

United States General Accounting Office

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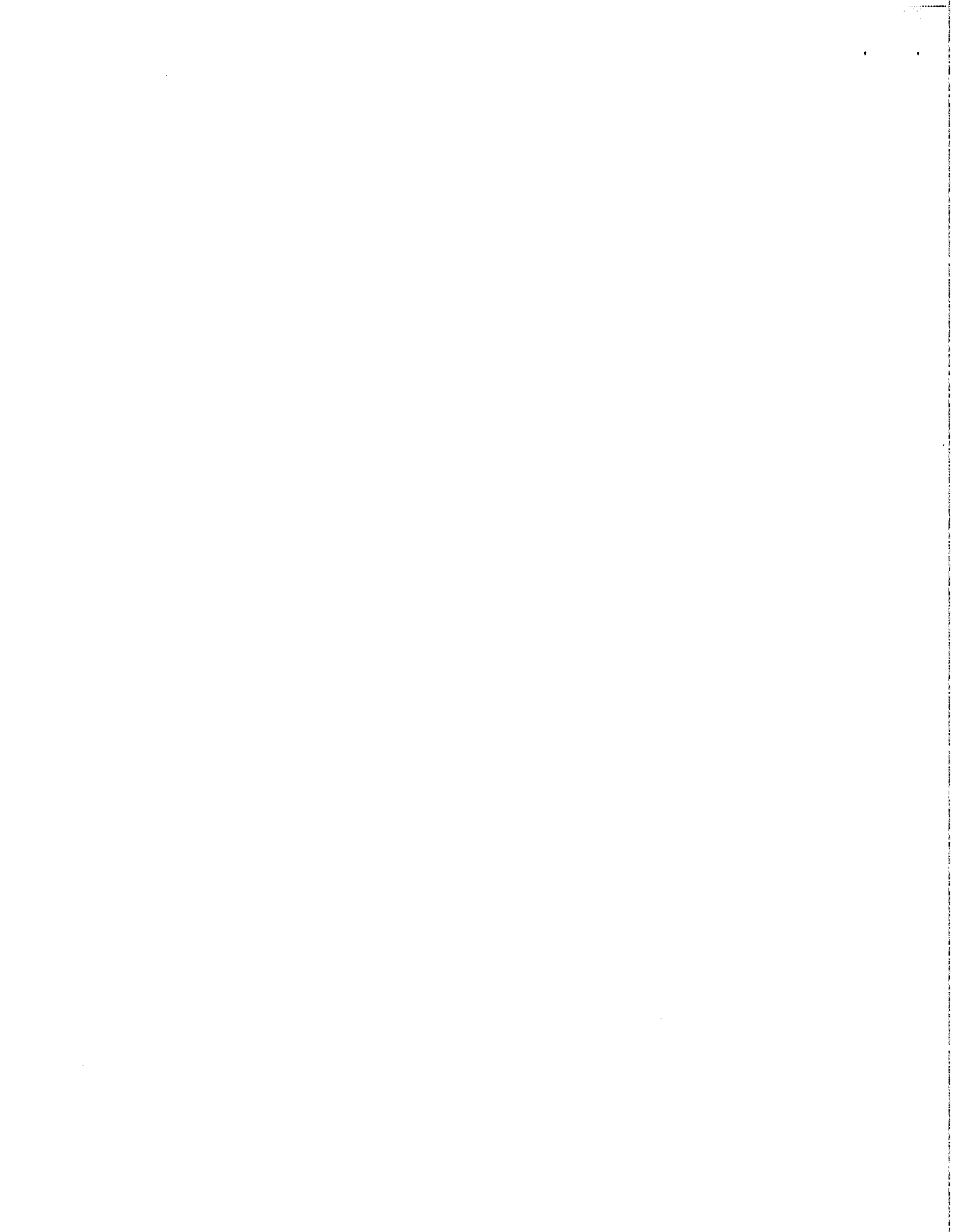
Report to the Chairman, Committee on
Governmental Affairs, U.S. Senate

March 1991

**DEFENSE
INVENTORY**

**DLA and Navy
Suspended Stocks
Should Be Processed
More Quickly**







United States
General Accounting Office
Washington, D.C. 20548

143523

National Security and
International Affairs Division

B-240571

March 14, 1991

The Honorable John Glenn
Chairman, Committee on
Governmental Affairs
United States Senate

Dear Mr. Chairman:

This report responds to your request that we examine defense secondary item inventories to assess efforts to minimize stocks of unknown status. Our work is ongoing to address the remainder of your request, dealing with the extent to which required secondary item stocks may be unessential.

As arranged with your office, unless you release its contents earlier, we plan no further distribution of the report until 30 days from its issue date. At that time, we will send copies to other interested committees and Members of Congress; the Secretaries of Defense and the Navy; and the Director of the Office of Management and Budget. Copies will also be made available to others on request.

This report was prepared under the direction of Donna M. Heivilin, Director, Logistics Issues, who may be reached on (202) 275-8412 if you have any questions. Other major contributors are listed in appendix III.

Sincerely yours,

Frank C. Conahan
Assistant Comptroller General

Executive Summary

Purpose

As of December 1988, the Department of Defense (DOD) had placed over \$900 million of spare parts and other secondary items in a suspended status—i.e., they cannot be issued because their usability was unknown or in dispute. With possible changes in force structure, returned materials from affected units could increase suspended stocks dramatically. The Chairman, Senate Committee on Governmental Affairs, asked GAO to determine whether (1) inventory managers promptly resolved the status of suspended items and (2) the managers used the items or disposed of them.

Background

Suspended stock occurs for various reasons. It is primarily managed by inventory control points and storage activities. Control points maintain accountable records for these items, usually initiate efforts to determine the status of suspended stock items, and decide whether the items should be returned to stock or disposed of. Storage activities receive, store, and issue items and maintain inventory records.

The primary suspended stock categories are stock whose condition is unknown (J), stock whose condition is unknown and was returned by a customer (K), and stock that was received from a supplier in unacceptable condition (L). GAO examined suspended stocks managed by the Defense Logistics Agency (DLA) and the Navy to see if long delays in resolving the status of stocks and associated management weaknesses reported by GAO in 1984 still occur.

Results in Brief

DLA and the Navy have made improvements since GAO's 1984 review, but they still do not resolve the status of suspended stock in a timely manner. Secondary items have frequently remained suspended beyond DOD time standards because resolving the items' status was not a high priority, program guidance did not contain key elements, and existing guidance was routinely not followed. Overall, stocks valued at about \$50 million, or 49 percent of the \$103 million of secondary items GAO sampled, remained suspended more than 6 months.

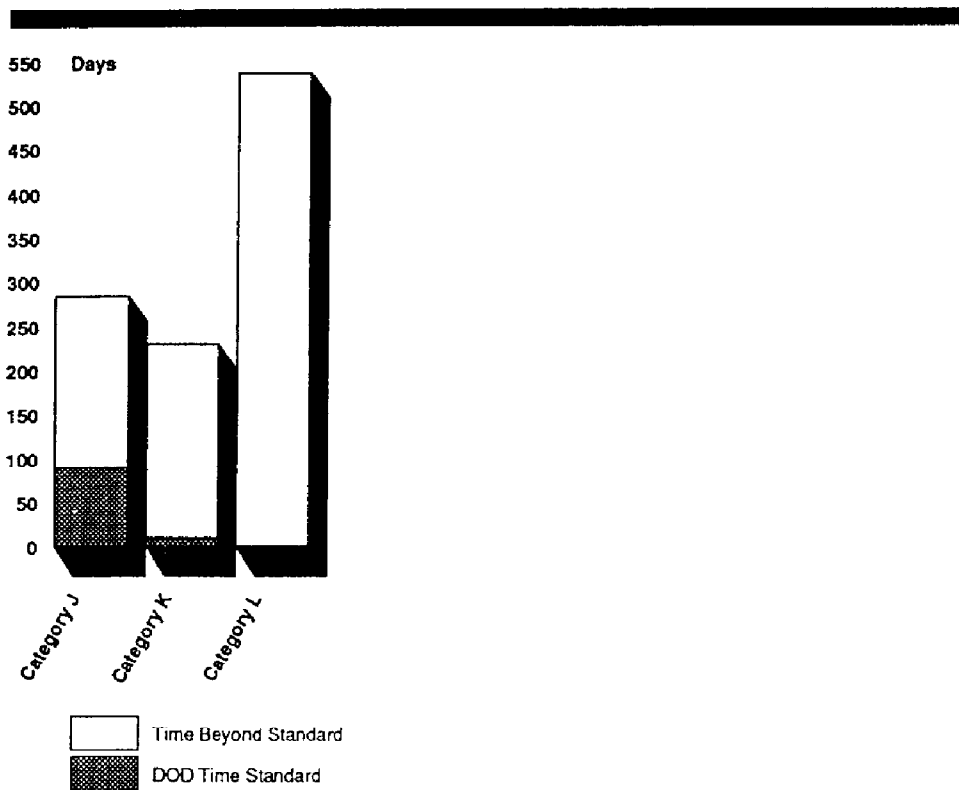
Once items are determined to be usable, item managers consider them in procurement decisions. However, the delays in resolving the status of items in suspended stock may result in unnecessary new procurements. In addition, some suspended items should have been disposed of. Using DOD data, GAO estimates that suspended items cost over \$9 million per year to store.

Principal Findings

Stock Remains in Suspended Status Past DOD Time Standards

DLA and the Navy have improved their suspended stock management since 1984. Most notably, the Navy has reduced the time for processing suspended stocks at selected supply centers from 21 months in 1984 to 14 months in 1989. However, secondary stock has often been in a suspended status in DLA and Navy inventories past DOD time standards. Under these time standards, the status of J and K category stocks is to be resolved in 90 days and 10 days, respectively. Although L stocks have no time limit, their status is to be resolved as soon as possible. The criteria used to set DOD's time standards are based on the reason for suspending the stock and the difficulty of determining an item's usability. The average time that items in GAO's sample were in suspended status was about 458 days. Figure 1 shows how long DLA and the Navy took to resolve the status of suspended stock in the primary categories.

Figure 1: Average Time Items Remained in Suspended Status in Navy and DLA Inventories



Note: Category L has no recommended time standard. The status of items in suspended stock is supposed to be resolved as quickly as possible.

Policies and Guidance Do Not Ensure Timely Resolution

Defense policies for managing suspended stock emphasize timely resolution by setting specific time standards. However, these policies and their implementation guidance do not provide the necessary key elements. They generally do not address organizational responsibilities, specific procedures for resolving the status of suspended stock, or the priority for reducing various categories of suspended stock. Instead, the policies state that each activity is to develop its own guidance on such matters. Some activities had developed adequate guidance, but others had not. For example, the DLA supply center had instructions that were out of date; stock management procedures and information systems have changed so much since the instructions were issued that they no longer apply.

Apart from the time standards, DLA and Navy procedures generally do not address how to follow up stock that has been suspended a long time. Inaccurate records precluded knowing of numerous items that needed follow-up. Several activities did not require periodic follow-up of long-term stock.

Item Managers' Instructions Are Not Always Followed

Item managers issue instructions on additional testing of suspended stock, changing the condition code of stock items to another category, and disposing of unusable items. GAO found that many items have remained in suspended status beyond time standards because DLA personnel did not follow item managers' instructions for resolving the status of suspended stock. GAO reviewed 6,439 items at DLA and estimates that DLA did not follow instructions for resolving the status of about 68 percent of them (4,348 items valued at about \$17.5 million).

For example, in April 1989, the Defense General Supply Center had placed 382 cutter bits in suspended status because it had received them from the contractor in poor condition. The inventory manager directed the Center to return the bits in July 1989; however, the Center had not returned them as of September 1989.

Unresolved Status of Suspended Stock Prevents Its Consideration in Procurements or Timely Disposal

DLA and Navy procedures state that once the status of suspended stock is resolved, the items should be considered in procurement decisions. However, because DLA and the Navy did not promptly resolve the status of suspended stock, item managers did not know if the items could be used and therefore could not consider the items in procurement decisions. For example, at one Marine Corps activity, 12 circuit-card assemblies worth \$3,840 had been in suspended status since December 1987.

After GAO's visit in August 1989, the activity checked the condition of the assemblies and scheduled them for repair. According to the item manager, the assemblies are routinely needed and requisitioned by DOD activities, although GAO could not determine how many new assemblies may have been purchased during the suspension period.

GAO found that some of its sample items met DOD's disposal criteria. For example, 17 (12 percent) of 146 DLA items suspended in categories J and K were subsequently found to be either excess or had been directed to disposal but not sent. Officials did not know why instructions were not carried out.

Recommendations

GAO is making six specific recommendations aimed at ensuring that organizational responsibilities are clearly defined and that adequate control mechanisms are in place to ensure effective implementation of time standards and routine compliance with applicable instructions.

Agency Comments

DOD agreed with GAO's findings and recommendations (see app. II). In its response, DOD described the actions it will take to correct the problems noted in this report. DOD also provided revised cost data, which GAO incorporated in the report.

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Abbreviations

DLA	Defense Logistics Agency
DOD	Department of Defense
GAO	General Accounting Office

Introduction

The Department of Defense (DOD) stores secondary items to support peacetime missions and equip forces for combat. These items consist of equipment, replacements, spare parts, and consumables, but not major items such as ships, tanks, or planes. Items that cannot be issued because their usability is unknown or in dispute are placed in suspended stock inventories. Suspended stocks can arise, for example, if a unit returns a used item to inventory or if an item different than ordered is received from a supplier.

Because suspended items are not available for issue, they do not contribute to military capability. According to Defense Logistics Agency (DLA) and service records, such inventories are valued at over \$900 million. We previously reported¹ problems in managing suspended secondary items. Congressional concern about such inventories and the chance of their increase through force structure changes prompted us to again examine the management of suspended secondary stock by DLA and the Navy, including the Marine Corps.

Roles and Responsibilities for Managing Suspended Stock

DLA and service headquarters, inventory control points, and storage activities are responsible for managing suspended secondary stock. Headquarters issue guidance and provide general oversight. Inventory control points maintain the accountable records and

- determine the condition of an item and decide on its disposition,
- decide whether to procure items in addition to those in suspended status, and
- direct suspended stock found to be unusable to disposal.

Storage activities receive and store suspended items and maintain inventory records for them. Once the suspended status of any items has been resolved, storage activities reclassify items found to be (1) usable and ready for issue and (2) to be unusable and ready for disposal.

Objectives, Scope, and Methodology

The Chairman, Senate Committee on Governmental Affairs, concerned about suspended stock, asked us to determine whether inventory managers (1) promptly resolved questions about suspended stock and (2) then either used the items or disposed of them. During our review, we focused on DLA and the Navy, which we had included in our prior

¹Navy Material in Suspended, Not Ready for Issue, Condition Needs More Management Attention (GAO/NSIAD-85-23, Nov. 19, 1984).

The items should be reclassified as soon as possible, but no specific time standard has been set. As an example, the Marine Corps Logistics Base suspended 10 field showers valued at \$164,800 while it resolved packaging discrepancies with the supplier.

Past Problems in Managing Suspended Stocks Have Not Been Fully Resolved

In 1984, we reported on needed improvements in Navy management of suspended material. We found that neither DLA nor the Navy were meeting the time standard for resolving the status of suspended stocks but that DLA had better management controls. Our tests at the Norfolk and Oakland Naval Supply Centers showed that the average suspension was 21 months. At Norfolk 88 percent of these stocks had been suspended over 3 months, 60 percent over 1 year, and 28 percent over 2 years. We attributed the lengthy suspensions primarily to inadequate management oversight and the lack of specific guidance defining the responsibilities for taking specific actions on this material.

We recommended increasing management oversight and more clearly defining the responsibilities for taking action to resolve the status of this material. Specifically, we recommended the Navy

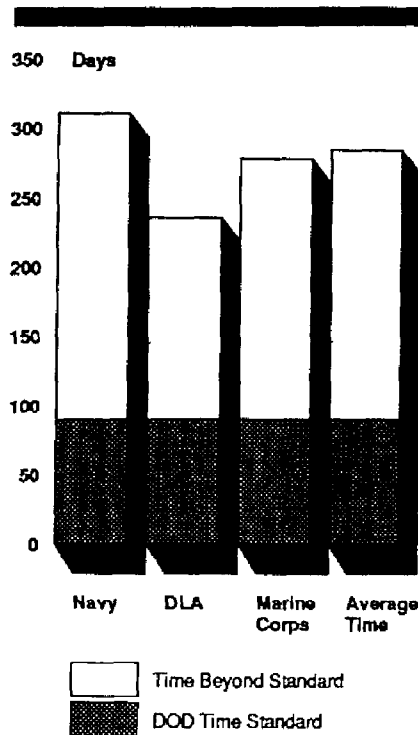
- increase visibility over suspended stocks and establish central control groups or individuals at inventory control points to monitor them to ensure that their status is timely resolved;
- provide more explicit guidance concerning the responsibilities for resolving suspended material so that the material could be issued or disposed of in a timely manner; and
- initiate a one-time special project to purge the supply system of suspended material.

Our current review showed progress in improving management of suspended stock. The Navy partly implemented our recommendations to increase the amount of management oversight over the suspended stock program and modified its information systems to increase its visibility over suspended material. However, overall Navy reports of secondary items do not identify this material. According to the Navy, the one-time project to purge the supply system was completed shortly after we issued our 1984 report. As discussed below, a significant amount of such stock remains and its resolution is not yet timely, despite the efforts. Also, management and guidance problems still exist (see ch. 3).

Time Standards for Resolving Suspended Stocks Are Not Met

The length of time stock remains in suspended status (categories J, K, and L) in DLA and Navy inventories we sampled far exceeds the established time standards. We estimate that for the items valued at \$103 million that we reviewed in these categories, the average suspension time was approximately 458 days. The average times by categories J, K, and L were 284, 229, and 538 days, respectively, as shown in figures 2.1, 2.2, and 2.3.

Figure 2.1: Time Stock in Category J Remained Suspended Beyond Time Standards



Chapter 2
Timeliness to Process Suspended Stocks Has
Improved but Is Still Not Within
DOD Standards

Figure 2.2: Time Stock in Category K Remained Suspended Beyond Time Standards

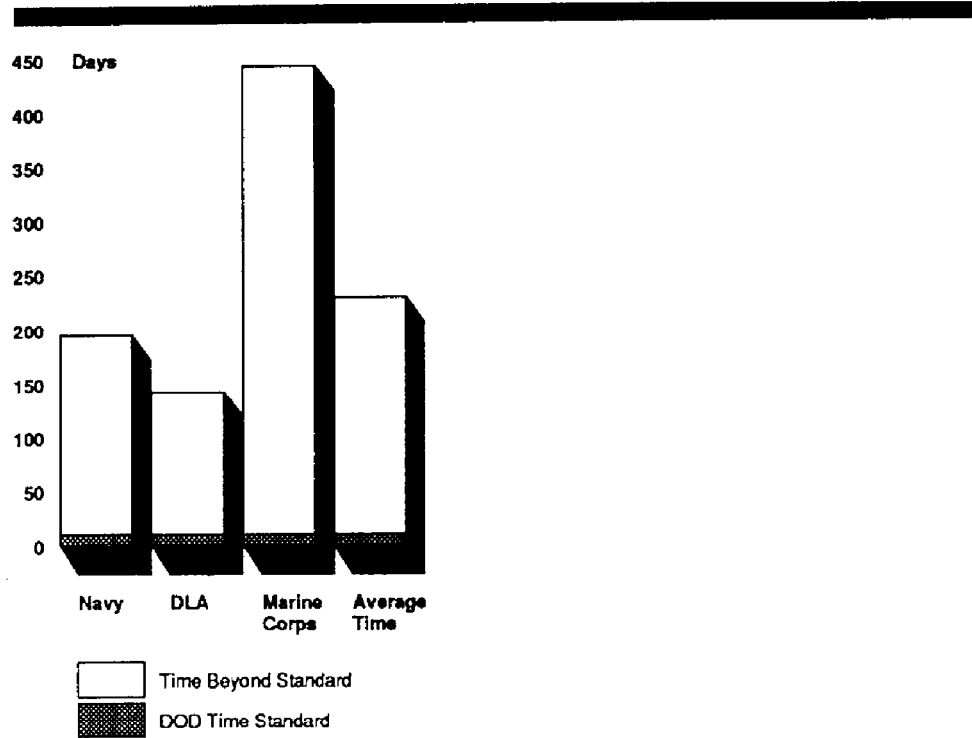
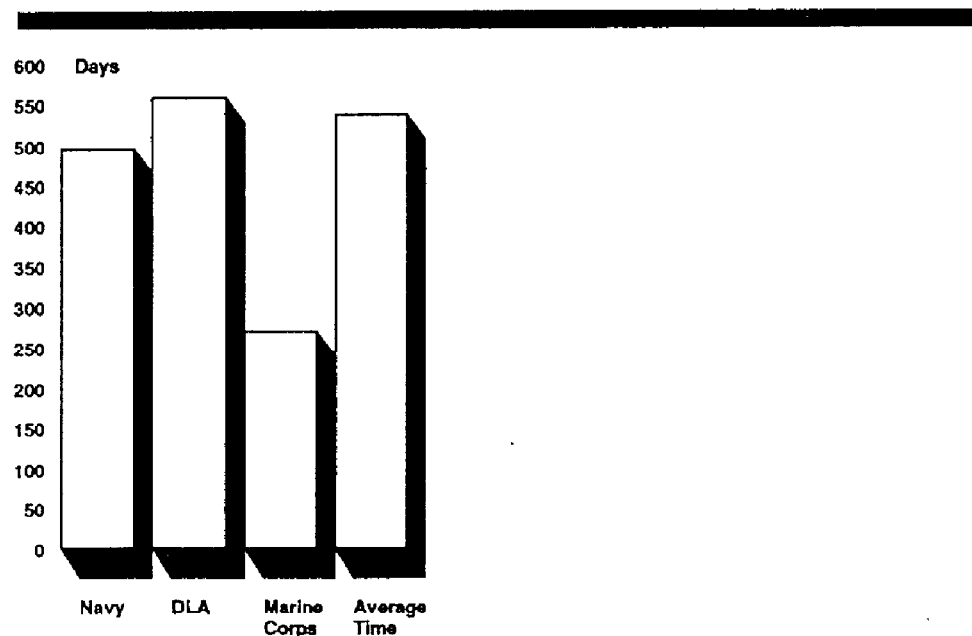


Figure 2.3: Time Stock in Category L Remained Suspended



**Chapter 2
Timeliness to Process Suspended Stocks Has
Improved but Is Still Not Within
DOD Standards**

Table 2.1 shows the value of items that had been suspended for more than 180 days for categories J, K, and L.

**Table 2.1: Value of Stocks Suspended
More Than 180 Days**

(Dollars in thousands)					
Locations	Category J	Category K	Category L	Total sample ^b	Total universe
Defense Depot, Richmond, VA	\$2,639.9	\$213.7	\$1,215.5	\$4,069.1	\$20,601.1
Naval Supply Center, Norfolk, VA	12,735.1	42.7	6,980.1	19,757.9	39,899.0
Marine Corps Logistics Base, Albany, GA ^a	17,744.4	1,254.9	7,508.2	26,507.5	42,500.9
Total^b	\$33,119.5	\$1,511.4	\$15,703.8	\$50,334.5	\$103,000.9

^aDue to the limited sample taken within the Marine Corps, the projections for each category for the Marines should only be used when combined with those of other services or when the three categories are combined

^bTotals may not add due to rounding.

Factors that we believe contributed to the above delays in resolving stock status are discussed in chapter 3.

Management of Suspended Stock Needs Improvement

DLA and Navy inventory policy and procedures do not ensure timely resolution of suspended stock worth millions of dollars. Program guidance did not contain key elements, and existing guidance was not routinely followed. Consequently, DLA and the Navy incur unnecessary holding and procurement costs and increase the risk of lost, stolen, or obsolete items as stock remains unissuable for long periods of time. Potential changes in force structure in Europe and movements of resources to and from the Middle East could increase the levels of suspended stocks and aggravate these problems.

Elements of Effective Suspended Stock Inventory Management

Essential components of effective management of suspended stocks include specific procedures for resolving the status of items and assignment of responsibilities for carrying out these procedures along with related accountability. These components should also include the assignment of the priority to be placed on the reduction of suspended stock and subcategories of such stock and ensure that stock does not remain suspended indefinitely. Management guidance should provide for routinely determining whether suspended stock is usable before making new procurements and for disposing of or returning stock that is not usable.

Existing Policies and Guidance Do Not Include Necessary Elements

Although DOD has provided policies and guidance on suspended material—definitions and time standards for the length of time stock may remain in suspended status—these policies and their implementing instructions are incomplete. They generally do not address organizational responsibilities, specific procedures for resolving suspended stock status, or the priority for reduction of various categories of suspended stock or of suspended stock in general. The same is true of implementing guidance promulgated by DLA and the Navy. In addition, inventory guidance developed by the local activities often does not ensure periodic follow-up on stock that has been suspended for a long time. Of the DLA and Navy activities we visited, two had not developed any local policies for managing suspended stock.

DOD and Implementing Guidance

DOD has provided guidance on suspended secondary stock in the form of condition categories and time limits on suspended status. This guidance is found in two publications: the Military Standard Transaction Reporting and Accounting Procedures, and the Military Standard Requisitioning and Issue Procedures.

The Marine Corps has issued no implementing regulations for managing suspended stock. According to a Marine Corps official, the Marine Corps considers DOD guidance to be sufficient.

In contrast, the Navy and DLA provide implementing policies that give more specific guidance to command and lower operating levels. This guidance addresses general organizational objectives, such as minimizing the quantity, value, and age of suspended material and focusing on items that have been suspended for a long period of time or that have a high unit or total value. Navy instructions direct two inventory control points—the Ships Parts Control Center in Mechanicsburg, Pennsylvania, and the Aviation Supply Office in Philadelphia, Pennsylvania—to ensure that all suspensions are resolved within the prescribed deadlines. DLA has delegated its responsibility in this area to its inventory control points. However, there is nothing specific in DLA's instructions that outlines how this is to be accomplished.

Inventory Control Point and Storage Activity Guidance

Guidance prepared by DOD, DLA, and the Navy does not provide specific instructions on the priority to be placed on actions to resolve suspended stock status, the specific procedures for resolving suspended status, or specific organizational responsibilities. They rely upon lower levels—inventory control points and storage activities—to prepare the explicit instructions essential to effectively manage stock. In some cases, that task is explicit; in others, no explicit requirement exists on these levels to develop more specific guidance.

Generally, the inventory control points we visited lacked specific guidance. The two Navy control points were instructed in June 1989 to provide procedures that achieve rapid resolution of suspended stock. Yet, at the time of our visit, agency officials at each location stated that these procedures had not been developed. A Marine Corps official informed us that standardized guidance for the inventory control points to manage suspended stock had not been issued, though officials at the control point in Albany, Georgia, were drafting such regulations for control point and storage activity managers. The other control point—DLA's Defense General Supply Center at Richmond, Virginia—had issued its principal instruction on managing suspended stock in 1986, but its stock-management procedures and information systems have changed so much since then that the guidance no longer applies.

Guidance prepared by the Navy and Marine Corps storage activities is specific, but the DLA Richmond Depot had not prepared guidelines. The

Navy and Marine Corps guidance for storage activities provide adequate instructions for handling suspended stock and establish periodic follow-ups of stock that has remained suspended for some time. For example, guidance developed by the Marine Corps storage activity requires managers to review the status of suspended items at least monthly. Their regulations also emphasize the importance of reducing suspended stock and direct that this objective be given high priority. However, DLA's Richmond activity, at the time of our visit, had not written any guidelines for managing suspended stock and lacked systematic procedures for follow-ups.

Disposition Instructions Are Not Routinely Followed

We found that the inventory control point instructions—usually for additional testing of suspended items, changing condition categories, and disposing of unusable items—often were not carried out. We estimate that, because disposition instructions were not followed, of 6,439 DLA line items, 4,348 items totaling \$17.5 million had remained suspended more than 180 days, with no action taken or planned to resolve their status.¹

We found that disposition instructions were not followed at Navy, Marine Corps, and DLA sites. In one case, the Norfolk Naval Supply Center was instructed in July 1986 to suspend 302 main bearings worth about \$29,000 because they needed testing. In February 1987, the Fleet Material Support Office directed the storage activity to ship these bearings to the Philadelphia Naval Base for testing. The storage activity sent 33 of these bearings to disposal and took no action on the remainder. Storage activity officials stated they did not know why the disposition instructions were not followed.

In another instance, this time at the Marine Corps activity, 28 wiring harnesses worth about \$118,000 had been suspended in February 1989 under the L category because they had been received from the supplier without an appropriate stock number. In June 1989, the item manager at the control point provided the activity the correct stock number and instructed it to reclassify the stock as issuable. Two months later, however, the items were still suspended in the L category. Activity officials said they did not know why the item manager's instructions had not been followed.

¹Our estimate of 4,348 is plus or minus 470 at the 95-percent level of statistical confidence. Similarly, we are equally certain that the true dollar value for these items is between \$15.6 million and \$35.8 million.

We found two similar cases at DLA's Richmond activity. The first involved 382 cutter bits, valued at \$1,910, that had been suspended in April 1989 because of their poor quality. In July 1989, the item manager had instructed the activity to return 130 of these bits to the contractor. The instructions were never followed, and these bits were still suspended in September 1989. DLA personnel were not sure whether the contractor would still accept these items for credit, since they had not been returned promptly. The second case concerned 88 packages of photographic paper worth about \$900 which had been suspended because the shelf life had expired. When testing proved that these items were still serviceable, the item manager directed that the paper be reclassified as issuable. However, this action was never taken, and at the time of our visit during August 1989 the shelf life had again expired. Activity officials said they did not know why these instructions had not been carried out.

Procedures Do Not Preclude Long-Term Suspended Stocks

In addition to not meeting specific time standards, some DLA and Navy suspended stocks have been unresolved for long periods, especially items in category L. In our opinion, inventory managers were not aware of all items needing follow-up because their records were inaccurate. Also, not all locations required periodic follow-up of long-term stock, so that an item could remain suspended indefinitely, even if properly accounted for.

Accountable Records for Suspended Stock Are Inaccurate

To assess the accuracy of the records being maintained for suspended stocks, we conducted physical counts of the 567 items in our sample. We estimate that the suspended items differed from the \$103-million value shown on the records by \$21 million or about 30 percent of the total suspended inventory line items we examined.² Although the circumstances surrounding these variances differ, they indicate the need for improving the accountability for such stock.

At the Norfolk Naval Supply Center, the projected inventory variance was \$8.1 million. For example, Navy records showed that one inventory location at the Center was supposed to have on hand about \$47,000 worth of stock, yet this location has not been used since it was damaged by fire about 6 years ago.

²Our estimate of the inventory variance at the 95-percent level of statistical confidence is \$21 million plus or minus \$11 million. Similarly, our estimate of the line items in error at this same level of confidence is 30 percent plus or minus 5 percent.

Changes in the perceived threat and accompanying force structure, including possible reductions in the number of active forces, may alter the make-up of defense facilities, the acquisition of major items of equipment, and logistical support. As such changes materialize, it is likely that there will be turn-ins of substantial numbers of secondary items in use by units here and abroad. Given the difficulties in maintaining accurate records to account for this material now, such turn-ins of material and corresponding increases in the levels of suspended stock will aggravate the accountability problems. Similarly, the increases may also make timely resolution more difficult.

Follow-Up Procedures Are Lacking

In a number of cases, stock remained suspended for long periods of time without resolution, even when managers have directed corrective action. Many of these instances could have been rectified if the activities had follow-up procedures to verify that actions have been implemented as envisioned and have been effective. We found, however, that three of the five activities we visited had no procedures for routine follow-up.

At the Norfolk Naval Supply Center, four members of the supply directorate are involved in managing and following up on suspended stock. We found several instances in which this group alerted managers concerning stock that had been suspended for a long time. However, in many of these cases, no actions were taken.

At the Marine Corps activity in Albany, a procedure for periodically following up suspended items had been recently established but, at the time of our visit, was not fully operational. This procedure, which was intended to alert inventory managers when items remained in suspended status, established a control desk to log each suspended item and periodically follow up on them. Fully implemented, this procedure should reduce the amount of suspended stock at this location.

Suspended Stock Not Always Considered in Lieu of Procurement

Suspended stock should be considered in lieu of making new procurements. However, because DLA and the Navy do not resolve suspended items in a timely manner, many such items would not be considered.

In our 1984 and current work, the long times that some of the material had been suspended and the resulting lack of records prevented us from identifying all procurements made for an item since it was suspended. However, in 1984, we determined that at least 25 percent of 189 Norfolk

sample items had procurements initiated during the time the material was suspended.

During our current review, item managers said that they usually do not take the time to consider suspended stock when making procurement decisions, or do so only when items are critically needed. Several of them said that they consider suspended stock only when an item is not available within the regular supply system.

At the Marine Corps storage activity, for example, 12 circuit-card assemblies worth \$3,840 had been suspended since December 1987. According to the item manager, this is an item that is routinely needed and requisitioned by DOD activities, and requisitions for it had been made since these assemblies were originally suspended. Subsequent to our visit, we were informed that the Marine Corps storage activity determined that these assemblies needed repair and scheduled the repair work.

Unusable Items Not Always Disposed of When Status Is Resolved

Some items that met DOD's disposal criteria had not been disposed of. Prompt disposal of such unusable items can reduce suspended stocks and reduce inventory holding costs. In our sample of 146 DLA items in suspended categories J and K, 17 items (12 percent) valued at \$37,726 were either excess or had been directed to disposal but not sent. Information was not readily available concerning whether most of our sample items were candidates for disposal.

Conclusions

The overall timeliness of processing suspended stocks has improved since our last report, but the time used still far exceeds DOD's standards. Key elements such as adequate procedures and clearly delineated responsibilities—problem areas identified in our previous work—have still not been satisfactorily addressed. The overall Navy reports of secondary item inventories do not identify inventory that cannot be issued because its status is unknown. Furthermore, our current evaluation showed that, in many cases where a disposition decision had been made, the applicable instructions were not followed. At one DLA location we visited, disposition instructions were not followed for an estimated two-thirds of the line items remaining suspended more than 180 days.

Thus, improving suspended stock management will require not only better guidelines and procedures, but also controls and incentives to ensure that overall objectives are met. We believe that the large gaps

between DOD time standards and actual performance necessitate setting achievable interim targets, measuring progress, and recognizing the results in each organization's performance evaluation system.

The targets should recognize that some criteria, such as the 10 days allowed to resolve the status of items routinely returned by customers, may not be realistic for unexpected large volumes of returns. If the reductions in the force structure presently envisioned because of the reduced tensions in Eastern Europe occur, the potential exists for significant increases in suspended stocks. Likewise, the deployment of forces to the Middle East involved shipments of stocks and may involve subsequent returns in unknown condition. Given the difficulty in managing the current level and because changes in the force structure could exacerbate the problems, we believe that management attention should be directed toward solving the problems associated with management of suspended stock.

Recommendations

To maximize the usefulness of secondary item inventory, we recommend that the Secretary of Defense direct the Secretary of the Navy and the Director, DLA, to ensure that:

- suspended items receive adequate visibility at all management levels, up to and including the service level;
- supply organizations establish responsibility and accountability for resolving suspended stock status, carrying out the action, and following up to make sure the actions are promptly and correctly taken; and
- supply organizations develop adequate plans, including objectives and milestones, for meeting DOD time standards in resolving the status of suspended stocks.

To assist Navy, DLA, and other DOD components' efforts to manage suspended stocks, we recommend that the Secretary of Defense

- establish the priority to be placed on resolving the status of suspended stock vis-a-vis the handling of other stock, and in doing so, consider the need for the items and cost considerations such as the cost of procuring like or similar items and the cost of storing them;
- consider modifying time standards to allow for resolving the status of large volumes of customer returns if DLA and the Navy believe the current standards are unreasonable; and

- establish organizational and personnel incentives to meet time standards and to consider checking suspended stock when making procurement decisions.

Agency Comments and Our Evaluation

DOD concurred with our findings and recommendations. DOD said that it will issue directions to DLA and the services by March 31, 1991. DOD stated that the directions will address visibility over suspended items and will require supply organizations to establish responsibility and accountability for following up and resolving suspended stock status. DLA and service plans are to include objectives and milestones for meeting time standards. By September 1991, a DLA working group will develop procedures to ensure follow-up on suspended stocks and compliance with inventory managers' disposition instructions.

DOD stated that it will consult with DLA and the services to address our last three recommendations. They will consider the priority structure for suspended items, possible modifications to time standards, incentives to meet standards, and the potential ways to check suspended stock when making procurement decisions.

We believe that DOD's proposed actions are steps in the right direction to address problems in managing suspended stocks.

Locations Visited

Office of the Secretary of Defense

- Assistant Secretary of Defense, Production and Logistics, Washington, D.C.

Defense Logistics Agency (DLA)

- DLA Headquarters, Alexandria, Virginia
- Defense General Supply Center, Richmond, Virginia
- Defense Depot, Richmond, Virginia

Navy

- Naval Supply Systems Command, Washington, D.C.
- Aviation Supply Office, Philadelphia, Pennsylvania
- Ships Parts Control Center, Mechanicsburg, Pennsylvania
- Naval Supply Center, Norfolk, Virginia

Marine Corps

- Marine Corps Headquarters, Washington, D.C.
- Marine Corps Logistics Base, Albany, Georgia

Air Force

- Air Force Logistics Command, Wright-Patterson Air Force Base, Ohio
- Air Logistics Center, San Antonio, Texas

Army

- Headquarters, U.S. Army Materiel Command, Alexandria, Virginia

Comments From the Department of Defense

Note: GAO comments supplementing those in the report text appear at the end of this appendix.



ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, DC 20301-8000

December 10, 1990

(L/SD)

Mr. Frank C. Conahan
Assistant Comptroller General
National Security and International
Affairs Division
U.S. General Accounting Office
Washington, DC 20548

Dear Mr. Conahan:

This is the Department of Defense (DoD) response to the General Accounting Office (GAO) Draft Report, "DEFENSE INVENTORY: DLA and Navy Suspended Stocks Should Be Processed More Quickly," dated October 11, 1990 (GAO Code 398004), OSD Case 8495. The Department concurs with the findings and recommendations.

The DoD plans to issue direction to the Military Services and the Defense Logistics Agency by March 31, 1991, to ensure suspended items receive adequate visibility at all levels, including the Service/Agency level. That will entail requiring supply organizations to establish responsibility and accountability for following up on, and resolving, suspended stock status in a more timely manner.

The detailed DoD comments on the report findings and recommendations are provided in the enclosure. The DoD appreciates the opportunity to comment on the draft report.

Sincerely,

A handwritten signature in cursive script, reading "David J. Berteau".

David J. Berteau
Principal Deputy

Enclosure

Appendix II
Comments From the Department of Defense

GAO DRAFT REPORT - DATED OCTOBER 11, 1990
(GAO CODE 398004) OSD CASE 8495

"DEFENSE INVENTORY: DLA AND NAVY SUSPENDED STOCKS
SHOULD BE PROCESSED MORE QUICKLY"

DEPARTMENT OF DEFENSE COMMENTS

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FINDINGS

o **FINDING A: The DoD Has About \$1 Billion of Parts In Suspended Status.** The GAO observed that secondary items consist of equipment, replacements, spare parts, and consumables, but not major items such as ships, tanks, or planes. The GAO further observed that those items which cannot be issued because their usability is unknown or in dispute, are placed in suspended stock inventories. The GAO explained that, because suspended items are not available for issue, they do not contribute to military capability. The GAO found that, as of December 1988, the Department had placed about \$1 billion of spare parts and other secondary items in a suspended status. The GAO further found that the inventory control points and storage activities for the Defense Logistics Agency and the Service headquarters are responsible for managing suspended secondary stock. The GAO concluded that, with the possible changes in force structure, returned materials from affected units could increase suspended stocks dramatically. (pp. 2-3, pp. 11-12/GAO Draft Report)

DOD RESPONSE: Concur. It should be noted, however, that the DoD cannot validate the \$1 billion figure cited by the GAO as the total value of suspended stock in DoD. The Navy and DLA figures for December 1988 for Condition Codes J, K, and L total \$256.5 million (Navy - \$131.5 million and DLA - \$125 million).

o **FINDING B: Stock Remains In Suspended Status Past DoD Time Standards.** The GAO referenced a prior report ("Navy Material in Suspended, Not Ready for Issue, Condition Needs More Management Attention," OSD Case 6609), which had identified needed improvements in Navy management of suspended material. The GAO noted it had found that the time standard for resolving the status of suspended stocks was not being met by either the Defense Logistics Agency or the Navy--but that the Defense Logistics Agency had better management controls. The GAO reported that its tests at two locations had shown that the average suspension was 21 months. The GAO observed that in

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the prior report, the lengthy suspension was primarily attributed to (1) inadequate management oversight and (2) the lack of specific guidance defining the responsibilities for taking specific actions on suspended material.

During its current review, the GAO found that there has been progress in improving management of suspended stock. The GAO pointed out that the Navy partly implemented the GAO recommendations to increase the amount of management oversight over the suspended stock program and modified information systems to increase visibility over suspended material. The GAO pointed out, however, that overall Navy reports of secondary items do not identify material in suspense. The GAO also found that a significant amount of stock remains, and its resolution is not timely. The GAO concluded, therefore, that management and guidance problems still exist.

The GAO also reported that the length of time stock remains in suspended status in the Defense and Navy inventories (i.e., categories J, K, and L) far exceeds the established time standards. The GAO estimated that, for those suspended items valued at \$103 million in the three categories, the average suspension time was approximately 458 days. The GAO concluded that the overall timeliness of processing suspended stocks has improved since its last report, but the time used still far exceeds DoD standards. The GAO added that key elements, such as adequate procedures and clearly delineated responsibilities--problem areas identified in the previous GAO work--still have not been satisfactorily addressed. (pp. 3-4, pp. 14-19, p. 28/GAO Draft Report)

DOD RESPONSE: Concur. Both the Navy and the Defense Logistics Agency have initiated action to reduce suspended stock levels. In August 1990, the Defense Logistics Agency established an Inventory Readiness Working Group to address the entire suspended stock area; the Inventory Readiness Working Group will prepare more comprehensive and clearly defined procedures and time standards for returning material to issuable condition to supplement the guidance contained in Defense Logistics Agency Manual 4140.2, Volumes II and III. The Navy has made inroads in the resolution of suspended material through established programs to monitor and return material to a non-suspended status. The referenced previous GAO report calculated that the Navy averaged 21 months to clear stock from suspended status, while the current report calculates the average time at the the Defense Logistics Agency and Navy to be 15 months (458 days). During the fourth quarter of FY 1990, the Navy Aviation Supply

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Office moved \$140 million worth of material from suspended to other conditions. It must be emphasized, however, that resolving suspended stock involves more and more extended procedures, including inspection, testing, and contract negotiations. Decreasing resources make it more difficult to perform the technical effort necessary to bring the material to a usable condition. (See the DoD response to Finding E.)

o FINDING C: Policies And Guidance Do Not Ensure Timely Resolution.

The GAO observed that, although the DoD has provided policies and guidance on suspended material--definitions and time standards for the length of time stock may remain in suspended status--those policies and their implementing instructions are incomplete. The GAO reiterated that the DoD policies and the implementing guidance do not provide the necessary key elements. The GAO noted, for example, that the policies and guidance generally do not address (1) organizational responsibilities, (2) specific procedures for resolving the status of suspended stock, or (3) the priority for reducing various categories of suspended stock. The GAO observed that each activity develops its own guidance on such matters. The GAO further observed that the same is true of implementing guidance promulgated by the Defense Logistics Agency and the Navy. The GAO further pointed out that the Marine Corps has issued no implementing regulations for managing suspended stock.

The GAO reported that, apart from the time standards, Defense Logistics Agency and the Navy procedures generally do not address how to follow-up on stock that has been suspended a long time. The GAO also found that inaccurate records precluded the identification of numerous items that needed follow-up--with several activities not requiring periodic follow-up of long term stock. (pp. 5-6, pp. 20-23/GAO Draft Report)

DOD RESPONSE: Concur. Within the Defense Logistics Agency, reorganizations at several inventory control points, as well as modifications to the automated information systems supporting the inventory managers, have outpaced changes to local implementing procedures. The newly established Defense Logistics Agency Inventory Readiness Working Group will develop standard procedures not later than September 1991, and the inventory control points will update local procedures to reflect these changes. The Defense Logistics Agency has guidance that requires the inventory control points, as their first priority, to resolve suspended stock conditions when backorders exist. Although procedures for suspending material and

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follow-up responsibilities to determine disposition do need more definition, the principal responsibility for establishing detailed operational procedures within the Defense Logistics Agency, the Navy and the Marine Corps should remain at the local level. The long-term solution to many of the problems encountered in processing suspended stocks will be inherent in the automation in the mid-1990s of much of the process, as part of the Modernization of the Defense Logistics Standard Systems process.

o **FINDING D: Disposition Instructions Are Not Routinely Followed.**

The GAO reported that item managers issue instructions on (1) additional testing of suspended stock, (2) changing the condition code of stock items to another category, and (3) disposing of unusable items. The GAO found, however, that many items have remained in suspended status beyond time standards, because Defense Logistics Agency personnel did not follow item manager instructions for resolving the status of suspended stock. The GAO estimated that, because disposition instructions were not followed, of the 6,439 Defense Logistics Agency line items, 4,348 items (totaling \$17.5 million) had remained suspended more than 180 days, with no actions taken or planned to resolve their status. The GAO asserted that inventory control point instructions were not followed at Navy, Marine Corps, and Defense Logistics Agency sites. The GAO concluded that improving suspended stock management will require not only better guidelines and procedures, but also controls and incentives to ensure that overall objectives are met. The GAO further concluded that the large gaps between DoD time standards and actual performance necessitate the following actions:

- setting achievable interim targets, measuring progress; and
- recognizing the results in each organization's performance evaluation system. (pp. 6-7, pp. 23-24, p. 28/GAO Draft Report)

DOD RESPONSE: Concur. Within the Navy, better documenting procedures and charging single organizations within activities with receiving and carrying out disposition actions will improve this problem. The Defense Logistics Agency will reiterate guidance and increase monitoring of compliance through depot operational site reviews which are accomplished annually, if funds are available. The GAO-recommended actions will be addressed by the Defense Logistics Agency Inventory Readiness Working Group within the next six months.

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o **FINDING E: Procedures Do Not Preclude Long-Term Suspended Stocks.**

The GAO reported that, in addition to not meeting specific time standards, some Defense Logistics Agency and Navy suspended stocks have been unresolved for long periods, especially items in category L (i.e., stock received from the supplier in unacceptable quantity or quality). The GAO found that, because their records were inaccurate, inventory managers were not aware of all items needing follow-up. The GAO also found that not all locations required periodic follow-up of long-term stock--so that an item could remain suspended indefinitely, even if properly accounted for. (p. 24/GAO Draft Report)

DOD RESPONSE: Concur. Due to the increasing complexity of resolving suspensions, and the decreasing resources, upgrading procedures alone will not prevent long-term suspensions. Although the time limits for clearing some suspended conditions may need review, the length of time to resolve suspended items in litigation will not be impacted. The period of suspension of category "L" stocks is a function of the complexity of the deficiency and, in cases of fraud (a significant percentage of the sample of the "L" suspensions), the processing actions taken by the U.S. attorneys.

o **FINDING F: Accountable Records For Suspended Stock Are Inaccurate.** In order to assess the accuracy of the records being maintained for suspended stock, the GAO conducted physical counts of 567 items in a sample. The GAO estimated that the suspended items differed from the \$103 million value shown on the records by \$20 million, or about 30 percent of the total suspended inventory line items examined. The GAO concluded that, although the circumstances surrounding the variances differed, it indicated the need for improving the accountability of such stock.

The GAO further concluded that changes in the perceived threat and accompanying force structure, including possible reductions in the number of active forces, may alter (1) the makeup of Defense facilities, (2) the acquisition of major items of equipment, and (3) logistical support. The GAO speculated that, as such changes materialize, it is likely that there will be turn-ins of substantial numbers of secondary items in use by units here and abroad. The GAO concluded that, given the difficulties in maintaining accurate records to account for this material now, such turn-ins of material and corresponding increases in the levels of suspended stock will aggravate the accountability problems. In addition, the GAO

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items require extensive testing to determine true condition, and procurement may not always be avoided.

Before December 31, 1990, the Office of the Assistant Secretary of Defense (Production and Logistics), in consultation with the Services and the Defense Logistics Agency, will examine the potential for encouraging more direct examination of potential suspended stock availability. (See the DoD response to Finding G.)

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RECOMMENDATIONS

o **RECOMMENDATION 1:** The GAO recommended that the Secretary of Defense direct the Secretary of the Navy and the Director, Defense Logistics Agency, to ensure that suspended items receive adequate visibility at all management levels, up to and including the Service-level. (p. 29/GAO Draft Report)

DOD RESPONSE: Concur. The Office of the Assistant Secretary of Defense (Production & Logistics) will issue appropriate direction to the Military Services and the Defense Logistics Agency, not later than December 31, 1990, to ensure necessary visibility of suspended items.

o **RECOMMENDATION 2:** The GAO recommended that the Secretary of Defense direct the Secretary of the Navy and the Director, Defense Logistics Agency, to ensure supply organizations establish responsibility and accountability for (1) resolving suspended stock status, (2) carrying out the action, and (3) following up to make sure the actions are promptly and correctly taken. (p. 29/GAO Draft Report)

DOD RESPONSE: Concur. The Office of the Assistant Secretary of Defense (Production & Logistics) will direct the Military Services and the Defense Logistics Agency to ensure supply organizations establish responsibility and accountability for (1) resolving suspended stock status, (2) carrying out the action, and (3) following up to make sure the actions are properly and correctly taken. Direction will be provided not later than March 31, 1991.

o **RECOMMENDATION 3:** The GAO recommended that the Secretary of Defense direct the Secretary of the Navy and the Director, Defense

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Logistics Agency, to ensure that supply organizations develop adequate plans, including objectives and milestones, for meeting DoD time standards in resolving the status of suspended stocks. (p. 29/GAO Draft Report)

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DOD RESPONSE: Concur. The Office of the Assistant Secretary of Defense (Production & Logistics) will direct the Military Services and the Defense Logistics Agency to ensure that supply organizations develop adequate plans, with appropriate objectives and milestones, for meeting the Department of Defense time standards. Direction will be provided not later than December 31, 1990.

o **RECOMMENDATION 4:** The GAO recommended that the Secretary of Defense establish the priority to be placed on resolving the status of suspended stock vis-a-vis the handling of other stock and, in so doing, consider the need for the items and cost considerations, such as the cost of procuring like or similar items and the cost of storing them. (p. 29/GAO Draft Report)

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DOD RESPONSE: Concur. The issue of establishing DoD priorities for suspended stock resolution becomes very complex given the multiple conditions inherent in the total suspension universe. For example, no priority can reasonably be established in cases of fraud litigation (Condition Code "L"), since control of the process is outside of the Department. The Office of the Assistant Secretary of Defense (Production & Logistics) will consult with the Services and the Defense Logistics Agency, by March 31, 1991, to determine if a DoD priority structure is seen as a potential aid in correcting problems in the operational execution of the resolution process. Appropriate action will follow this consultation within 90 days.

o **RECOMMENDATION 5:** The GAO recommended that the Secretary of Defense consider modifying time standards to allow for resolving the status of large volumes of customer returns, if the Defense Logistics Agency and the Navy consider the current standards to be unreasonable. (p. 29/GAO Draft Report)

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DOD RESPONSE: Concur. The Office of the Assistant Secretary of Defense (Production & Logistics) will consult with the Military Services and the Defense Logistics Agency to consider modifying time standards to improve management of suspended stock. Action will be taken not later than March 31, 1991.

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o RECOMMENDATION 6: The GAO recommended that the Secretary of Defense establish organizational and personnel incentives to meet time standards and to consider checking suspended stock when making procurement decisions. (p. 29/GAO Draft Report)

DOD RESPONSE: Concur. The Office of the Assistant Secretary of Defense (Production & Logistics), in consultation with the Military Services and the Defense Logistics Agency, will examine the potential for encouraging more direct examination of potential suspended stock availability before initiating procurements. Action will be taken before December 31, 1990.

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The following are GAO's comments on DOD's letter dated December 10, 1990.

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1. We revised our draft report's suspended stock total from \$1 billion to over \$900 million based on DOD's revised suspended stock figure of \$131.5 million for the Navy as of December 1988. However, we believe that the Navy and overall suspended stock totals are probably higher because of DOD's comments that suspended aviation stocks alone have been subsequently reduced by \$140 million. In a separate response, the Navy indicated that overall suspended stocks still exceeded \$150 million as of October 1990.

Major Contributors to This Report

National Security and
International Affairs
Division,
Washington, D.C.

Uldis Adamsons, Assistant Director
Carolyn S. Blocker, Reports Analyst

Program Evaluation
and Methodology
Division,
Washington, D.C.

Harry M. Conley, Statistician

Norfolk Regional
Office

Harry E. Taylor, Evaluator-in-Charge
David A. Schmitt, Site Senior
Cora M. Bowman, Site Senior
Jeanett H. Reid, Evaluator
Lisa J. Kreisel, Evaluator
Melissa Van Tine, Writer-Editor



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