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**REPORT TO THE SUBCOMMITTEE
ON GOVERNMENT PROCUREMENT
SELECT COMMITTEE
ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES**



**Review Of The Savings
Expected From Centralization
Of The Procurement And Storage
Of Vehicles Repair Parts** B-114874

Post Office Department

**BY THE COMPTROLLER GENERAL
OF THE UNITED STATES**

FEB. 17, 1971

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COMPTROLLER GENERAL OF THE UNITED STATES

WASHINGTON, D.C. 20548

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Dear Mr. Chairman:

Further reference is made to your letter of May 6, 1970, that transmitted copies of correspondence from the House Post Office and Civil Service Committee's Subcommittee on Postal Operations, the National Small Business Association, and the Automotive Service Industry Association, requesting that we examine into the Post Office Department's proposed plan to centralize the procurement and storage of motor vehicle repair parts at Topeka, Kansas. We were subsequently requested to limit our examination to ascertaining the reasonableness of the Department's estimated annual savings of \$4.7 million that would be achieved under the plan. H02911 D2426 D2427 D. 1799

In accordance with the arrangements made later with your office, we terminated our review before its completion, because the then-pending legislation (the Postal Reorganization Act of 1970) granted the Department broad procurement authority. We are furnishing you with a summary of the results of the limited review.

Our review was conducted at the Post Office Department headquarters and the vehicle maintenance facility in Washington, D.C., and at the office of the consultant firm that developed the historical data used by the Department in the development of the proposed procurement plan.

Because of our limited review, we cannot conclusively state what, if any, savings may result from central procurement and storage of motor vehicle repair parts. We believe, however, that the estimated savings of \$4.7 million were not realistic, because the estimate was based on faulty comparative-pricing data and questionable estimates of costs to operate a central procurement and storage system.

The Department started implementing the centralized procurement and storage plan, and, as of December 14, 1970, the Department had awarded about 100 contracts for approximately 500 different types of repair parts costing about \$1.1 million. According to a Department official, the storage area for the

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vehicle parts at Topeka has been established and funds have been made available for employees to operate the facility.

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We have not requested the Post Office Department or the consultant firm to review or formally comment on the information in this report. We plan to make no further distribution of this report unless copies are specifically requested, and then we shall make distribution only after your agreement has been obtained or public announcement has been made by you concerning the contents of the report.

Sincerely yours,



Comptroller General
of the United States

The Honorable James C. Corman, Chairman
Subcommittee on Government Procurement
61 Select Committee on Small Business H06101
House of Representatives

GENERAL ACCOUNTING OFFICE REVIEW OF
SAVINGS EXPECTED FROM CENTRALIZATION OF
PROCUREMENT AND STORAGE OF VEHICLE REPAIR PARTS
POST OFFICE DEPARTMENT

STUDY MADE BY THE CONSULTANT FIRM

On April 23, 1968, the Department awarded a contract for about \$260,000 to a consultant to make a motor vehicle logistics study. According to the contract's scope of work, this study:

"Shall include development of mortality data. Establish inventory control procedures, user and depot stock levels, parts identification including assignment of Federal stock numbers, and preparation of repair parts catalogs concerning selected lines of repair parts used in the United States Post Office Department vehicle fleet."

The consultant's study covered 5,000 types of repair parts used by the Department. Because of low usage of some of the parts, interchangeability with other parts, low cost of other parts, and parts included in sets and/or kits, the consultant recommended for initial stocking at a central storage facility in Topeka, Kansas, only 1,011 types of repair parts. Under its proposed central procurement system, the Department was interested in stocking only those parts which have a high turnover-use rate and which have large retail markups. Therefore the proposed system would provide only certain parts for vehicles, and the vehicle maintenance facilities (VMFs) would continue to purchase all other parts directly from suppliers.

In April 1969, the consultant completed its initial list of parts and quantities recommended for central stockage without giving consideration to pricing data. This was in accordance with contract terms. In November 1969, the Department received pricing data from the consultant for the 1,011 repair parts. We were informed by the contracting officer's representative that the pricing data had been provided as a courtesy, without cost to the Department.

POST OFFICE DEPARTMENT'S ESTIMATED
SAVINGS OF \$4.7 MILLION UNDER
PROPOSED PROCUREMENT PLAN

The Department operates about 270 VMFs throughout the country to maintain its fleet of about 83,000 vehicles. The VMFs are responsible for procuring and storing the repair parts needed to service the vehicles assigned to them. VMFs procure about half of the repair parts by ordering them under General Services Administration contracts and procure other repair parts from local vendors.

According to the pricing data developed by the consultant, the central procurement of the recommended quantities of the 1,011 repair parts would cost about \$3.3 million annually, whereas, under the present system, the VMFs procurement of the same quantities of repair parts would cost about \$4.9 million. Therefore central procurement of these parts would result in annual savings of about \$1.6 million, or 33 percent.

On the basis of these data, the Department estimated that savings of about \$5.3 million would be realized in fiscal year 1972 by centrally stocking about 3,000 parts to support about 80,000 vehicles. The Department estimated that the annual cost of centrally procuring such parts would be \$10.7 million, whereas the estimated annual cost for VMFs to procure the parts locally would be about \$16 million. After deducting estimated costs of \$600,000 to operate the proposed centralized procurement system, the Department estimated net annual savings of \$4.7 million.

GAO'S EVALUATION OF DEPARTMENT'S
ESTIMATED SAVINGS OF \$4.7 MILLION BY 1972

Because the Department's estimated savings of \$4.7 million were based on a projection of the savings computed for 1,011 parts, we directed our efforts to evaluating the pricing data for these parts. Any deficiencies noted in the pricing of the 1,011 parts would therefore be magnified in the Department's estimated savings of \$4.7 million.

Following are the deficiencies noted in the computation of the estimated savings of \$1.6 million on the 1,011 repair parts.

Pricing data

We were advised by the Department that the consultant obtained local pricing data on the 1,011 parts from the records at 36 VMFs. At the time of our inquiry, however, the consultant had disposed of the supporting documents relating to the pricing data obtained at 25 of the VMFs.

The consultant, in computing the average VMF prices, used the Washington, D.C., VMF prices as a guide. For example, the consultant advised the Department that, when the prices extracted from records at the various VMFs appeared questionable, it made adjustments based on Washington VMF prices.

To test the savings estimated by the consultant, we selected for review 100 parts which we could readily identify in the Washington VMF parts records and on which sufficient information had been on the records to enable us to compute reliable prices. Although we could not determine the specific source of the consultant's prices for most of the 100 selected parts, we used the Washington VMF prices in our test because the consultant said that he had relied heavily on the Washington VMF prices.

The data we obtained from the Washington VMF parts records showed that the average price for most of the 100 parts was less than the average VMF price established by the consultant for these parts. Since the estimated savings to be realized through the central procurement plan were based on the difference between the anticipated central procurement price and the VMF price, any such reduction in the estimated average VMF price would also result in reducing the estimated savings.

We do not know how many of the consultant's prices were based solely on the Washington VMF prices, but we found that the prices of two parts were. The following table shows the differences between the consultant's prices for the two parts and the prices we obtained at the Washington VMF for these parts and the resulting differences in savings.

Part	Quantity	Estimated VMF price		Consultant's estimated central procurement price	Price savings		Overstatement of savings
		Consultant	GAO		Consultant	GAO	
A	25,000	\$2.15	\$1.03	\$0.63	\$38,000	\$10,000	\$28,000
B	6,000	2.26	1.02	0.62	9,840	2,400	7,440

The overstatement of savings occurred because the consultant appeared to have used the highest prices rather than the average of all prices paid for the same part over a period of time.

By comparing the estimated VMF prices with the estimated central procurement prices, the consultant computed a price differential savings of 30 percent that would be realized if the parts were purchased centrally.

The consultant obtained historical pricing data from VMF records for about 50 percent of the 1,011 parts. For the other parts, the consultant estimated the VMF prices by adding 30 percent to the estimated central procurement prices. The consultant's representative advised us that the estimated central procurement prices for parts had been obtained from suppliers' parts catalogues and informal price quotations from other automotive parts suppliers. We were unable to verify the estimated central procurement prices because of the lack of adequate supporting documentation. The consultant also used the 30-percent price differential--that is, it deducted 30 percent from the VMF prices--to estimate the central procurement price of certain parts, when central pricing information had not been obtained.

Mathematical errors

Mathematical errors resulted in overstating by about \$500,000 the estimated savings relating to the 1,011 parts proposed for initial central procurement and stockage.

Costs to operate and administer the program

The Department considered in its calculation of annual savings of \$4.7 million in 1972 that annual in-house costs of \$600,000 would be incurred in operating the centralized vehicle repair parts program consisting of centralized warehousing costs of \$100,000 (salaries, \$80,000; facility maintenance, \$7,000; operating costs, \$13,000) and shipping costs of \$500,000.

On the basis of our limited review of the Department's records and interviews with a procurement official, we question whether the Department's estimate of the annual savings was reasonable and whether it was based on a consideration of all the cost factors that would be applicable to such an operation. Our observations on the Department's estimate of operation and administrative costs are as follows:

Fringe benefits--The salary cost of \$80,000 was based on 10 employees having an average salary of \$8,000. We did not determine the reasonableness of the staffing complement, however, the Department's estimate did not include fringe benefits. On the basis of data furnished by the Department, we estimate that fringe benefits will amount to an additional \$18,000 annually.

Shipping costs--The Department included an estimated shipping cost of \$500,000 based on 5 percent of the estimated annual cost of repair parts. A procurement official told us that this cost represented the cost of shipping by commercial carrier, but he did not provide any supporting data. We question whether transportation costs can be directly related to the cost of the parts shipped, since most transportation rates are based on distance, weight, and/or volume. Department records indicate that the Department would use the parcel post system to ship the parts. Since parcel post rates are based on weight and the distance shipped, we believe that it was not reasonable for the Department to estimate shipping costs as a direct percentage of the costs of repair parts.

The Department did not include other costs of maintaining an inventory of repair parts such as obsolescence, pilferage, and interest on investment in the inventory. Although certain of these costs are being incurred under the present system, we believe that any differences in such costs that are related

solely to the centralized procurement system should be recognized in the cost comparisons.

CONCLUSIONS

Because of our limited review, we cannot conclusively state what, if any, savings may result from the central procurement and storage of the repair parts. We believe, however, that the estimated savings of \$4.7 million are not realistic because the estimate was based on faulty comparative-pricing data and questionable estimates of costs to operate a central procurement and storage system.