistics cycle time and streamline logistics infrastructure through implementing best business practices that result in reductions of minimally required inventory levels.

To contribute to accomplishing the corporate goal to reduce LRT:

- DSCR needed to establish goals to reduce LRT for DVD and
- DSCR needed to improve its efforts to optimize cost-effectiveness and responsiveness to customers' requirements of DVD processes.

LRT Goals for DVD

DSCR did not establish goals to reduce LRT for DVD. To determine whether goals for improving LRT for DVD were established, we reviewed the "Defense Logistics Agency FY 1997/1998 Performance Plan" (DLA Performance Plan) and discussed the establishment of those goals with personnel at DSCR. Because DoD corporate goals included an emphasis on using commercial practices, such as DVD, along with a goal to reduce LRT, we considered establishing goals to reduce LRT for DVD a reasonable management control to support DoD goals.

DLA Performance Plan. Inspector General, DoD, Report No. 99-101, "Logistics Response Time for the Direct Vendor Delivery Process, Defense Supply Center, Columbus," March 4, 1999, stated that DLA did not establish and implement goals for reducing LRT for requisitions filled through DVD. The materiel management program indicators in the DLA Performance Plan state the LRT goals for DVD processes were to be determined. In FY 1997, DVD was used to fill requisitions worth \$533.3 million (16.3 percent) of the total DLA

Finding B. Logistics Response Time Goals and Performance Measurement

consumable hardware sales of \$3.3 billion. DLA personnel stated that focus for the future is on other commercial practices, such as the Prime Vendor⁹ initiative, that would result in cost-effective and responsive customer service.

DSCR LRT Goals for DVD. DSCR did not have LRT goals for requisitions filled through DVD. DSCR management stated it did not have LRT goals for DVD because DLA had not set goals. Since reducing LRT is a corporate goal and DVD is a commercial practice encouraged in the DoD Logistics Strategic Plan, we believe DSCR should establish LRT goals for DVD and monitor goal accomplishment.

Cost-Effectiveness and Responsiveness of DVD Processes

DSCR did not use the Method of Support Model or an alternative method to optimize cost-effectiveness and responsiveness to customer requirements of DVD processes. The Method of Support Model measures the cost-effectiveness of DVD processes; however, its ability to measure the effectiveness of DVD processes to meet customers' RDDs was limited. As a result, there was no assurance that opportunities to effectively use DVD processes were identified or that responsiveness to customers' RDDs was effectively considered.

Balancing DoD Goals to Reduce Inventories and Shorten LRTs. Achieving the DoD corporate goals to both reduce inventories and shorten LRTs requires maximizing the benefits intended by both goals. The Fundamental Principles of Operations in the 1998 DoD Logistics Strategic Plan require that performance be measured based on improving customer support and reducing total logistics costs. The Customer Needs Statement in the plan states that customers require materiel and logistics services to be priced competitively based on "best value." Also, Logistics Management Imperatives in the plan require management to shorten LRT and to apply best business practices. DoD Regulation 4140.1-R formalizes the requirements for DVD, stating that DoD should use DVD whenever it is cost-effective and responsive to customer requirements. The Regulation also states that timely satisfaction of customer requirements shall be a primary factor, along with the anticipated cost and benefits, in determining whether initiation of new procurements are in the best interest of the Government. In view of those concepts, a method is needed to optimize cost-effectiveness and responsiveness.

Practices to Optimize Cost-Effectiveness and Responsiveness. DSCR product centers used a lead item manager/buyer team approach to determine the cost-effectiveness and responsiveness of a potential planned DVD procurement under a long-term contract. The teams first identified commercial supply items suitable for long-term contracts that had high business volume and value. Then, DSCR buyers determined the potential vendor's ability to respond to a standard delivery period of up to 30 days. Finally, DSCR personnel used their experience to estimate the cost-effectiveness of a potential DVD procurement.

Selecting Supply Items for DVD. Item managers and buyers in each product center jointly determined whether a procurement should be filled through

⁹A Prime Vendor buys inventory from a variety of suppliers and stores the inventory in its own warehouse.

Finding B. Logistics Response Time Goals and Performance Measurement

stock or DVD. DSCR personnel made that decision based on a demand history for an NSN that consisted of at least 4 requisitions for a total of 12 items in the past year. If there were sufficient demands for an item and it belonged to a weapon system, then greater consideration was given to stocking the item. In addition, if the item was a commercial item, then it was considered a good candidate for DVD contracts. Finally, after considering the demand history, applicability for weapon systems, and the commercial nature of items, DSCR personnel assessed vendor responsiveness to customer requirements and cost-effectiveness based on item manager/buyer judgment and analysis of the vendor's willingness and ability to supply items directly to customers.

Determining Responsiveness to Customer Requirements. To determine responsiveness to customer requirements, DSCR managers informed us that they used UMMIPS standards and the Military Standard Requisitioning and Issue Procedures Priority Codes that require delivery periods of up to 30 days as a guide in negotiating long-term contract delivery periods. For corporate contracts,¹⁰ DSCR negotiated 48-hour delivery for high priority requisitions and for routine orders they negotiated 8-day delivery. If potential vendors could meet those delivery requirements, then DSCR buyers would consider placing the items in the Paperless Order Placement System, an automated purchasing method to electronically transmit DVD orders to vendors.

Determining Cost-Effectiveness. To determine cost-effectiveness of a potential DVD procurement, DLA established the Method of Support Model to measure savings from converting an item from stocked to non-stocked status. The Method of Support Model produces the break-even price for stock and DVD alternatives and the percentage that a DVD price could increase above the most current representative price and still result in savings. DSCR management personnel informed us that while DSCR used a 20 percent threshold, that threshold was not formalized in DSCR policy. Defense Supply Center, Columbus, also used a 20 percent threshold, which it had based on past experience with the Method of Support Model.

Review of DSCR Performance. DSCR did not always use the UMMIPS standards and did not consider customers' RDDs when negotiating DVD contracts, which could erode customer confidence in the timeliness of the supply system. Additionally, DSCR did not use the Method of Support Model to measure cost-effectiveness.

Negotiated Delivery Periods. We judgmentally selected 149 contracts to review DSCR use of the UMMIPS standards in negotiating delivery dates. Table 5 compares the delivery periods negotiated by DSCR and the UMMIPS standards that DSCR personnel stated were used as a guide for DVD contracts. As shown in Table 5, the negotiated delivery periods for 73 of the 149 contracts in the sample exceeded the UMMIPS standards. Of those 73 contracts, 57 were for planned DVD.

¹⁰A corporate contract is a long-term contractual agreement, managed by a single supply center, against which multiple supply centers and Services can place orders.

Finding B. Logistics Response Time Goals and Performance Measurement

Table 5. Comparison of Negotiated Delivery Periods and UMMIPS Standards

<u>Contract Type</u>	<u>No. of Contracts</u>		<u>Delivery Periods (days)</u>	
	<u>In the Sample</u>	<u>Not Meeting UMMIPS</u>	<u>Median Negotiated</u>	<u>Median UMMIPS Standards</u>
Requirement ¹	118	51	30	31
Delivery order ²	21	12	30	12
Long-term, corporate, and General Services Administration ³	<u>10</u>	<u>10</u>	116	8
Total	149	73		

¹A requirement contract is used for acquiring supplies when the Government anticipates recurring requirements but cannot predetermine the precise quantities needed during a definite period. Orders for requirement contracts are processed through the Paperless Order Placement System.

²A delivery order contract provides for the issuance of orders for the delivery of supplies during the contract period but does not specify a firm quantity (other than a minimum and maximum).

³A General Services Administration contract is a federal supply schedule containing information necessary for placing delivery orders with designated contractors to obtain commonly used commercial supplies at prices associated with volume buying.

We also reviewed the same sample for responsiveness to RDDs. For the 149 contracts in the sample, the RDD had passed for 21 contracts before DSCR received the requisition. Also, DSCR negotiated delivery dates for 132 contracts that exceeded RDDs, while the negotiated delivery dates for 17 contracts met the RDDs. Vendors successfully delivered on or before the negotiated delivery dates for 132 contracts. Nevertheless, items were delivered after RDDs for 74 contracts. Table 6 shows the results of our review.

Table 6. Responsiveness of 149 Contracts to Required Delivery Dates

	<u>No. of Contracts</u>	<u>Median Days</u>	<u>Excess Days</u>
For the 149 sample contracts:			
RDD passed before DSCR received requisition	21	62	1-881
Negotiated delivery date exceeded RDD	132	22	1-1,658
Shipment made after RDD	74	20	1-1,644
Shipment made after negotiated delivery date	17	10	1-71

Finding B. Logistics Response Time Goals and Performance Measurement

DoD Customer Confidence in Timeliness of the DLA Supply System.

As customers lose confidence in the ability of the DLA supply system to deliver requisitioned materiel by the RDD, they may build up retail inventories as a safeguard. Customers may also shorten RDDs in an effort to ensure timely delivery. Personnel at DSCR stated they do not evaluate their success in meeting RDDs as a performance measure. According to DSCR, the RDD data field did not always contain information against which a measurement might be made. Because requisitions include a priority designator and a requisition date, we believe the RDD can be derived by adding the days for the customer-specified requisition priority to the requisition date. A future audit will review RDDs for reasonableness and for proper application of priority designators.

Cost-Effectiveness Measurement. Although some DSCR personnel were aware of the Method of Support Model, DSCR personnel stated that they were not using that Model or an alternative method to measure cost-effectiveness of potential DVD contracts. DSCR management stated that while in the past it had used the Method of Support Model to help determine the cost-effectiveness threshold on a case-by-case basis, the results of using that model had consistently shown too many errors and problems to be useful in analysis and decisionmaking. Although the Method of Support Model's User's Guide states that buyers are responsible for maintaining model history in a logical and timely manner, DSCR management stated it had not retained a database or any information on DSCR use of the Method of Support Model. DSCR management also stated it stopped using the Method of Support Model because its use was not mandated by DLA. DSCR management confirmed that DSCR no longer used the Method of Support Model but recently scheduled new training sessions on the use of the Vendor Stock Retention Model that predates the Method of Support Model. The Vendor Stock Retention Model supports decisionmaking by quantifying the savings that result from removing items from a stocked position to a DVD arrangement.

Management Actions. During our previous audit of Defense Supply Center, Columbus, DLA took clear action to emphasize the importance of the proper use of DVD and DSCR responded to the guidance.

DLA. In a June 8, 1998, memorandum to DLA supply centers, the Commander, Defense Logistics Support Command:

- emphasized the proper use of DVD;
- stated that DVD is a method to allow DLA to provide responsive, best value supplies to its customers;
- expressed concern that planned DVD was not meeting or beating depot support; and
- stated that tools, such as the Vendor Stock Retention Model and the Method of Support Model, were available to the DLA supply centers to verify that customer requirements are not adversely affected by DVD contracts and that costs are reduced.

Additionally, on September 8, 1998, DLA briefed DSCR on the use of the Vendor Stock Retention Model and its potential for use in the DSCR decisionmaking processes.

Finding B. Logistics Response Time Goals and Performance Measurement

DSCR. Realizing the importance of analytical tools that assist in inventory acquisition decisions, DSCR had contracted with the accounting firm of KPMG to develop the Corporate Contracting Decision Tool. The Corporate Contracting Decision Tool is an economic analysis tool to identify and measure incremental cost differences associated with DLA supply centers' decisions to retain or transfer inventory and its management to a vendor. DSCR management also planned to formally institutionalize the 20 percent threshold in DSCR policy for personnel to use in their analyses after DSCR management reviewed the results of ongoing studies, performed by DLA, of the Vendor Stock Retention Model. The ongoing studies include a comparative analysis of data reliability of the DSCR Corporate Contracting Decision Tool and the Vendor Stock Retention Model; the decision tool and the model assist management in the decision to fill requisitions from stock or through DVD.

Summary

DSCR did not establish LRT goals for consumable hardware items procured through DVD, and there was no evidence that DSCR used the existing systems to ensure the effective and responsive use of DVD processes to satisfy customer requirements. As a result, there was no assurance that DVD would contribute to achieving the DoD goal to reduce LRT. Establishing LRT goals for DVD would highlight the importance of DVD to helping achieve the DoD goal of reducing LRT. DLA took clear action to emphasize the importance of the proper use of DVD by issuing guidance to its supply centers. However, DSCR should place more emphasis on the proper application of an approach to optimize cost-effectiveness and responsiveness of DVD procurements.

Recommendations, Management Comments, and Audit Response

B. We recommend that the Commander, Defense Supply Center, Richmond:

1. Establish goals for logistics response time for direct vendor delivery for consumable hardware items.

Management Comments. DLA concurred, stating that its December 22, 1998, memorandum advised the Hardware Inventory Control Points that a DVD goal would be established and requested they review their established long-term contracts. That review was to determine why long procurement lead times were established on some arrangements and why vendors were not shipping within established time frames. The estimated completion date for corrective actions is March 31, 1999.

Finding B. Logistics Response Time Goals and Performance Measurement

2. Optimize the cost-effectiveness and responsiveness to customer requirements of the direct vendor delivery process by using the Method of Support Model or an alternative method.

Management Comments. DLA concurred, stating that DSCR has already begun fielding the Corporate Contracting Decision Tool as an alternative method to comparing the relative benefits of depot stockage with DVD. Training has been provided to DSCR personnel. The estimated completion date for corrective actions was January 31, 1999.

Part II - Additional Information

Appendix A. Audit Process

Scope

We performed the audit at DoD organizations with responsibilities for establishing, accomplishing, and monitoring execution of goals for LRT and DVD. The organizations included the Office of the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management); DLA; DSCR; the Defense Automatic Addressing System Center; and Service logistics offices. Our analysis focused on DVD procurements. We reviewed applicable laws, DoD regulations, and other documents, including:

- National Defense Authorization Act for FY 1996 (Public Law 104-106, Section 352);
- DoD Regulation 4140.1-R, "DoD Materiel Management Regulation," January 1993;
- DoD Regulation 4140.1-R, "DoD Materiel Management Regulation," May 1998;
- DoD Logistics Strategic Plans, Editions 1996/1997 and 1998;
- DLA FY 1997/1998 Performance Plan;
- DLA performance report for FY 1996;
- DSCR requisition history interrogations for the sample items;
- DSCR contracts, and award-related documents for the sample items;
- DSCR BPA transactions referred by SAMMS Procurement by Electronic Data Exchange for review from September 29 through October 1, 1998;
- DSCR purchase requests placed on contract from January 1 through August 31, 1998, that had purchase requests for identical items aging in referral;
- DSCR purchase requests aging in referral as of the September 21, 1998, SAMMS F-31/F-32 report, "Purchase Requests Returned to Supply/Technical/(or Others)";
- DLA statistics on requisitions filled through DVD in FY 1997; and
- DSCR Exception File as of October 1998.

DoD-Wide Corporate Level Goals. In response to the Government Performance and Results Act, DoD has established 6 DoD-wide corporate level performance objectives and 14 goals for meeting these objectives. This report pertains to achievement of the following objectives and goals.

- **Objective:** Maintain highly ready joint forces to perform the full spectrum of military activities. **Goal:** Maintain high military personnel and unit readiness. **(DoD-5.1)**
- **Objective:** Fundamentally reengineer the Department and achieve a 21st century infrastructure. **Goal:** Reduce costs while maintaining required military capabilities across all DoD mission areas. **(DoD-6)**

DoD Functional Area Reform Goals. Most major DoD functional areas have also established performance improvement reform objectives and goals. This report pertains to achievement of the following functional area objectives and goals.

- **Acquisition Functional Area. Objective:** Deliver great service. **Goal:** Achieve visibility of 90 percent of DoD materiel assets, while resupplying military peacekeepers and warfighters and reducing average order to receipt time by 50 percent. **(ACQ-1.2)**
- **Logistics Functional Area.** The logistics functional area included two objectives in support of the DoD-wide corporate level performance objectives.

Objective: Reduce logistics cycle times. **Goal:** Reduce average LRT by one-third by September 1997 (based on the first quarter of FY 1996 averages), and reduce average age of backordered items to 30 days by October 2001. **(LOG-1.1)**

Objective: Streamline logistics infrastructure. **Goal:** Implement most successful business practices (resulting in reductions of minimally required inventory levels). **(LOG-3.1)**

High-Risk Area. The General Accounting Office has identified several high-risk areas in the DoD. This report provides coverage of the Defense Inventory Management high-risk area.

Methodology

At the Office of the Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management), we reviewed DoD goals for LRT, dissemination of those goals to DoD Components, and monitoring of plans to accomplish those goals. At DLA, we reviewed plans to accomplish DoD LRT goals, policy on using DVD, and how those plans and policies were disseminated to DLA supply centers. At DSCR, we reviewed the determination of delivery dates for DVD contracts and management of the DSCR segment of LRT. We analyzed requisitions filled through DVD processes by DLA in FY 1997 to determine the characteristics of DVD procurements. Additionally, we reviewed the effect of different contracting methods on LRT. While we selected the supply centers

Appendix A. Audit Process

based on FY 1997 shipments, our review was based on judgmental samples of purchase requests for requisitions that DSCR filled through DVD processes during FY 1997, purchase requests placed on contracts from January 1 through August 31, 1998, and purchase requests in referral to technical and supply operations personnel as of September 21, 1998.

To determine whether price analyses resulted in cost-effective and responsive procurement decisions, we reviewed DLA Manual 4715.1, "SAMMS Contracting Subsystem Operating Procedures," January 1998, for policy on the requirement to perform price analyses; DSCR practices for performing price analyses; and reports that contained data on purchase requests referred to buyers for price analyses. We reviewed a non-statistical sample of five offers made in response to BPA orders to determine the effectiveness and efficiency of price analyses.

To examine management of purchase requests for hard-to-fill items in referral to technical and supply operations personnel, we examined relevant DSCR policies and controls, interviewed buyers, supervisors, and technical and supply operations personnel. We also examined the potential for consolidation of a non-statistical sample of 20 purchase requests in referral, and we reviewed how long purchase requests stayed in referral for 52 purchase requests from an aging report.

To assess the DSCR practices for using DVD processes, we reviewed the Method of Support Model's User's Guide, updated June 1996; evidence of using the Method of Support Model; how a customer's RDD was considered in negotiating delivery times with vendors; and how the issues of cost and responsiveness were optimized. To examine DSCR practices, we reviewed a non-statistical sample of 149 contracts (long-term, corporate, requirement, General Services Administration, and delivery order). Those contracts were awarded between 1992 and 1997. We also reviewed that sample to determine responsiveness of negotiated delivery periods to customers' RDDs. We also interviewed DSCR personnel about the DSCR decision process for using DVD.

Use of Computer-Processed Data. We relied on computer-processed data from SAMMS to determine which DLA supply centers to visit, and to determine audit sample selection. To test the reliability of the computer-processed data obtained from SAMMS, we compared the requisition receipt dates, purchase request processing dates, and contract award dates of our sample to SAMMS. SAMMS accurately reflected that information.

Universe and Sample. We used judgmental techniques to select four samples of DSCR procurement information to evaluate the effectiveness and efficiency of DSCR management of the DVD process. The samples used to conduct separate tests were extracted from various universes, as shown in the following table.

Judgmental Samples

Sample Size by DVD Process

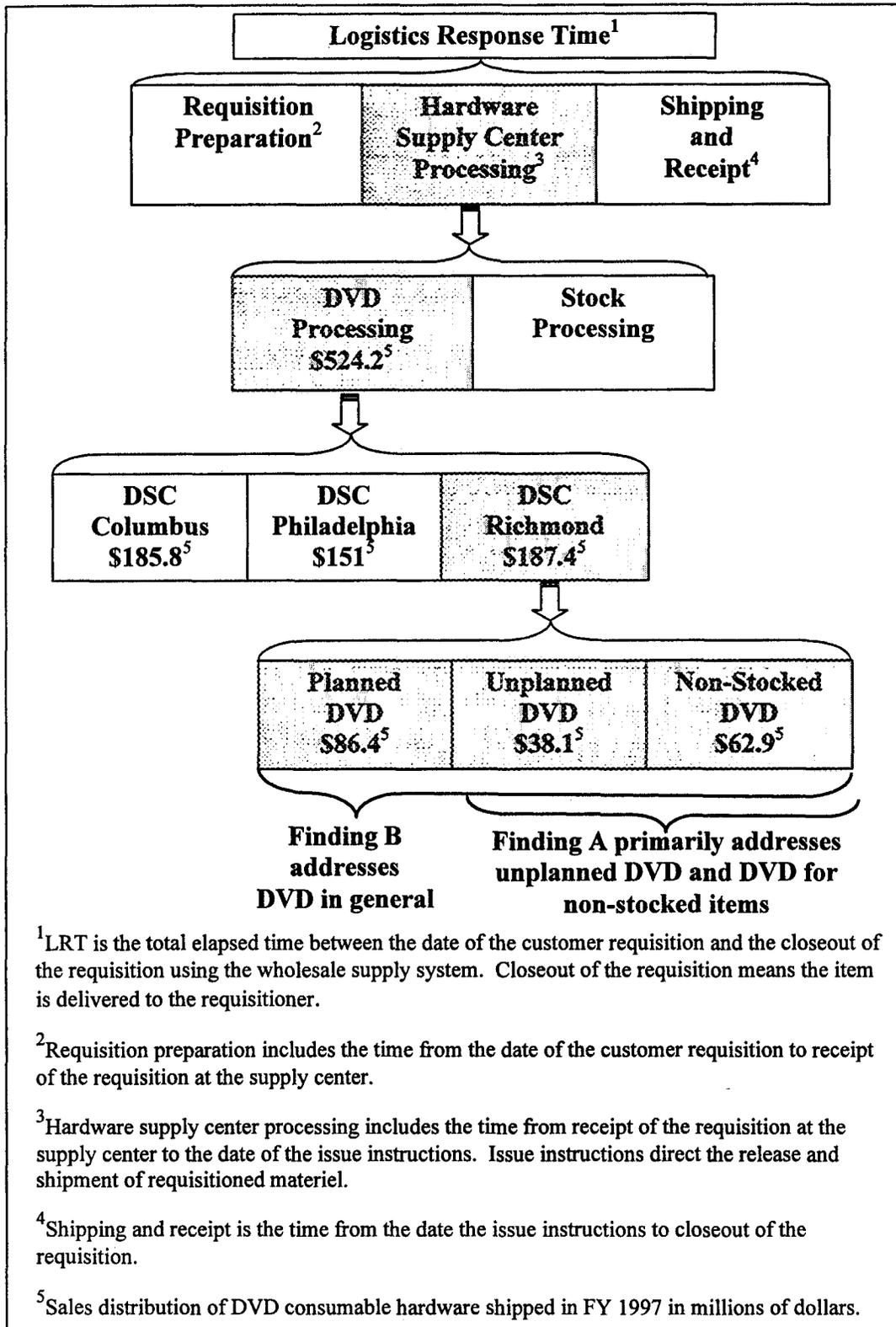
<u>Issue Tested</u>	<u>Sample Size</u>	<u>Planned</u>	<u>Unplanned and Non-Stocked</u>	<u>Universe</u>
Price variance analysis	5		5	Note 1
Consolidation of hard-to-fill items	20		20	Note 2
Aging of hard-to-fill items	52		52	Note 3
DVD process responsiveness	149	133	16	Note 4

Notes.

1. No total accounting of records was available to select from. The sample consisted of DVD purchase requests that the SAMMS Procurement by Electronic Data Exchange had referred to buyers as requiring review because of price variance of offers received over 3 days in September and October 1998 in response to orders against BPAs.
2. Total of 127 DVD contract awards for purchase requests for items that were also in other purchase requests in referral to technical or supply operations personnel.
3. Total of 3,118 purchase requests in referral to technical operations personnel listed in a September 21, 1998, aging report.
4. Total of 259,407 DVD procurements completed in FY 1997. The sample was used to test whether DSCR used the UMMIPS standards to determine negotiated delivery dates, and to test responsiveness to RDDs. Sample items were used to perform more than one test.

The following figure shows the LRT area and DVD types covered in this audit and the relationship of the audit coverage to the findings in this report. LRT segments can be grouped in requisition preparation time, hardware supply center processing time, and shipping time. In this audit, we reviewed hardware supply center processing time for the DVD process at DSCR; the Defense Supply Center, Columbus, was covered in a previous audit. Finding A primarily addresses unplanned DVD and DVD for non-stocked items, while Finding B addresses the DVD process in general.

Appendix A. Audit Process



Audit Type, Dates, and Standards. We performed this economy and efficiency audit from October through November 1998 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.

Contacts During the Audit. We visited or contacted individuals and organizations within DoD. Further details are available on request.

Management Control Program

DoD Directive 5010.38, "Management Control Program," August 26, 1996, 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 the Management Control Program. At DSCR, we reviewed the adequacy of management controls over manual and automated contracting procedures. We also reviewed the results of management's self-evaluation of those management controls.

Adequacy of Management Controls. We identified material management control weaknesses for DSCR as defined by DoD Directive 5010.38. DSCR management controls for DVD procurements were not adequate because they allowed purchase requests to be excluded from the automated process; did not provide for effective consolidation and tracking of purchase requests for hard-to-fill items; and did not emphasize the proper use of procedures to determine cost-effectiveness and responsiveness of potential DVD procurements. All recommendations, if implemented, will improve the DSCR LRT for DVD. A copy of the report will be provided to the senior officials responsible for management controls in DLA and DSCR.

Adequacy of Management's Self-Evaluation. DSCR officials did not identify contracting procedures for DVD as an assessable unit; therefore, DSCR did not identify or report the material management control weaknesses identified by this audit.

Appendix B. Summary of Prior Coverage

During the last 5 years, the General Accounting Office and the Inspector General, DoD, issued seven audits related to DVD. Most of the audits only briefly mentioned LRT.

General Accounting Office

Report No. NSIAD-98-47 (OSD Case No. 1485), "Defense Inventory Management--Expanding Use of Best Practices for Hardware Items Can Reduce Logistics Costs," January 20, 1998.

Inspector General, DoD

Report No. 99-101, "Logistics Response Time for the Direct Vendor Delivery Process, Defense Supply Center, Columbus," March 4, 1999.

Report No. 98-064, "Commercial and Noncommercial Sole-Source Items Procured on Contract N000383-93-G-M111," February 6, 1998.

Report No. 97-220, "Direct Vendor Delivery and Just-In-Time Management Initiatives," September 24, 1997.

Report No. 97-018, "The Patriot Advanced Capability-3 Program," November 4, 1996.

Report No. 96-035, "Price Challenges on Selected Spare Parts," December 12, 1995.

Report No. 95-107, "Controls Over Materiel Procured for Direct Vendor Delivery," February 10, 1995.

Appendix C. Management of the Exception File

DSCR planned to improve its management controls over its NSN/Federal supply class Exception File. Improvements were planned to enhance control over the processes and procedures used to exclude purchase requests from being processed by the SAMMS Automated Small Purchase System. As a result, DSCR will further limit the potential for misuse of the Exception File and the potential negative effect on LRT.

Introduction. DSCR recognized that the Exception File process could potentially extend LRT because of the time associated with manually processing purchase requests. However, DSCR did not believe that the Exception File had extended LRT. The function of the Exception File is to prevent specific NSNs from being processed through Phase I, Phase II, or both Phases I and II of the SAMMS Automated Small Purchase System. Phase I is an automated method of processing orders of \$2,500 or less against BPAs and up to \$25,000 against indefinite-delivery contracts. Phase II is an automated method of requesting and processing offers for contracts up to \$25,000. DSCR planned to incorporate additional management controls that will enhance the operation of the Exception File and further reduce the potential impact on LRT.

DLA Guidance for Exception File Maintenance. Chapter 15 of DLA Manual 4715.1 states that certain NSNs and entire Federal supply classes must be excluded from the SAMMS Automated Small Purchase System for various reasons. The reasons include NSNs that are on mandatory General Services Administration schedules and Federal supply classes that are not conducive to contracting through the automated system. However, DLA Manual 4715.1 does not provide detailed guidance on maintaining the Exception File.

DSCR Exception File Policies and Procedures. DSCR had limited official guidance for maintaining and using the Exception File. The Procurement Systems Branch of the Systems and Procedures Division was responsible for managing the Exception File, but did not have written guidance for the file's management. In 1995, DSCR published the "Guide and Instructions for Automated Small Purchases Phase I" and a similar guide for Phase II to assist buyers and supervisors in understanding, operating, and maintaining the SAMMS Automated Small Purchase System. The guides include information about the purpose and use of the NSN Exception File and information about how NSNs and Federal supply classes can be added to the Exception File. Additionally, the guides list acceptable reasons for including NSNs on the Exception File. The guides do not, however, include information about the need, nature, or frequency of reviews of the Exception File, and DSCR did not have additional guidance for reviews. Management controls over the Exception File process should require establishment of effective policies and procedures for reviews to be properly implemented. Without those policies and procedures, DSCR will not have assurance that the Exception File is effectively maintained, will risk unnecessarily processing purchase requests manually, and may consequently increase LRT.

DSCR Review of Exception File. DSCR had conducted an extensive review of the Exception File in 1996, but was not conducting periodic reviews. However, DSCR planned to initiate a weekly review of the Exception File to ensure it

Appendix C. Management of Exception the File

continues to operate properly. DSCR used the Exception File process to exclude items from automated processing through Phase I, Phase II, or both Phases I and II. The Exception File process does not exclude all automated processing. NSNs and Federal supply classes that had to be excluded from the SAMMS Phases I and II processes because of special conditions, such as first article testing, were recorded properly in the Exception File. DSCR also used the Exception File to allow Phase II solicitations to reach a wider population of prospective vendors, and more than one-third of the NSNs included on the Exception File were added for that reason. Another major reason DSCR included NSNs on the Exception File was because the NSNs were associated with long-term contracts that were not subject to Phase I or II processes.

Review of the Exception File. To review the Exception File, we compared the NSNs in the October 1998 Exception File to the NSNs associated with DVD contracts that DSCR awarded during FY 1997. The Exception File included 3,520 NSNs associated with more than 195,000 DVD contracts. However, nearly 192,000 of those contracts had been automatically processed. Therefore, for FY 1997, manual processing was required for only about 2 percent of the DVD contracts with NSNs that were included on the October 1998 Exception File.

Processing Time. We identified the DSCR processing time for manual and automated contract awards for the items that DSCR procured. The average time for automatic processing of orders against BPAs under Phase I for FY 1997 was 7.6 days compared to 99.3 days for all manually processed purchase requests. We believe that appropriate maintenance of the Exception File is essential to ensuring that LRT does not increase through unnecessarily processing purchase requests manually.

Manually Processed Purchase Requests. DSCR did not have a report to distinguish those purchase requests that were manually processed as a result of NSNs contained in the Exception File. By not reporting this information, DSCR did not have visibility over potential increases in manually processed purchase requests resulting from unnecessary exclusions. A complete review of the reasons why purchase requests bypass Phases I and II automatic processing requires DSCR management to have visibility of the impact of purchase requests processed manually as a result of the Exception File.

Summary. DSCR had effective management controls for its Exception File. However, the management controls could be improved by establishing policies and procedures for periodic reviews. DSCR needs to continue incorporating management controls that will enhance the operation of the Exception File.

Appendix D. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition and Technology
Deputy Under Secretary of Defense (Logistics)
Assistant Deputy Under Secretary of Defense (Materiel and Distribution Management)
Director, Defense Logistics Studies Information Exchange
Under Secretary of Defense (Comptroller)
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)
Assistant Secretary of Defense (Public Affairs)

Joint Staff

Director, Joint Staff

Department of the Army

Deputy Chief of Staff for Logistics (Supply Policy Division)
Auditor General, Department of the Army

Department of the Navy

Assistant Secretary of the Navy (Financial Management and Comptroller)
Deputy Chief of Naval Operations for Logistics (Supply Programs and Policy)
Auditor General, Department of the Navy

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)
Deputy Chief of Staff for Installations and Logistics (Directorate of Supply)
Auditor General, Department of the Air Force

Defense Organizations

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

Appendix D. Report Distribution

Non-Defense Federal Organizations

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

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

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 Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Management, Information, and Technology,
Committee on Government Reform
House Subcommittee on National Security, Veterans Affairs, and International Relations,
Committee on Government Reform

Part III - Management Comments

Defense Logistics Agency Comments



DEFENSE LOGISTICS AGENCY
HEADQUARTERS
8725 JOHN J. KINGMAN ROAD, SUITE 2533
FT. BELVOIR, VIRGINIA 22060-6221

IN REPLY
REFER TO

DDAI

17 February 1999

MEMORANDUM FOR DIRECTOR, READINESS AND LOGISTICS SUPPORT,
INSPECTOR GENERAL, DEPARTMENT OF DEFENSE

SUBJECT: Draft Audit Report on the Logistics Response Time for the Direct Vendor
Delivery Process, Defense Supply Center, Richmond
(Project No. 8LH-0012.01)

Enclosed are DLA comments in response to your 17 December 1998 request. If
you have any questions, please contact Ms. Mimi Schirmacher, DDAI, 767-6263.

Encl

Alvin Coleman
FOR JEFFREY GOLDSTEIN
Chief (Acting), Internal Review

cc
DLSC-B
DLSC-L
DLSC-P
DSCR-DI

SUBJECT: Logistics Response Time for the Direct Vendor Delivery Process, Defense Supply Center, Richmond (Project No. 8LH-0012.01)

FINDING A.: Effectiveness and Efficiency of Direct Vendor Delivery in Improving Logistics Response Time. DVD was effective in reducing consumable hardware inventory; but, as implemented by DSCR, it did not optimize LRT. LRT for DVD was not optimized because DSCR did not use its successful post-award price analyses for automated small purchases to reduce its pre-award analyses of those purchases, and did not properly consolidate or sufficiently monitor purchase requests for hard-to-fill items. As a result, DSCR prolonged LRT for 25 purchase requests for unplanned DVD and DVD for non-stocked items in two of our samples by an average of 60 days. DoD goals were to achieve an average LRT of 30 days by February 1998 and 24 days by February 1999.

DLA COMMENTS:

PARTIALLY CONCUR. The draft audit report states that the objective was to evaluate the effectiveness and efficiency of DVD in improving LRT. The DoDIG identified three types of DVD: Planned, unplanned, and non-stocked items. The DoDIG correctly points out that for planned DVD, where a conscience effort was made to include items on long term contracts that provided for DVD with significantly reduced LRT, the average supply center processing time was 8.3 days, well within acceptable standards. The DoDIG also recognized that unplanned DVD and the DVD process for non-stocked items is used when DLA depots run out of stock or when the supply centers do not receive enough requests to justify stocking the item. The report discusses these two types of DVD purchases and actually focuses on simplified acquisition Procurement Administrative Lead Time (PALT), in lieu of LRT. DLA recognizes that absent depot stock or a planned DVD long term contract, these two types of DVD purchases, by their very nature, cannot succeed in reducing LRT since each acquisition must be solicited and awarded independently without the benefit of pre-established terms/conditions and prices. These DVDs are usually issued to mitigate the increased LRT associated with bringing material into stock and then issuing a material release order to the customer. DLA continuously reviews items for placement on planned DVD contracts to alleviate the need for unplanned DVD purchases. Consistent with DLA's Strategic Plan, reengineering our business practices to include more items on planned DVD contracts where appropriate will improve LRT, customer support, and reduce PALT.

The business tradeoffs associated with extensive price analysis on low dollar value purchases will be taken into consideration. However, care must be exercised to avoid contradictory findings of the DoDIG on several recent audits critical of DLA for paying prices higher than previous prices paid. The 25 percent threshold for automated award unit price variance was established as a cost control to avoid automatic award at substantially higher prices than previous prices paid. While these purchases are low in value, and the administrative costs to manually process the awards sometimes exceed the value of the material being purchased, prudence demands that we exercise sound

Defense Logistics Agency Comments

business judgment to guarantee the best price for our customers. Sound business judgment is subjective in nature. It can be facilitated by analytical tools and policies that augment automated system purchases when exceptions occur, such as excessive price quotes. The controls and processes in place ensure that the integrity of the automated system itself, and more importantly, the integrity of the procurement system, is free of fraud, waste or mismanagement, thereby ensuring that a material weakness does not exist. The procedures established to prevent "price creep" in DLA's automated system that results in increased PALT for a few of the many thousands of automated simplified acquisition does not constitute a material weakness. It may signify a lapse in procedural implementation that DSCR will evaluate and implement changes as appropriate to more effectively use the Phase I System to reduce LRT. These changes will be monitored under the Management Control Program to assure that anticipated savings materialize and that potential risks are mitigated.

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- (X) Nonconcur.
() Concur; weakness will be reported in the DLA Annual Statement of Assurance.

RECOMMENDATION A.1: Recommend that the Director, Defense Logistics Agency, provide guidance to the hardware Defense Supply Centers to maximize the use of post-award price analyses, while minimizing unnecessary pre-award price analyses for automated small purchases.

DLA COMMENTS: PARTIALLY CONCUR. As stated in our response to Finding A, the 25 percent threshold of automated award unit price variance was established as a cost control to avoid automatic award at substantially higher prices than previous prices paid. Currently, SASPS I automated procurements are only referred to a buyer for a pre-award price review when a vendor's offered price exceeds the Government's expected price by 25 percent. This management control is consistent with the FAR and DFARS guidance highlighted by the DoDIG in the draft audit report. FAR 13.202 does indeed provide contracting officers the flexibility to avoid price analyses on micro-purchases that are not cost effective. However, it continues to state that action to verify the reasonableness of pricing need only be taken if the contracting officer suspects or has information to indicate that the price may not be reasonable (e.g., comparison to the previous price paid). Supplementing guidance in DFARS 217.7504 states that the contracting officer shall not award a contract when the price of the part has increased by 25 percent or more over the most recent 12-month period. Clearly, the guidance requires a positive determination of price reasonableness for micro-purchases, regardless of the dollar value of the material being purchased, when deemed necessary by the contracting officer. The 25 percent threshold in the automated system was programmed to comply with the FAR and DFARS.

SASPS I uses SAMMS Procurement Electronic Data Exchange (SPEDE) to transmit requests for quotes, evaluates vendors' responses, and awards. The DoDIG finding is based on the incorrect assumption that procurements referred to a buyer for violation of the 25 percent price increase threshold must always be manually awarded, thus incurring higher administrative costs to process and increasing LRT. The buyer has access to contract history for each SPEDE purchase request. Upon review, if the buyer determines that the vendor's price is reasonable based on previous prices paid, the buyer simply presses a button and SPEDE resumes its normal automated process and the award is sent to SAMMS for funding. After the order is funded, SPEDE will automatically transmit it to the vendor without buyer intervention. When SPEDE automatically processes an award, the award transaction is placed in the SAMMS upload file. Similarly, when a buyer promotes a SPEDE award after performing a pricing review, the transaction is placed in the same upload file. The SAMMS upload file is a batch file that contains all of the SPEDE awards for that day. Therefore, the pricing review process has a negligible effect on LRT for buyer promoted buys through SPEDE. Three of the five pre-award pricing review items sampled by the DoDIG were verified as being awarded as buyer promoted SASPS I buys.

In FY 97, DSCR processed 24,636 buys through SASPS I. The remaining two items in the DoDIG sample, which prolonged LRT by a median of 5 days, do not indicate that a systemic problem exists in increasing LRT by performing pre-award pricing reviews of items referred to the buyer from the automated system. Advocating that DLA contracting officers forego price reasonableness determinations in favor of post-award pricing reviews is contrary to the guiding principles in the FAR and relies on voluntary reimbursement of overpayments by contractors. Recoupment of a voluntary refund is considerably more expensive and administratively time consuming than performing a pre-award pricing review for small number of items that exceed the 25 percent threshold. DLA will evaluate the small percentage of SASPS I buys that are referred to buyers for pricing review and awarded manually and implement streamlining guidance where appropriate.

DISPOSITION:

- Action is ongoing. ECD: March 31, 1999
- Action is complete.

Defense Logistics Agency Comments

RECOMMENDATION A.2.a: Recommend that the Commander, Defense Supply Center, Richmond establish procedures that consider the negative effect on logistics response time and that ensure optimum price variance dollar thresholds are used by buyers for pre-award and post-award price variance analyses for automated small purchases of \$2,500 or less.

DLA COMMENTS: PARTIALLY CONCUR. As discussed in recommendation A.1, the sample reviewed by the DoDIG does not indicate that a systemic problem of increasing LRT due to pre-award pricing review of buys that breach the 25 percent price increase threshold in the SASPS I automated system exists. However, DLA will evaluate the small number of SASPS I buys that are awarded manually and implement streamlining guidance as appropriate.

DISPOSITION:

- Action is ongoing. ECD: March 31, 1999
- Action is complete.

RECOMMENDATION A.2.b: Recommend that the Commander, Defense Supply Center, Richmond emphasize the requirement for buyers to assess and maximize opportunities to consolidate purchase requests for the same item and for buyers to follow up with technical or supply operations personnel at periodic intervals to determine status and disposition of referred purchase requests.

DLA COMMENTS: CONCUR. DSCR policy will be issued to re-emphasize the requirement to combine purchase requests for the same NSN, when feasible. Combining PRs does not necessarily decrease LRT. For example, if a PR is at the point of award and a new PR is added, the award pending will likely be delayed awaiting revised pricing from the proposed awardee, as well as other offerors within the competitive range. Therefore, policy will be qualified to state that contracting officers should maximize opportunities to combining PRs when it makes proper business sense to do so. Buyers will also be reminded of the existing requirements to document contract files with their rationale when a decision is made not to consolidate PRs. Additionally, coverage will be added to the DSCR Acquisition Procedures to require buyers to follow-up on purchase requests referred to technical and supply personnel.

DISPOSITION:

- Action is ongoing. ECD: March 31, 1999
- Action is complete.

RECOMMENDATION A.2.c: Recommend that the Commander, Defense Supply Center, Richmond clarify guidance to address consolidation of purchase requests for unplanned direct vendor delivery and stock or foreign military sales requirements.

DLA COMMENTS: CONCUR. Guidance will be issued to clarify the policy on consolidating purchase requests for unplanned DVD, stock, and FMS requirements, taking into consideration the following factors:

- Fast Payment procedures are frequently used for DVD shipments if the item does not require Government source inspection and the dollar value of the order does not exceed \$25,000, and can only be applied on an entire contract basis. DLAD 13.302(90) prohibits the use of Fast Payment procedures for depot stock and FMS buys.
- Since Fast Payment procedures may not be used on a depot stock buy, contractor payment problems can arise when consolidating PRs for DVD and stock onto the same award since inspection and acceptance will be at destination and payment will not be made until receipt acknowledgement is received from the requisitioner.
- FMS buys require Government source inspection to ensure contractor payment since material receipt acknowledgement by the FMS customer is often delayed for an extended period of time. By adding FMS requirements to DVD requirements, Government source inspection will apply to the entire contract, thereby increasing LRT.
- FMS requirements contain special provisions which do not apply to other DVD or stock buys. Using DLA Procurement Automated Contract System (DPACS), the buyer cannot specify that clauses or provisions apply to only one contract line and not another. Therefore, the buyer needs to manually amend to award to identify which clauses only apply to the FMS portion of the award. This also increases LRT.

DISPOSITION:

- (X) Action is ongoing. ECD: March 31, 1999
- () Action is complete.

RECOMMENDATION A.2.d: Recommend that the Commander, Defense Supply Center, Richmond make software changes to ensure that buyers with purchase requests aging in referral are automatically notified if an order is issued for the same item.

DLA COMMENTS: NONCONCUR. Buyers currently have visibility of open PRs through DPACS. On the PR Summary Screen, there is a field entitled "Open PRs." If "Yes" is in the data field, there are additional PRs for that item and a buyer can highlight the field and press a key to obtain a list of all open PRs and their status (e.g., referred to technical, etc.). The buyer is able to consolidate these PRs with the instant procurement,

Defense Logistics Agency Comments

when appropriate, thereby possibly reducing overall LRT and the price paid. The DoDIG recommendation that a buyer with a purchase request aging in referral be notified of an award for the same item provides no value added since notification after the fact cannot reduce LRT. DSCR will emphasize consolidation or PRs aging in referral in guidance to be issued under recommendations A.2.b. and A.2.c. of this report.

DISPOSITION:

- Action is ongoing. ECD: March 31, 1999
- Action is complete.

RECOMMENDATION A.2.e: Recommend that the Commander, Defense Supply Center, Richmond direct buyers to either use the Defense Logistics Agency Pre-Award Contracting System to refer and monitor purchase requests referred to technical or supply operations personnel or modify the Workload Tracking System to interface with and update the Standard Automated Materiel Management System and the Defense Logistics Agency Pre-Award Contracting System.

DLA COMMENTS: CONCUR. DSCR is currently transitioning from DPACS to DPACS Graphical User Interface (GUI). Once DPACS GUI has been deployed, DSCR plans to provide Technical Specialists online access to receive and reply to PR referrals, which will eventually eliminate the need for the current Workload Tracking System for PR suspensions.

DISPOSITION:

- Action is ongoing. ECD: DPACS GUI is scheduled to be deployed by March 31, 1999. When deployment occurs, estimated completion is 90 days after full deployment.
- Action is complete.

FINDING B: Logistics Response Time Goals and Performance Measurement.

Although DoD established a corporate goal to reduce LRT, subordinate and supporting goals were not established at DSCR. Specifically, DSCR did not establish goals to reduce LRT for DVD and did not use the Method of Support Model or an alternative method to optimize cost-effectiveness and responsiveness to customer requirements of DVD processes. As a result, there was no assurance that DVD would contribute to achieving the DoD goal to reduce LRT.

DLA COMMENTS: CONCUR. The DLA Strategic Plan contains goals and objectives to ensure that DLA meets mission requirements to provide acquisition and logistics support to our myriad of customers through teamwork and partnership. Those goals and

objectives, while not expressly stated, include the goal to reduce LRT. The basis of effective partnering with our customers and vendors to develop and implement reengineered commercial business practices that take advantage of our national buying power and emerging technology contain a fundamental principle that the arrangement sought must improve service to the customer. LRT is the most visible area to effect change and DLA will establish LRT goals for our innovative contracting solutions that provide for planned DVD.

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- Concur
- Nonconcur

RECOMMENDATION B.1: Recommend that the Commander, Defense Supply Center, Richmond establish goals for logistics response time for direct vendor delivery for consumable hardware items.

DLA COMMENTS: CONCUR. By memorandum dated December 22, 1998, DLA advised the Hardware ICPs that a goal will be established for planned DVD and requested that each ICP review their established long term contracts that provide for planned DVD and advise why long Procurement Lead Times (PLTs) were established on some arrangements and why vendors were not shipping within established timeframes. Results are anticipated February 2, 1999.

DISPOSITION:

- Action is ongoing. ECD: March 31, 1999
- Action is complete.

RECOMMENDATION B.2: Recommend that the Commander, Defense Supply Center, Richmond, optimize the cost-effectiveness and responsiveness to customer requirements of the direct vendor delivery process by using the Method of Support Model or an alternative method.

DLA COMMENTS: CONCUR. The Corporate Contract Decision Tool (CCDT) is an automated method of comparing the relative benefits of depot stockage versus DVD

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similar to the Method of Support Model. Training has already been provided to DSCR personnel and the model is being fielded for use at DSCR.

DISPOSITION:

- Action is ongoing. ECD: January 31, 1999
- Action is complete.

ACTION OFFICER: Amy Sajda, DLSC-PPB, (703) 767-1368

REVIEW/APPROVAL: Thomas D. Ray, Assistant Executive Director (Procurement Operations), (703) 767-1455

COORDINATION: Mimi Schirmacher, DDAI

DLA APPROVAL:



E.R. CHAMBERLIN
Rear Admiral, SC, USN
Deputy Director

Audit Team Members

The Readiness and Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, DoD, produced this report.

Shelton R. Young
Raymond D. Kidd
Hassan A. Soliman
Lieutenant Colonel Diana E. Francois, U.S. Air Force
Donney J. Bibb
Joel E. McLeod
Timothy E. Moore
Elizabeth A. Lucas
Steven G. Schaefer
Lam Ba Nguyen
Cheryl L. Snyder