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BY THE U.S. GENERAL ACCOUNTING OFFICE

## Report To The Secretary Of Defense

# Procurement To Satisfy Requisitions For Out-Of-Stock Material Could Be Reduced

The Navy needs to improve its procedures and practices for responding to requisitions for material which cannot be filled from stock on hand. Opportunities exist for the Navy to reduce the volume of costly spot buys through (1) greater use of existing replenishment purchase order contracts, (2) prompt and effective processing of cancellation requests for nonstocked items, and (3) proper assignment of priority designators to requisitions.



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UNITED STATES GENERAL ACCOUNTING OFFICE  
WASHINGTON, D.C. 20548

NATIONAL SECURITY AND  
INTERNATIONAL AFFAIRS DIVISION

B-211969

The Honorable Caspar W. Weinberger  
The Secretary of Defense

Attention: Office of GAO Report Analysis

Dear Mr. Secretary:

We have reviewed the Navy's procedures and practices for responding to requisitions which cannot be filled from stock on hand. Such requisitions are for items not normally stocked or for stockage items whose inventory has been drawn down. In such cases, a common practice is to make a single purchase, referred to as a spot buy. The Navy could save millions of dollars annually in administrative and procurement costs by (1) relying more on existing replenishment contracts rather than making spot buys, (2) promptly processing customer cancellation requests, and (3) requiring customers to properly assign priority designator codes to their requisitions.

The Navy has two principal inventory control points where these requisitions are received. These are the Ships Parts Control Center (SPCC), Mechanicsburg, Pennsylvania, and the Aviation Supply Office (ASO), Philadelphia, Pennsylvania. These activities have developed local guidelines under which requisitions for out-of-stock material are either backordered, filled by reconsignment from an existing stock replenishment contract, or filled by a spot buy or repair action. Basically, spot buys are supposed to be limited to high priority requisitions. However, spot buys may be made to satisfy any requisition for a nonstocked item.

When spot buys are made, the contract usually provides for delivery of the items directly from the contractor to the user. At the time of our review (Apr. through Dec. 1982), SPCC and ASO files contained about 100,000 direct delivery actions for material valued at about \$307 million. We reviewed the practices and procedures of these two activities to determine their effectiveness in processing requisitions for out-of-stock material. We randomly selected open requisitions from the document status files at each activity.

The sample included requisitions for both stocked and nonstocked items. In addition to reviewing files and interviewing personnel at SPCC and ASO, we visited the Philadelphia Naval Shipyard to determine the procedures for assigning priority designator codes to their requisitions. Our review was made in accordance with generally accepted government auditing standards.

GREATER USE COULD BE MADE OF  
EXISTING REPLENISHMENT BUYS

To fill requisitions for nonstocked items, inventory activities must buy the items. Thus, spot buys in these instances are routine. However, requisitions for stocked items are not supposed to be routinely handled this way. Before deciding to spot buy stocked items, inventory activities are supposed to consider the priority of the requisition and whether it can be filled from stock due in from a normal replenishment contract. In these cases, the stock is normally shipped from the contractor to depots, but some of the items can be directed for shipment to the user. This is referred to as reconsignment. The practices followed by ASO and SPCC differ significantly.

At ASO, officials told us that their present practice regarding requisitions for stocked items is to backorder the requisition when reconsignment is not feasible and that they do not spot buy stocked items under any circumstances. Our review of randomly selected requisitions from Navy users supported this. Of 130 sample items selected, 54 were for stocked items. Only one spot buy had been made.

At SPCC, practices and procedures were not equally effective. This activity's procedures require that inventory managers try to expedite delivery of material due in on awarded contracts but do not require any special attention if a contract has not yet been awarded, i.e., still in a purchase request status. If they cannot get early delivery, in certain instances managers are supposed to try reconsignment. We found that spot buys were being made for items that could be furnished just as promptly, and often at less cost, from a replenishment buy in process.

At SPCC, decisions to make spot buys are made by the inventory manager rather than by the buyer of material, who has firsthand knowledge on the status of procurement actions. Therefore, the inventory manager may not be aware that a pending purchase request or contract for a stock replenishment buy will afford earlier delivery than a just-initiated spot buy. Compounding the problem is the fact that SPCC buyers are

assigned purchase requests, from which to award contracts, based on dollar value. Therefore, different buyers, and even different branches within the purchase division, may be responsible for procuring a single item.

The quantity and value of spot buys for stock items by SPCC have increased over the past 5 years, as shown by the following table.

<u>Fiscal year</u>	<u>Number of awards</u>	<u>Dollar value</u> (millions)
1978	20,559	\$ 54.0
1979	23,358	70.8
1980	18,677	73.3
1981	24,297	88.4
1982	26,406	148.5

In May 1982, SPCC's document status file contained 25,941 customer requisitions for stocked items, in direct delivery status, having a total value of \$126 million. We randomly selected 100 of these valued at \$272,000 for review. Fifty-six were spot buys; 28 were reconsignments; 8 were repair orders; and in 8 instances, supply action had not been decided. We followed up on these last eight requisitions to determine what actions had been subsequently taken. No action was taken on four, three were canceled by the requisitioning units, and one was filled from stock received as a result of a routine replenishment buy.

Of the 56 spot buys, we concluded that 25 were not necessary because, in most instances, stock replenishment buys would have provided the material just as promptly or even before delivery on the spot buy. The prices paid for material on these 25 spot buy contracts were, on the average, 24 percent higher than the prices paid for the same material on replenishment contracts. Also, the average administrative cost to award a spot buy contract is \$175, which could have been avoided. Following are examples of costly spot buys which we believe were unnecessary.

--On March 12, 1982, SPCC initiated a purchase request for 10 motor takeup reels for stock replenishment. This request resulted in a contract being awarded on June 24, 1982, at a unit price of \$1,243, with delivery scheduled on January 20, 1983. On March 24, 1982, 12 days after the purchase request for stock replenishment

was initiated, SPCC received a high priority requisition for one motor takeup reel. On September 2, 1982, a little over 2 months after the stock replenishment contract was awarded, a spot buy was awarded to the same contractor at a unit cost of \$6,150, nearly five times the price being paid on the replenishment contract. Further, the scheduled delivery date under the spot buy contract was March 31, 1983, or more than 2 months after scheduled delivery from the replenishment buy.

--On July 13, 1981, SPCC initiated a purchase request for four extractors for stock replenishment. This request resulted in a contract being awarded on October 1, 1981, at a unit price of \$115 with delivery scheduled for March 2, 1982. On August 2, 1981, 20 days after initiating a purchase request for stock replenishment, SPCC received a high priority requisition for one extractor. On October 9, 1981, 8 days after the stock replenishment contract was awarded, a spot buy contract was awarded for one extractor at a cost of \$457, nearly four times the stock replenishment price. Further, delivery under the spot buy contract was scheduled for October 20, 1982, more than 7 months after the expected delivery date of the stock replenishment contract.

--On May 7, 1981, SPCC received a priority requisition for one circuit card assembly and awarded a spot buy contract for it on February 26, 1982, at a cost of \$3,276. Delivery under the spot buy contract was scheduled for September 29, 1983. When the spot buy requisition was received, SPCC had a stock replenishment contract with the same contractor for delivery on March 15, 1982. The unit price under the replenishment contract was only \$1,397, or \$1,879 less than the spot buy cost.

--On June 21, 1981, SPCC received a priority requisition for a salinity indicator cell and on September 25, 1981, awarded a spot buy contract at a unit cost of \$345, with delivery scheduled for December 4, 1981. When the spot buy requisition was received, SPCC had a stock replenishment contract for a quantity of 1,200 cells at a unit price of \$145, \$200 less than the spot buy price. Also, scheduled delivery under the stock replenishment contract was more than 1 month sooner than the spot buy delivery date.

We selected requisitions for review by using statistical sampling techniques. Assuming these items are representative

of the universe of requisitions in SPCC's document status file, we believe that the activity could save millions of dollars annually in procurement and administrative costs by making greater use of replenishment buys.

SPCC officials generally agreed with our findings, but stated that increased administrative costs, resulting from separate spot buy contracts, would be offset somewhat by costs associated with reconsignment action in instances when that was the alternative. They also agreed that the buyer probably should be making the decision about how to best obtain the material, rather than the inventory manager. They stated that the responsibility for making spot buy decisions has been under consideration and that under a recent command reorganization, all items are to be procured by a single section and hopefully the same buyer. As stated previously, under the old organization, depending on the dollar value of the buy, the same item could be purchased under separate awards by different buyers.

CANCELLATION REQUESTS FOR NONSTOCKED  
ITEMS NEED TO BE PROCESSED PROMPTLY

Navy procedures require that inventory control points try to cancel requisitions if asked to do so by the requisitioning units. If a contract has already been awarded, inventory managers should attempt cancellation if the value of the requisition is \$200 or more. If a contract has not been awarded, the requisition is supposed to be canceled, regardless of the dollar amount.

Requests to cancel requisitions for stocked items are automatically processed by the computer. We found no problems in processing cancellation requests for such items. However, neither of the inventory control points is effectively handling requests to cancel requisitions for nonstocked items.

At ASO, we found that no attempts were being made to process requests to cancel requisitions for nonstocked items. They are rejected by the computer and are to be processed manually by the technical division. However, that division was not processing them. ASO officials said that there was insufficient time to process these requests because of a lack of personnel.

In July 1982, ASO's document status file contained 31,794 direct delivery actions. From these, we selected a random statistical sample of 130 requisitions from Navy activities. Of these, 76 were for nonstocked items. We examined the

status of all 76 requisitions and found that in 55 instances (72 percent) cancellation requests had been received from the customers. But they had not been processed. The 55 cancellation requests were for items valued at about \$18,500, or \$336 per requisition. Of the 55 cancellation requests, 24 were received before the contracts were awarded. The other 31 cancellation requests were received after the contracts had been awarded, but delivery of the material was often far into the future. For example, 8 of the 31 cancellation requests, valued at \$9,300, were received 90 or more days prior to the scheduled contract delivery dates.

ASO maintains a log of cancellation requests rejected by the computer for manual processing. For a 2-month period in late 1982, this log showed that ASO was receiving about 500 cancellation and followup requests weekly that were not processed. Since these items are not stocked in the system and the requisitioning customers no longer need them, failure to cancel procurement of such items results in a waste of money spent to buy them. Therefore, every effort should be made to cancel requisitions/contracts for nonstocked items. Following are some examples of cancellation requests that were not processed.

- On December 10, 1981, ASO received a requisition for a bushing assembly and on March 28, 1982, received a cancellation request from the customer. ASO awarded a contract for the bushing assembly nearly 2 months after receiving the cancellation request.
- On February 2, 1982, ASO received a requisition for 12 clamps and on June 20, 1982, the requisition was canceled. ASO awarded a contract for the clamps about 3 weeks after the cancellation request was received.
- On May 30, 1980, ASO received a requisition for a keeper and about 6 weeks later, ordered the material at a cost of \$203. The customer canceled the requisition 2 weeks after the order was placed. Even though delivery was not scheduled until April 1, 1982 (20 months after the cancellation request), and the contract value exceeded \$200, ASO took no action to cancel it.
- On February 3, 1981, ASO received a requisition for six bolts and on March 4, 1981, ordered the material at a cost of \$2,972. About 2 months after the order was placed, ASO received a cancellation request. Although the contract value exceeded \$200 and delivery was not scheduled until January 1982, or about 8 months after

receipt of the cancellation request, ASO took no action to cancel it.

At SPCC, we selected a random statistical sample of 100 requisitions for nonstocked items from the document status file on October 4, 1982. For these, seven cancellation requests had been received from customers. Based on current procedures, SPCC personnel were required to attempt cancellation on four of the seven requests, but took action on only one. We found no evidence of any action on the remaining three requests, even though it was several months between the cancellation request dates and scheduled delivery and the contract values exceeded \$200.

Despite the low rate of cancellation attempts at SPCC (7 percent), we believe that prompt action on cancellation requests could result in significant savings in procurement costs. As of October 4, 1982, there were 45,783 requisitions for nonstocked items in the SPCC document status file valued at \$28.3 million.

CUSTOMERS IMPROPERLY STATE THEIR  
URGENCY OF NEED FOR MATERIAL

Our review of requisitions submitted by one major user--the Philadelphia Naval Shipyard--disclosed that priority designator codes assigned to requisitions do not properly reflect the urgency of need for the items. Many requisitions which should have been coded to reflect routine processing were coded with a high priority code. As a result, SPCC made spot buys and, as previously discussed, incurred unnecessary procurement and administrative costs.

Priority designator codes (ranging from 01 to 15) are assigned to requisitions by customers and are the basis for expressing the urgency of need for material. Codes 01 through 03 are considered high priority material requirements and, for these, SPCC generally authorizes spot buys. Depending on the situation, spot buys may also be authorized to satisfy priority codes 04 through 08 requisitions. Requisitions with priority codes 09 through 15 are subject to routine processing and spot buys are not authorized.

We initially reviewed 27 requisitions included in the SPCC document status file as of May 8, 1982, that had been received from the Philadelphia Naval Shipyard. All 27 requisitions were coded either priority 02 or 03, indicating that the material was required for immediate use. Nine of the 27 requisitions (33.3 percent) were erroneously coded because the material was requisitioned in advance of the scheduled overhaul of two ships. Generally, codes 11 through 15 are to be

used when material is ordered in advance of the scheduled repair/maintenance or replacement of equipment.

Of the nine requisitions, three for the U.S.S. LUCE overhaul were submitted about 4 months prior to the overhaul start date. Initially these were assigned a priority code 13, but were upgraded to a priority 03 at 45 days before overhaul start date. The other six requisitions, for the U.S.S. FORRESTAL overhaul, were submitted at various times prior to the overhaul start date. Initially they were assigned a priority code 12, but were upgraded to priority code 02 or 03 nearly 10 months before overhaul start date.

We discussed these requisitions and their assigned codes with shipyard officials. They told us that their policy is to requisition material using priority designator 12 or 13 about 1 year prior to the ship overhaul start date. About 60 days prior to the overhaul start date, the requisitions are to be upgraded to priority 05 or 06, and at 30 days prior to overhaul start, upgraded to priority 02 or 03. However, to assure availability of material in time for the U.S.S. FORRESTAL overhaul, they said that outstanding requisitions were upgraded to priority 02 or 03 in March 1982. This was about 10 months prior to the overhaul start date.

After our discussions with shipyard officials, we scanned SPCC's document status file to determine the extent of open requisitions from the shipyard. The file contained 245 erroneously coded high priority requisitions valued at \$2.1 million from the shipyard for the U.S.S. FORRESTAL. Of these, 200 had resulted in spot buys. We examined 54 of the 200 requisitions and found that 18 were unnecessary because replenishment buys were in process and had scheduled delivery dates either earlier than the spot buy delivery or prior to the FORRESTAL overhaul start date.

While our review at the requisitioning level was limited to one major user, the practice of improperly coding requisitions appears widespread, as evidenced by a Naval Audit Service report. That report, dated August 7, 1980, was the result of a multilocation audit and noted that a significant number of material requisitions with erroneous priority designators were being issued. That review included a cross section of 23 naval shore activities classified into five types: naval shipyards, naval air stations, Marine Corps air stations, naval air rework facilities, and naval supply centers. As a result of reviews at the 23 activities, the Naval Audit Service found that error rates for priority designators ranged from 10 percent for naval air rework facilities to 65 percent for naval shipyards. They estimated that because of erroneous priority designators assigned by stock points, as many as

2,195 requisitions in the document status files at SPCC and ASO from October 1, 1978, through June 17, 1979, could have resulted in unnecessary spot buys.

CONCLUSIONS AND RECOMMENDATIONS

The Navy could save millions of dollars annually in procurement and administrative costs by reducing the number of spot procurements to satisfy requisitions for out-of-stock material. Accordingly, we recommend that the Secretary of Defense assure that the Navy implements effectively the following actions:

- Inventory managers should establish the necessary procedures to assure that replenishment procurements are fully considered prior to making spot buys.
- Inventory managers should comply with procedures for canceling requisitions/procurements upon request of the customers.
- Requisitioning activities should comply with procedures for assigning priority designators to requisitions.

AGENCY COMMENTS

DOD and Navy agreed with our position on spot buy procedures at SPCC and noted that since we completed our review the purchasing functions at SPCC had been consolidated. As a result, inventory managers now need contact only one group of people to get contract information and delivery schedules. According to DOD, this should make inventory managers more aware of the potential for supplying high priority requisitions from replenishment contracts and will permit more cost effective decisions on the potential for reassignment from existing contracts.

They also agreed with our position that users improperly code requisitions for material and that the inventory control points do not effectively process requests from users to cancel requisitions. They stated that ASO and SPCC managers are reviewing their procedures for handling cancellation requests and noted that the need for coordination between inventory managers and buyers is being emphasized. They also stated that the purchasing division is developing procedures to promptly identify cancellation requests and that special attention will be given to such requests for items not normally stocked in the system.

In agreeing with our conclusions and recommendations, DOD noted that procedures for making spot buys and for

processing cancellation requests are now in place and that the inventory control points' progress in implementing them will be closely monitored. DOD stated that both subjects would be proposed as special interest items for command inspectors general and contract management reviews. In view of this, DOD stated there is no need for the Secretary to direct this action, as recommended in the draft. DOD also agreed with our recommendation for properly coding requisitions and stated that a method to monitor compliance with procedures is under consideration. It stated that the most effective method would be selected and applied, but also stated that there is no need for the Secretary to direct this action. We are encouraged by DOD's positive response to our recommended actions, and we agree that in these circumstances it is not necessary for the Secretary of Defense to direct the Navy to act. We believe, though, that the Secretary should monitor the Navy's actions to assure that they are effectively implemented. We have modified our recommendations accordingly. The agency's comments on matters discussed in this report are attached as an appendix.

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As you know, 31 U.S.C. § 720 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Director, Office of Management and Budget; the Secretary of the Navy; and the chairmen of the appropriate congressional committees.

Sincerely yours,



Frank C. Conahan  
Director



SS  
MANPOWER,  
RESERVE AFFAIRS  
AND LOGISTICS

ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D.C. 20301

10 JUN 1983

Mr. Donald J. Horan  
Director, Procurement, Logistics  
and Readiness Division  
General Accounting Office  
Washington, D. C. 20548

Dear Mr. Horan:

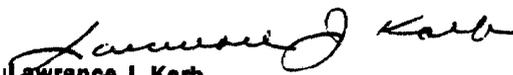
This is in response to your Draft Report, "Procurements To Satisfy Requisitions For Out-Of-Stock Material Could Be Reduced," Dated April 6, 1983 (GAO Code No. 943198) (OSD Case No. 6234).

Comments received from the Navy have been considered in preparing the enclosed detailed response which addresses the findings, conclusions and recommendations contained in the Draft Report.

We appreciate the opportunity to comment on this report in draft form.

Sincerely,

Enclosure  
As stated

  
Lawrence J. Korb  
Assistant Secretary of Defense  
(Manpower, Reserve Affairs, and Logistics)

GAO DRAFT REPORT, DATED APRIL 6, 1983  
(GAO CODE NO. 943198) OSD CASE NO. 6234

"Procurements To Satisfy Requisitions For Out-Of-Stock  
Material Could Be Reduced"

DOD RESPONSE TO FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

FINDINGS

FINDING A: Practices Regarding Requisitions For Stocked Items Differ Significantly at Naval Control Points. GAO found that practices followed by the Aviation Supply Office (ASO), Philadelphia, Pennsylvania and the Ships Parts Control Center (SPCC), Mechanicsburg, Pennsylvania, differ significantly regarding requisitions for stocked items: (1) at ASO the present practice is to backorder the requisition when reconsignment is not feasible and not to spot buy under any circumstance, and (2) at SPCC spot buys are made for items that could be furnished just as timely, and often at less cost from a replenishment buy. GAO further found that SPCC procedures require that inventory managers (1) attempt to expedite delivery of material due-in on awarded contracts but do not require any special attention if it is still in a purchase request status and (2) if early delivery can't be made, in certain instances they are supposed to attempt reconsignment action. (GAO noted that these Navy control points have guidelines under which requisitions for out-of-stock items, i.e., items not normally stocked or stocked items for which the inventory has been drawn down, are either back ordered, filled by reconsignment from an existing stock replenishment contract, or filled by a spot buy or repair action. GAO further noted that spot buys (single purchases) are normally limited to high priority requisitions but may be used to satisfy requisitions for nonstock-numbered items. Requisitions for stocked items are not supposed to be routinely handled this way--should consider the priority and whether the requisition could be filled from stock due-in

from a normal replenishment contract). (pp. 1, 2, 2a, 3, 4, 5, and 6, GAO Draft Report)

DoD Comment: Concur. Since GAO completed its study at SPCC, a functional reorganization has taken place. Purchasing, which had been split between specialists who handled replenishment requisitions and other specialists who performed spot buys, has been consolidated. As a result, inventory managers can now go to one group of people to get consolidated information on contracts awarded, in process, and the related delivery schedules. This improved information will allow the inventory manager, in conjunction with the purchase agent, to make a cost-effective decision regarding the potential for reassignment from existing contracts. To insure that SPCC is reducing its number of spot buys, NAVSUP will propose this as a continuing interest item from its IG reviews. Also note that differences in requisition processing by ICPs are not always a sign of management deficiencies. ICPs need the freedom to establish procedures to meet different customer needs, and in dealing with a different industrial base.

FINDING B: Spot Buy Decisions Are Being Made By SPCC Inventory

Managers. GAO found that at SPCC (1) decisions to make spot buys are made by the inventory managers rather than the buyer of material who has first-hand knowledge on the status of procurement actions, (2) the inventory manager may not be aware of a pending purchase request or a contract for a stock replenishment buy that might afford better delivery than a just-initiated buy, and (3) SPCC buyers are assigned purchase requests from which to award contracts based on dollar value--therefore, different buyers/branches may be responsible for procurement of a single item. (GAO noted that SPCC officials stated that the decision

responsibility for spot buys has been under consideration and they agreed that probably the buyer should be making the decision about how to best obtain the material). (pp. 3 and 6, GAO Draft Report)

DoD Comment: Concur. Under SPCC's reorganization, responsibilities for procurements of a particular item rest within a single group. This change allows the item manager to have a single source of information about possible alternatives for meeting a requirement.

It is DoD's position that it is the item manager, in conjunction with the buyers, who has the ultimate authority to meet the requirement at least cost. SPCC's reorganization was made to reinforce this basic responsibility while providing the item manager with necessary and sufficient information to make effective decisions.

FINDING C: Greater Use Of Stock Replenishment Buys Could Reduce Costs at SPCC. Through a random selection at SPCC of 100 of 25,941 customer requisitions for stocked items, GAO found that (1) 56 were spot buys, 28 were reconsignments, 8 were repair orders, and 8 were undecided supply actions, (2) 25 of the 56 spot buys were unnecessary as stock replenishment buys would have provided the material just as timely or even before delivery on the spot buy, (3) prices paid for these 25 spot buys were on the average 24 percent higher than the prices paid for the same material on replenishment contracts and (4) the \$175 average administrative costs to award a spot buy contract could have been avoided. (See pp. 4-6, GAO Draft Report for examples of costly spot buys). GAO further found the quantity and value of spot buys for stocked items at SPCC has increased over the

past five years, i.e., 1978-\$54 million, 20,559 awards, 1982-\$148.5 million, 26,406 awards (GAO noted that SPCC officials generally agreed with the findings, however, they stated that increased administrative costs of spot buys would be somewhat offset by costs associated with reconsignment action where this was the alternative. GAO further noted reconsignment is defined as stock filled from stock due-in from a normal replenishment contract with stock normally shipped from the contractor to depots but some of the items can be directed for shipment to the user). (pp. 2, 3, 4, and 6, GAO Draft Report)

DoD Comment: Concur. SPCC's reorganization should make inventory managers more aware of the potential for supplying high priority requisitions from replenishment contracts in processing prior to award. By comparing smaller quantity spot buy costs to the costs of reconsignment, the item manager will be able to make the best decision. In the short run, the Navy Stock Fund bears the expense of higher spot buy procurement costs.

The fact that a spot buy was ultimately made on a requisition does not mean that other actions were not attempted. SPCC's requisition processing matrix requires the item manager to attempt to expedite delivery and seek out reconsignment before going to spot buy.

Also note that using aggregate dollar amounts for spot buy statistics magnifies the scope of the potential problem because SPCC lumps foreign military sales purchases under the spot buy category.

FINDING D: Cancellation Requests for Nonstock Items Not Effectively Handled at Inventory Control Points Resulted In Unnecessary Costs. GAO found that neither of the inventory control points were effectively handling requests to cancel requisitions for unstocked items, specifically:

- (1) at ASO no attempts were being made to process requests to cancel requisitions for nonstock items--ASO officials stated there was insufficient time to process them due to lack of personnel,
- (2) a random selection of 130 ASO requisitions indicated that for 76 requisitions for nonstocked items 55 cancellation requests (72 percent) had been received but not processed--items valued at \$18,500 or \$336 per requisition. Of these 55 cancellation requests 24 were received before the contracts were awarded with the other 31 received after the contract award but with delivery far into the future,
- (3) ASO's log of cancellation requests, for a 2-month period, showed 500 weekly cancellations and follow-up requests that are not processed, and,
- (4) at SPCC a random selection of 100 requisitions for nonstocked items showed 7 cancellation requests had been received from customers and based on procedures SPCC personnel were required to attempt cancellation on four of the seven requests but had taken action on only one.

GAO further found that since these items are not stocked in the system and the requisitioning customers no longer need them, failure to cancel procurement of such items results in wasted money to buy them. (GAO noted

that Navy procedures require that inventory control points attempt to cancel requisitions if asked to do so by the requisitioning units, and if a contract has already been awarded, cancellation should be attempted if the value of the requisition is \$200 or more--if the contract hasn't been awarded it should be cancelled regardless of dollar amount. GAO further noted that requests to cancel requisitions for stocked items are automatically processed by the computer system whereas requests to cancel requisitions are rejected and processed manually). (pp. 6, 7, 8, and 9, GAO Draft Reprt)

DoD Comment: Concur. ASO and SPCC are currently reviewing internal procedures for effective handling of requests to cancel requisitions for nonstocked items. Emphasis is being placed on the need for coordination between inventory managers and buyers in determining the best method of processing spot buys in terms of delivery and cost. Procedures are being developed to identify cancellation requests for prompt action by the purchase division. Special attention will be given to cancellation requests for items not stocked in the system since these actions cannot be diverted to stock. Compliance with established procedures for effective processing of spot buy awards and cancellations will be proposed as a special interest item for Command Inspectors General and Contract Management reviews.

The reorganization at SPCC of the Inventory Management/Procurement function should aid in the cancellation of contracts before they are issued.

FINDING E: Customers Improperly State Their Urgency of Need For Items

GAO found that priority designator codes assigned to requisitions did not properly reflect the urgency of need for the items, for one major user--

the Philadelphia Naval Shipyard, i.e., requisitions which should have been coded to reflect routine processing were coded a high priority code resulting in costly spot buys. GAO further found that (1) 9 of the 27 requisitions reviewed were erroneously coded because the material was requisitioned in advance of the scheduled overhaul of two ships and (2) SPCC's status file showed there were 245 erroneously coded high priority requisitions valued at \$2.1 million from the shipyard for the USS Forrestal--200 resulted in spot buys. (GAO noted that discussions with shipyard officials indicated their policy is to (1) requisition material using priority designators 12 or 13 about 1 year prior to the ship overhaul date, (2) about 60 days prior to the overhaul date upgrade the requisition to 05 or 06 and (3) at about 30 days upgrade to priority 02 or 03. GAO further noted that officials stated the outstanding requisitions on the USS Forrestal were upgraded to 02 or 03 about 10 months prior to the overhaul date to assure material availability). (pp. 9, 10, and 11, GAO Draft Report)

DoD Comment: Concur. The Draft Report states that "SPCC's status file showed there were 245 erroneously coded high priority requisitions valued at \$2.1 million from the shipyard for the USS Forrestal--200 resulted in spot buys." This statement infers that the spot buys occurred because the requisitions were erroneously coded. Although improper assignment or priorities could lead to spot buys vice reconsignment from existing contracts, it should not be assumed that procurement was not required for the 200 requisitions in question.

FINDING F: The Practice of Improperly Coding Requisitions Appears Widespread.

GAO found that while their review efforts were limited to one major user, the

practice of improperly coding requisitions appears widespread, as evidenced by a Naval Audit Service Report. (GAO noted that the Naval Audit Service Report was the result of a multilocation audit. As a result of reviews at 23 Naval shore activities it was found that error rates for priority designators ranged from 10 percent to 65 percent. GAO further noted it was estimated that because of erroneous priority designators assigned by stock points, as many as 2,195 requisitions in document status files at SPCC and ASO from October 1, 1978 through June 17, 1979, could have resulted in unnecessary spot buys). (p. 11, GAO Draft Report)

DoD Comment: Concur.

#### CONCLUSIONS

CONCLUSION 1. GAO concluded that the Navy could save millions of dollars annually in procurement and administrative costs by reducing the number of spot procurements to satisfy requisitions for out-of-stock material. (p. 12, GAO Draft Report)

DoD Comment: Concur, based on the conditions that existed at SPCC at the time of the review that some level of dollar savings is possible and a reduction in spot buys is anticipated to be one of the benefits of the reorganization of SPCC.

CONCLUSION 2. GAO concluded that opportunities exist for the Navy to reduce the volume of costly spot buys through (1) greater use of existing replenishment purchase order/contracts, (2) prompt and effective processing

of cancellation requests for nonstock items, and (3) proper assignment of priority designators to requisitions. (p. 12, GAO Draft Report)

DoD Comment: Concur. An increasing use of replenishment contracts is expected, as is increases in requisition cancellations processed.

#### RECOMMENDATIONS

RECOMMENDATION 1. GAO recommended that the Secretary of Defense direct the Navy to require inventory managers to establish the necessary procedures to assure that replenishment procurements are fully considered prior to making spot buys. (p. 12, GAO Draft Report)

DoD Comment: Concur in principal. The necessary procedures are in place and the progress made by Navy ICPs will be closely monitored by proposing this topic as a continuing interest item for its IG reviews. Accordingly, there is no need for the Secretary to direct the action.

RECOMMENDATION 2. GAO recommended that the Secretary of Defense direct the Navy to require inventory managers to comply with established procedures for cancellation of requisitions/procurements upon request of the customer. (p. 12, GAO Draft Report)

DoD Comment: Concur in principal. Compliance with established procedures for cancellation of requisitions/procurements upon request of the customer will be assured by proposing this topic as a special interest item for Command Inspectors General and Contract Management Review. Cancellation action will be based on cost

effective considerations and decisions will be documented in appropriate inventory management files for management review. Accordingly, there is no need for the Secretary to direct compliance with the established procedures.

RECOMMENDATION 3. GAO recommended that the Secretary of Defense direct the Navy to require requisitioning activities to comply with established procedures for assigning priority designators to requisitions. (p. 12, GAO Draft Report)

DoD Comment: Concur in principal. Compliance with established procedures will be monitored to assure proper assignment of priority designators. The method in which to monitor compliance is currently under consideration. The most effective method will be selected and applied. Accordingly, there is no need for the Secretary to direct the action.





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