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INVENTORY VALUATION AT THE
DEFENSE SUPPLY CENTER COLUMBUS

Report No. D-2001-078

March 14, 2001

Office of the Inspector General
Department of Defense

Form SF298 Citation Data

Report Date <i>("DD MON YYYY")</i> 14Mar01	Report Type N/A	Dates Covered (from... to) <i>("DD MON YYYY")</i>
Title and Subtitle Inventory Valuation at the Defense Supply Center Columbus		Contract or Grant Number
Authors		Program Element Number
Performing Organization Name(s) and Address(es) OAIG-AUD (ATTN: AFTS Audit Suggestions) Inspector General, Department of Defense 400 Army Navy Drive (Room 801) Arlington, VA 22202-2884		Project Number
Sponsoring/Monitoring Agency Name(s) and Address(es)		Task Number
Distribution/Availability Statement Approved for public release, distribution unlimited		Work Unit Number
Supplementary Notes		Performing Organization Number(s) D-2001-078
Abstract The Defense Supply Center Columbus, Ohio, is the lead DLA inventory control point for Maritime and Land-Based weapon systems and manages more than 2 million different construction and electronic spare parts owned by DLA. At the end of FY 2000, the Defense Supply Center Columbus reported total-on-hand inventories of about \$3.1 billion, which represented about 37 percent of the \$8.3 billion of total DLA on-hand inventories maintained in the DLA Standard Automated Materiel Management System.		Monitoring Agency Acronym
Subject Terms		Monitoring Agency Report Number(s)
Document Classification unclassified		Classification of SF298 unclassified
Classification of Abstract unclassified		Limitation of Abstract unlimited
Number of Pages 42		

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Acronyms

ACC	Acquisition Cost Code
DLA	Defense Logistics Agency
DSCC	Defense Supply Center Columbus
NSN	National Stock Number
NIRF	National Inventory Record File
SAMMS	Standard Automated Materiel Management System
SPMF	Standard Pricing Master File



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

March 14, 2001


MEMORANDUM FOR DIRECTOR, DEFENSE LOGISTICS AGENCY

**SUBJECT: Audit Report on Inventory Valuation at the Defense Supply Center
Columbus (Report No. D-2001-078)**

We are providing this audit report for review and comment. We performed the audit in support of the requirements of the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994. We considered management comments on a draft of this report in preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The comments received from the Defense Logistics Agency were generally responsive to the recommendations. However, comments were only partially responsive to Recommendations 1.a. and 1.d. and comments to Recommendation 4 were not responsive. Therefore, we request that the Director provide additional comments to Recommendations 1.a., 1.d. and 4 by May 14, 2001.

We appreciate the courtesies extended to the audit staff. For additional information on this report, please contact Mr. James L. Kornides at (614) 751-1400, extension 11 (jkornides@dodig.osd.mil) or Ms. Amy J. Frontz at (614) 751-1400, extension 13 (afrontz@dodig.osd.mil). See Appendix C for the report distribution. See the inside back cover for a list of audit team members.


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Office of the Inspector General, DoD

Report No. D-2001-078

(Project No. D2000FJ-0067.002)

March 14, 2001

Inventory Valuation at the Defense Supply Center Columbus

Executive Summary

Introduction. The Defense Supply Center Columbus, Ohio, is the lead DLA inventory control point for Maritime and Land-Based weapon systems and manages more than 2 million different construction and electronic spare parts owned by DLA. At the end of FY 2000, the Defense Supply Center Columbus reported total on-hand inventories of about \$3.1 billion, which represented about 37 percent of the \$8.3 billion of total DLA on-hand inventories maintained in the DLA Standard Automated Materiel Management System.

Objective. The objective of the audit was to evaluate management assertions for valuation, completeness, and existence of DoD inventory accounts and to determine whether the financial statements presented the accounts fairly. This part of the audit focused on the valuation assertion. The objective was to determine whether the values assigned to inventories that the Defense Supply Center Columbus managed were accurately computed in accordance with generally accepted accounting principles and were supported by contract data. We also evaluated applicable management controls. See Appendix A for a discussion of the scope and methodology, the management control program, and prior audit coverage.

Results. The Defense Supply Center Columbus assertion that inventory valuation was accurate and supported by contract data was not reliable. Of the 1,740 items selected for review with on-hand inventories valued at \$64 million, the values assigned to 1,195 items (68.7 percent) with on-hand inventories valued at \$52 million were not accurately computed based on the latest representative obligations or were unsupported. Specifically, 307 items valued at \$8 million had acquisition costs that were inaccurate; 218 items valued at \$14 million had acquisition costs that were not supported by obligation history records; and 670 items valued at \$30 million had acquisition costs that were based on obligation history records that could not be verified to originating contract files.

Additional inaccurate and unsupported acquisition costs are probable in material amounts in the universe of items managed by the Defense Supply Center Columbus. There were 445,089 items with on-hand inventories valued at \$853 million that the Defense Supply Center Columbus managed at the end of FY 2000 with acquisition costs that were coded as being developed using the same methods identified as inadequate by this audit. Until the deficiencies leading to the inaccurate and unsupported acquisition costs are corrected and fully disclosed, inventory valuation data from the Defense Supply Center Columbus for \$3.1 billion of inventory cannot be relied upon to support the inventory amounts reported on the DLA financial statements. See the Finding section for a discussion of the audit results.

During the audit, the Defense Supply Center Columbus corrected the specific acquisition costs that were inaccurate. Those actions corrected a \$2.5 million financial inventory value misstatement. Further, the actions reduced the standard (sales) prices for the affected items and resulted in \$2 million of funds put to better use for DLA customers for on-hand inventories expected to be sold over the 6-Year Future Years Defense Program. While our review showed that 68.7 percent of the items reviewed at the Defense Supply Center Columbus were not accurately computed or were not supported, similar rates of discrepancy were found in items reviewed at the Defense Supply Centers in Richmond and Philadelphia. The results of all three Centers will be reported in a summary report.

Summary of Recommendations. We recommend that the Commander, Defense Supply Center Columbus, develop and implement procedures to accurately compute acquisition costs based on the latest representative purchase prices, identify and correct all acquisition costs in the national inventory record file that were inaccurately computed, establish a quality assurance program for inventory prices, identify and disclose the amount of on-hand inventories that were valued based on acquisition costs that contract data do not support, estimate acquisition costs for items without a procurement history based upon current manufacturer's price listings or market price quotations, and develop and implement procedures to retain contract data to support the value of on-hand inventories on the financial statements in accordance with DLA contract retention requirements.

Management Comments. The Director, DLA Logistics Operations, concurred or partially concurred with all recommendations. He agreed to ensure the inventory valuation methodology is fully documented, review updates to the national inventory record file, and eliminate acquisition costs based on canceled contracts. He also agreed to develop a sampling plan to test the accuracy of prices and to evaluate the cost and benefits of disclosure of the values of on-hand inventory where contract data do not support acquisition costs. Although the Director partially concurred with the recommendation on developing retention procedures for supporting data, he stated that contracts were retained in accordance with Federal Acquisition Regulation guidelines and that the recommendation should be readdressed to the Under Secretary of Defense (Comptroller). See the Finding section of the report for a discussion of management comments and the Management Comments section of the report for the complete text of the comments.

Audit Response. The Director's comments were partially responsive to the recommendations. He did not fully address problems with documenting estimated acquisition costs and identifying and correcting erroneously estimated acquisition costs or those inaccurately computed during a FY1992 valuation method conversion. The Director's comments did not address the retention of obligation history records in the Standard Automated Material Management System Pricing System. DLA needs to issue policy to ensure that its Inventory Control Points comply with Federal Acquisition Regulation requirements and require that these procedures are incorporated in to any automated contract folder initiatives. Those actions are the responsibility of DLA, not the Under Secretary of Defense (Comptroller). We request that the Director provide additional comments on the final report by May 14, 2001.

Table of Contents

Executive Summary	i
Introduction	
Background	1
Objectives	2
Finding	
Valuation of Inventories	3
Appendixes	
A. Audit Process	
Scope	22
Methodology	23
Management Control Program Review	25
Prior Coverage	26
B. Acquisition Cost Calculation	27
C. Report Distribution	28
Management Comments	
Defense Logistics Agency	31

Background

Inventory and inventory-related transactions represent major portions of the total assets, obligations, revenue, and expenses reported on the DLA financial statements. Underlying the financial statements are management assertions on the valuation, ownership, existence, completeness, and presentation of inventories. Assertions regarding inventory valuation deal with whether inventories have been included in the financial statements at the appropriate dollar amounts and whether the basis of valuation is appropriate, properly applied, and consistent with previous periods.

This report is the third in a series of reports on the amounts of inventories reported on the DLA financial statements. The first report discussed issues regarding the condition and accountability of DoD chemical protective suits. The second report focused on the statistical sampling plan that DLA developed to measure the dollar value accuracy of its inventories reported on the financial statements of the DLA Working Capital Fund. The second report pointed out that the DLA sampling plan did not include procedures to validate the inventory valuation data in the logistics feeder systems.

DLA provides centralized management of consumable spare parts, food, clothing and textiles, and medical supplies through its inventory control points, which are located at its Defense supply centers in Columbus, Ohio; Philadelphia, Pennsylvania; and Richmond, Virginia. The inventory control points are responsible for maintaining accurate and reliable inventory values.

This report focuses on our efforts to validate the inventory valuation data in the Standard Automated Materiel Management System (SAMMS), which is the primary inventory logistics feeder system used to maintain inventory valuation data at the Defense Supply Center Columbus (DSCC), Ohio. DSCC is the lead DLA inventory control point for Maritime and Land-Based weapon systems and manages more than 2 million different construction and electronic spare parts. At the end of FY 2000, DSCC reported total on-hand inventories of about \$3.1 billion, which represented about 37 percent of the \$8.3 billion of total DLA on-hand inventories maintained in SAMMS.

Generally Accepted Accounting Principles on Inventory Valuation. The American Institute of Certified Public Accountants designated the Federal Accounting Standards Advisory Board as the accounting standards setting body for Federal government entities. The Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standards No. 3, "Accounting for Inventory and Related Property," October 27, 1993, provides the inventory valuation policy for Federal Government agencies. The policy requires that inventories be valued on the financial statements at historic cost or latest acquisition cost adjusted to estimate historic cost. The cost of an item should include all appropriate purchase, transportation, and production costs incurred to bring an item to its current condition and location. Any abnormal costs such as excessive handling or rework costs are to be charged to operations of the period. Additionally, the latest acquisition cost method requires that the last representative purchase price be applied to all like items, including those items

acquired through donation or non-monetary exchange. The latest acquisition cost must be adjusted to approximate historic cost. The approximation is accomplished by establishing allowance accounts to capture unrealized gains and losses from price changes occurring throughout the year and using the allowance accounts to revalue ending inventories and cost of goods sold at least annually.

DoD Inventory Valuation Policy. The DoD policy for inventory valuation is established in DoD Regulation 7000.14-R, the “DoD Financial Management Regulation,” volume 11B, “Reimbursable Operations, Policy, and Procedures for the Defense Business Operations Fund,” December 1994. DoD policy requires inventories to be reported on the financial statements at their latest acquisition cost in accordance with generally accepted accounting principles. DoD Policy also states that for items without a procurement history, an acquisition cost can be estimated based upon current manufacturer’s price listings or market price quotations.

Logistics Reassignment of Inventories. The logistics reassignment process involved the transfer of material management responsibility from a losing DoD inventory manager to a gaining DoD inventory manager. In 1990, the Deputy Secretary of Defense approved the transfer of the management of about 1 million consumable items from the Military Departments to DLA. Additionally, as part of the 1995 Defense base realignment and closure decision, DLA realigned more than 600,000 items between its inventory control points. The logistics reassignments occurred between FY 1991 and FY 2000. DLA Manual 4140.2, volume II, part 1, “Defense Logistics Agency Supply Operations Manual,” July 1, 1999, provides the policy for pricing items acquired during the logistics reassignment process. Specifically, the policy requires the gaining inventory control point to use contract history data that the losing inventory control point provided during the logistics reassignment process to price all transferred inventory until additional procurement action takes place at the gaining inventory control point.

Objectives

The objective of the audit was to evaluate management assertions for valuation, completeness, and existence of DoD inventory accounts and to determine whether the financial statements presented the accounts fairly. Our prior audit reports focused on the existence and completeness assertions. This part of the audit focused on the valuation assertion. The objective was to determine whether the values assigned to inventories that DSCC managed were accurately computed in accordance with generally accepted accounting principles and were supported by contract data. We also evaluated applicable management controls. See Appendix A for a discussion of the scope and methodology, the management control program, and prior audit coverage.

Valuation of Inventories

The DSCC assertion that inventory valuation was accurate and supported by contract data was not reliable. Of the 1,740 items selected for review with on-hand inventories valued at \$64 million, the values assigned to 1,195 items (68.7 percent) with on-hand inventories valued at \$52 million were not accurately computed based on the latest representative obligations or fully supported by the originating contract files. Specifically,

- 307 items valued at \$8 million had acquisition costs that were inaccurate.
- 218 items valued at \$14 million had acquisition costs that were not supported by obligation history records.
- 670 items valued at \$30 million had acquisition costs that were based on obligation history records that could not be verified to originating contract files.

Additional inaccurate and unsupported acquisition costs are probable in material amounts in the universe of DSCC-managed items. Our analysis of the \$3.1 billion of FY 2000 DSCC inventories showed that 445,089 of the items valued at \$853 million had acquisition costs that were coded as being developed in the same manner as those found to be inaccurate and unsupported by our limited review. These conditions occurred because procedures were not in place to compute acquisition costs based on latest purchase cost information, disclose unsupported cost data that were used, and retain supporting contract data. Additionally, DSCC had not established a quality assurance program for inventory prices. Until the deficiencies leading to the inaccurate and unsupported acquisition costs are corrected and fully disclosed, DSCC inventory valuation data cannot be relied upon to support the inventory amounts reported on the DLA financial statements.

Inventory Items Reviewed

For the statistical sampling plan that DLA developed to measure the dollar value accuracy of its inventory amounts reported on the financial statements of the DLA Working Capital Fund, we analyzed the acquisition costs for 1,740 national stock numbers (NSNs) that DSCC managed. The 1,740 items consisted of 1,336 items that were included in a total of 3,153 items that DLA randomly selected from the on-hand inventory records maintained in the Distribution Standard System at 11 DLA distribution depots. Because the DLA sampling plan did not include procedures to validate the inventory pricing data for the sample items, we performed pricing reviews at the managing DLA inventory control points. The 1,740 items reviewed also included a judgmental sample of 404 items that were

selected to provide additional coverage of unusually low and high-value acquisition costs. See Appendix A for details on the sample item selection.

We determined whether the acquisition costs used to value the 1,740 items in DSCC financial reports were accurately computed and supported by obligation history records. We then determined whether the obligation history records could be verified to the originating contract files. We performed the review to verify whether the acquisition costs were based on the latest acquisition cost inventory valuation method as required by generally accepted accounting principles.

DSCC Inventory Valuation Processes

DLA Inventory Valuation Policy. The DLA policy for pricing inventory is established in DLA Manual 7000.2, volume II, part 1, “Standard Automated Materiel Management System Financial Subsystem Operating Procedures,” July 1, 1999. DLA policy requires the price for each NSN to be based on the latest procurement cost. According to DLA policy, the Pricing Activity at each inventory control point is the only organization authorized to initiate a revision to an established price. The policy states that each item may be scheduled for review as required to ensure that the price is based upon the latest procurement cost and provides instructions on performing the scheduled reviews.

DSCC Inventory Pricing. DSCC uses SAMMS to manage its inventories. SAMMS consists of five operational subsystems: technical, requirements, distribution, procurement, and financial. Inventory prices are calculated within the SAMMS financial subsystem by the Standard Pricing Application (Pricing System). The Pricing System computes an acquisition cost for each item based on obligation history records stored in the standard pricing master file (SPMF) and provides the acquisition cost to inventory files in the other four subsystems. The acquisition cost is used to value on-hand inventories on the financial statements and is updated monthly after any procurement action. Additionally, the Pricing System calculates a standard price for each item that consists of the item’s acquisition cost plus a cost recovery factor or surcharge. The standard price is the sales price charged to customers and is updated annually at the beginning of each fiscal year. See Appendix B for a detailed description of the acquisition cost calculation process.

The DSCC Pricing Activity operated under the Office of the DSCC Comptroller and consisted of two pricing analysts responsible for ensuring the accuracy of the prices for more than 2 million different construction and electronics items. DSCC had no procedures concerning the establishment and maintenance of acquisition costs. The DSCC Pricing Activity relied on the procedures established in DLA Manual 7000.2 as well as a functional description of the SAMMS Pricing System written by a computer specialist at the DLA Systems Integration Office, which was the DLA organization responsible for maintaining SAMMS.

DSCC Financial Inventory Reporting. Within the SAMMS distribution subsystem, the national inventory record file (NIRF) contains the total on-hand

asset balance for each national stock number (NSN) that DSCC managed. In addition, the NIRF contains each item's acquisition cost that should be derived from the SAMMS Pricing System. At the end of each reporting period, the total DSCC-owned assets are multiplied by the acquisition cost to arrive at the extended inventory value for each item. The extended inventory value for all DSCC-managed items are combined to arrive at the total NIRF inventory value. The NIRF is the source file for the inventory amounts reported on the DSCC Defense Stock Fund Trial Balance. The Defense Finance and Accounting Service relies on the DSCC Defense Stock Fund Trial Balance to prepare the DLA financial statements. DSCC is responsible for ensuring that inventory amounts provided in the NIRF and the DSCC Defense Stock Fund Trial Balance are complete, accurate, and reliable.

Acquisition Cost Accuracy

DSCC did not always accurately value the inventory items that it managed using available obligation history information. DSCC did not accurately value 307 of the items, with on-hand inventories valued at approximately \$8 million, based on the latest representative purchase price on record. The inaccurate acquisition costs resulted in approximately a \$2.5 million gross misstatement of the on-hand inventory values. Our analysis of the acquisition costs reflected the following errors as depicted in table 1.

Table 1. Items With Inaccurate Acquisition Costs			
<u>Reason for Inaccurate Acquisition Cost</u>	<u>Number of Items</u>	<u>Financial Inventory \$</u>	<u>Misstatement of Inventory \$</u>
Incorrect Estimations	143	\$4,998,972	\$1,895,082
FY 1992 Conversion to Latest Acquisition Cost	90	2,354,066	470,686
Inconsistent Data In Systems Computing and Reporting Costs	40	57,885	12,101
SAMMS Pricing System Errors	24	545,872	100,560
Zero Value Acquisition Costs	10	0	20,599
Totals	307	\$7,956,795	\$2,499,028

Estimated Acquisition Costs. Of the 307 items that were incorrectly priced, the acquisition costs for 143 were inaccurately estimated. The acquisition costs were identified by an acquisition cost code (ACC) of "E," indicating that they were estimated and not calculated by the SAMMS Pricing System based on obligation history records (see Appendix B for a definitions of ACCs). Documentation was not available to support the methodology used to estimate the acquisition costs, and they differed from the latest representative procurements on record.

Obligation History Records in the SAMMS Pricing System. Of the 143 items, 58 items had estimated acquisition costs that differed from the most recent procurement prices recorded on obligation history records in the purchase trailer of the SAMMS Pricing System. For example, one item in our review was a mechanical drive housing (NSN 3040-01-154-9958) that the DSCC construction commodity managed. At the time of our review, 14 of these assets were on hand valued at an acquisition cost of \$1,066 each. However, the most recent obligation history record in the purchase trailer section of the SAMMS Pricing System was for the stock replenishment of 17 items at a purchase cost per unit of \$809. We obtained the originating contract file and verified that the \$809 was the latest representative stock replenishment buy. No data supported the estimated acquisition cost of \$1,066, or explained why the last purchase cost per unit of \$809 was not used. As a result, the acquisition cost of the item was overstated by \$257, and the total inventory value for the 14 on-hand assets was overstated by \$3,598.

Acquisition costs for 2 of the 58 items were incorrectly estimated when catalog changes were processed in SAMMS to change the unit of issue for the items. When the new units of issue became effective, the acquisition costs were recomputed based on the old acquisition costs multiplied by a conversion factor. Problems with that process resulted in a significant overstatement of the inventory value for the affected items. For example, one item in our review was electrical wire (NSN 6145-01-303-8472) that the DSCC electronics commodity managed. At the time of our review, the NIRF showed an on-hand inventory balance of one sleeve (containing 500 feet of wire), valued at an acquisition cost of \$417,500 that was estimated when the unit of issue had converted from “each” to “sleeve” on April 1, 1999. The latest obligation record in the purchase trailer of the SAMMS Pricing System was for the stock replenishment of 500 feet of wire at a purchase cost of \$835. The unit of issue error resulted in a \$416,665 overstatement of the on-hand inventory value.

During the audit, the DLA Systems Integration Office implemented a system change to modify the methodology for calculating unit prices for items affected by unit-of-issue changes. However, the systems change was not retroactive. Therefore, all items inaccurately priced as a result of a unit-of-issue change would have to be manually identified and corrected.

Obligation History Records in Other SAMMS Files. Of the 143 incorrectly priced items, 40 items had estimated acquisition costs that differed from the most recent procurement prices recorded on obligation history records in other SAMMS contract history files. Obligation history records in the purchase trailer of the SAMMS Pricing System did not support the 40 items.

For 25 of the 40 items, DSCC did not use obligation history records provided by the previous DoD inventory manager during the logistics reassignment process to compute the acquisition cost. The obligation history records resided in the SAMMS logistics reassignment data file, a file that serves as a repository for supply management and contract history data that the losing DoD inventory manager provided during the logistics reassignment process, but were not posted to the SAMMS Pricing System. DLA logistics reassignment policy requires the gaining inventory control point to use contract history data

provided during the logistics reassignment process to price all transferred inventory. By not using the appropriate contract history data, DSCC misstated the inventory value for the affected items. For example, one item in our review was a turbine blade set (NSN 2825-00-147-2851) that the DSCC construction commodity managed. At the time of our review, six blade sets were on-hand that had been transferred from the Navy in 1994 as part of the logistics reassignment process. The SAMMS Pricing System showed an acquisition cost of \$110,871 that was estimated on October 1, 1996, however, the purchase trailer data section had no obligations to support the acquisition cost. Our review of the SAMMS logistics reassignment data file showed that as part of the management transfer in 1994, the Navy provided DSCC with obligation history data showing that the last contract unit price paid for the item was \$95,605. By not using the Navy-provided obligation history data, DSCC overstated the acquisition cost for the item by \$15,266, and the total inventory value for the six turbine blade sets was overstated by \$91,596.

For 15 of the 40 items, obligation history data resided in the contract history data listing section of the SAMMS contracting technical data file that differed from the estimated acquisition cost. The contracting technical data file is an automated database file that supports the procurement of items by DLA, and the contract history field should be updated automatically when a transaction is posted to the SAMMS active contract file by a DSCC contracting organization. None of the 15 items were supported by obligations in the purchase trailer of the SAMMS Pricing System. By not using the appropriate contract history data, DSCC misstated the inventory value for the affected items. For example, one item in our review was a circuit card assembly (NSN 5998-00-005-0278) that the DSCC electronics commodity managed. At the time of our review, 26 assets were on hand. The SAMMS Pricing System showed an acquisition cost of \$646 that was estimated on October 1, 1996, and the purchase trailer data section had no obligations to support the acquisition cost. Our review of the contract history buy data listing section of the SAMMS contracting technical data file showed that the most recent DSCC electronics contract was for 10 items at an acquisition cost of \$446 each. By not using the last contract price for the item, DSCC overstated the acquisition cost for the item by \$200 and overstated the total inventory value for the 26 items by \$5,200.

Obligation History Records in Other Contract History Files. Of the 143 incorrectly priced items, 43 items had estimated acquisition costs that differed from the most recent procurement prices recorded on obligation history records residing in the procurement history file that the Information Handling Service's Haystack Windows Online Service (the Haystack) maintained and that was readily available to DSCC. For those items, none of the SAMMS contract history files had obligation history records. The Haystack is an on-line parts research and logistics management system that provides comprehensive information on more than 11 million parts contained in the Federal Supply Catalog and related databases. The Haystack procurement history file contains procurement data obtained on a quarterly basis from the Military Departments and DLA through the Freedom of Information Act. The obligation history record from the procurement history file contains the contract number, source, date of contract award, unit price, purchased quantity, and total obligation amount. Contract information from the Haystack procurement history database appeared to be reliable. For the

545 items in our review for which we were able to obtain contract files, procurement history reports were available from the Haystack service for 543 of the items. The pricing information from the contract files for all 543 items matched the pricing information from the Haystack procurement history file.

The Haystack procurement history file showed latest purchase price information that differed significantly from the DSCC-assigned pricing data. For example, one item in our review was an Aircraft Exit Cone Assembly (NSN 1420-01-203-7028), which the DSCC construction commodity managed. At the time of our review, two assets on hand had been transferred from the Air Force in 1993 as part of the logistics reassignment process. The SAMMS Pricing System showed an acquisition cost of \$68,026 that was estimated on October 1, 1996, and the purchase trailer data section had no obligation history records. Additionally, no obligation history data were available in the SAMMS logistics reassignment data file. However, the logistics reassignment data file contained a \$67,654 standard (selling) price that the Air Force charged before transfer, which included the purchase cost of the item plus the Air Force surcharge. The Haystack procurement history report for the item showed that only one Air Force contract was awarded for the item, which was for the purchase for two items at a cost of \$56,136 each. The \$68,026 acquisition cost estimated by DSCC was \$11,890 more than the last recorded contract cost. Additionally, the DSCC standard (selling) price for the item at the time of our review was \$89,046, which was \$21,392 greater than the Air Force standard (selling) price before transfer and \$18,033 greater than the latest acquisition cost of \$56,136 plus the 26.5-percent DSCC surcharge.

Other Estimations. Of the 143 items incorrectly priced, 2 items had estimated acquisition costs that were not supported by valid obligation history data and the estimated acquisition costs differed significantly from the next best available pricing information. One item was a radio frequency amplifier (NSN 5996-01-316-0620), which the DSCC construction commodity managed. At the time of our review, 13 assets on hand had been transferred from the Navy in 1993 as part of the logistics reassignment process. The SAMMS Pricing System showed an acquisition cost of \$500 that was estimated on March 1, 1994, and the purchase trailer data section had no obligation history records. Additionally, the SAMMS logistics reassignment data file had no obligation history data. However, the logistics reassignment data file contained a \$32,030 standard (selling) price that the Air Force charged before transfer, which included the purchase cost of the item plus the Air Force surcharge. DSCC established the \$32,030 Air Force-provided standard price as the DSCC standard price on March 1, 1994, because the Air Force did not provide any obligation history data during the logistics reassignment process. However, DSCC could not support the \$500 acquisition cost. Therefore, we requested that DSCC establish a reasonable acquisition cost using the best available pricing information. An acquisition cost of \$23,210 was established for the item based on the \$32,030 Air Force-provided standard price less a 38-percent surcharge that DSCC applied to similar items. DSCC understated the inventory value for the 13 assets by \$295,230 (13 x \$22,710) because it used an inaccurate acquisition cost.

Similar problems may be resident in a material portion of the universe of DSCC-managed items. In addition to the items that were included in our review,

12 percent of the \$3.1 billion of inventory that DSCC reported on its September 30, 2000, NIRF was valued based on estimated acquisition costs (see table 4). The data were derived from a program that the DLA Systems Integration Office developed that stratified the number of items and on-hand inventory value on the September 30, 2000, DSCC NIRF by Acquisition Cost Code. DSCC managed 124,293 items, with on-hand assets valued at about \$357 million, that had an ACC of "E."

Conversion to Latest Acquisition Cost. For 90 of the 307 items incorrectly priced, DLA computed the acquisition costs when it converted to the latest acquisition cost inventory valuation method in FY 1992. Those acquisition costs were identified by an ACC of "C" in the SAMMS Pricing System. The conversion process did not ensure that the newly calculated acquisition cost was supported by the latest stock replenishment obligations.

Before 1992, the inventory maintained in SAMMS was valued at its standard price. The standard price of an item consisted of its acquisition cost plus a cost recovery percentage, or surcharge, and a 3.8 percent inflation factor that the managing inventory control point applied. On July 1, 1992, the DLA Systems Automation Center (renamed the DLA Systems Integration Office in June 1999) completed a massive change to SAMMS to value inventory at its latest acquisition cost rather than at its standard price. To compute the latest acquisition cost for each NSN, a one-time job was executed that scanned the SPMF and calculated an acquisition cost by removing the surcharge and the 3.8 percent inflation factor from the current standard price.

The conversion process resulted in a misstatement of the inventory value for the 90 affected items. To illustrate, one item in our review was an interference blanker (NSN 5895-00-442-3937) that the DSCC electronics commodity managed. At the time of our review, 36 assets were on hand, valued at an acquisition cost of \$741 each. The SAMMS Pricing System showed an ACC of "C," indicating that the acquisition cost was calculated when DLA converted to the latest acquisition cost inventory valuation method in FY 1992. However, the purchase trailer of the SAMMS Pricing System contained an obligation record for the stock replenishment of 25 items at a purchase cost per unit of \$517. Documentation was not available to support the acquisition cost of \$741. We concluded that the acquisition cost of the item was overstated by \$224, and the total inventory value for the 36 on-hand assets was overstated by \$8,064.

Additionally, the conversion process resulted in acquisition costs that were not supported by pricing information in other logistics files. For example, one item in our review was a shaft (NSN 3040-00-678-7419), that the DSCC construction commodity managed. At the time of our review, one shaft was on hand, valued at an acquisition cost of \$63,852. The SAMMS Pricing System showed an ACC of "C," indicating that the acquisition cost was calculated when DLA converted to the latest acquisition cost inventory valuation method in FY 1992. Our review of the SAMMS logistics reassignment data file indicated that management responsibility for the item was transferred from the Navy to DSCC in 1991. The Navy transferred one asset and provided DSCC with the item's standard price of \$4,310 (the \$3,285 cost of the item plus the Navy surcharge of \$1,025). Our review of a Haystack procurement history report for the item confirmed that the

Navy made only one purchase of the item in 1990 at a price of \$3,285. The DSCC Pricing Activity could not provide any support for the acquisition cost of \$63,852. As a result, the acquisition cost and total inventory value of the item was overstated by \$60,567. Additionally, the DSCC standard price for the item was \$80,773, which was \$76,463 greater than the \$4,310 standard price that the Navy charged for the item before management responsibility transferred to DSCC.

Similar problems may be resident in a material portion of the universe of DSCC-managed items. In addition to the items that were included in our review, 16 percent of the \$3.1 billion of inventory that DSCC reported on its September 30, 2000, NIRF was valued based on acquisition costs calculated during the conversion to the latest acquisition cost inventory valuation method in FY 1992 (See table 4). The data were derived from a program that the DLA Systems Integration Office developed that stratified the number of items and on-hand inventory value on the September 30, 2000, DSCC NIRF by Acquisition Cost Code. DSCC managed 320,796 items with on-hand assets, valued at about \$496 million, that had an ACC of "C." Because the conversion process was a one-time effort that was executed in FY 1992, we made no recommendations to correct its problems. However, DSCC should correct deficiencies introduced in the conversion process when it identifies and corrects the acquisition costs for the affected items residing in the NIRF.

Consistency Between Files Computing and Reporting Prices. For 40 of the 307 items incorrectly priced, the acquisition cost in the NIRF used to value the on-hand assets on the financial statements differed from the acquisition cost that the SAMMS Pricing System computed and that was maintained in the SPMF. The costs differed because no procedures were in place to ensure the consistency between the two files.

The SAMMS NIRF is the source file for the on-hand inventory amount reported on the DSCC Stock Fund trial balance. The NIRF contains a field for each item's acquisition cost. The acquisition cost on the NIRF should be based on the acquisition cost maintained in the SPMF, which the SAMMS Pricing System computed using obligation history records. Inconsistencies between the files resulted in a misstatement of the financial statement inventory value for the affected items. For example, one item in our review was a relay assembly (NSN 5945-00-933-6131) that the DSCC electronics commodity managed. At the time of our review, 12 assets on-hand, valued at an acquisition cost of \$199 each, were in the SAMMS NIRF. The SAMMS Pricing System showed an acquisition cost of \$143, which was supported by an obligation history record in the purchase trailer of the SPMF. The DSCC Pricing Activity could not explain why the acquisition cost in the NIRF, which is used to value assets in the financial statements, exceeded the acquisition cost in the pricing application by \$56. The inaccurate acquisition cost caused the financial statement inventory value for the item to be overstated by \$672.

SAMMS Pricing System Computations. For 24 of the 307 items incorrectly priced, the SAMMS Pricing System computed the acquisition costs based on obligation history records. The items were identified with an ACC of "A." Flaws

in the computation process resulted in a misstatement in the inventory value for the affected items.

Canceled Contracts. The SAMMS Pricing System inaccurately computed the acquisition costs for 15 of the 24 items based on contracts that had been canceled in their entirety. Because of a programming flaw, the Pricing System did not recalculate the acquisition cost using the second most recent stock replenishment obligation when the most recent obligation was canceled. The SAMMS Pricing System computed a new acquisition cost for an item when DSCC awarded a contract instead of when the materiel was actually received. When DSCC awarded a contract, an obligation transaction passed from the SAMMS procurement subsystem to the SAMMS Pricing System. The Pricing System computed a new acquisition cost using the newly received obligation transaction and all other eligible obligation records in the purchase trailer of the SPMF. When DSCC canceled a contract, the quantity and dollar value fields of the associated obligation history record in the purchase trailer data section were updated to reflect zeros. However, the SAMMS Pricing System did not recalculate the acquisition cost using the next most recent obligation history record.

The use of canceled contracts to develop acquisition costs resulted in the misstatement of inventory values. For example, one item in our review was a switch actuator adapter (NSN 5930-01-147-8667) that the DSCC electronics commodity managed. At the time of our review, 18 assets were on hand that had been transferred from the Navy in 1993 as part of the logistics reassignment process. The SAMMS Pricing System showed an acquisition cost of \$567 that was established on April 1, 1998, based on a DSCC contract awarded in 1998 for 20 items at a purchase cost per unit of \$567 each. The quantity and value fields of the obligation record in the purchase trailer contained zeros, and according to the originating contract file, the contract was canceled in its entirety in 1998. The contract was the only one awarded by DSCC for the item. Conversely, the SAMMS logistics reassignment data file showed that as part of the management transfer, the Navy provided DSCC with obligation history data showing that the last contract unit price paid for the items physically transferred was \$4. When the DSCC contract was canceled, no attempt was made to adjust the acquisition cost from \$567 to the next most recent contract price of \$4. As a result, the acquisition cost of the item was overstated by \$563, and the total inventory value for the 18 on-hand assets that had been transferred from the Navy was overstated by \$10,134. Additionally, the \$760 DSCC standard price of the item was significantly overstated for the item because it was calculated by multiplying the \$567 acquisition cost by a 34-percent surcharge. Had the \$4 acquisition cost been used, the standard price would have only been \$6.

We discussed the issue with the DLA Systems Integration Office and were informed that the programming did not allow for the acquisition cost to be recalculated when a contract was canceled. The computer specialist responsible for maintaining the SAMMS Pricing System implemented a systems change during the audit to correct the programming. However, the change was not retroactive. Therefore, the Pricing Activity at each DLA inventory control point would have to identify and correct any existing acquisition costs that were based on canceled contracts.

Other Inaccurate System-Calculated Acquisition Costs. Of the 24 items that had acquisition costs inaccurately computed by the SAMMS Pricing System based on obligation history records, 9 items had acquisition costs that were determined to be inaccurate for a variety of reasons that did not relate to the issues previously discussed. Reasons included nonrepresentative obligation history records being used in the acquisition cost calculation, representative obligation history records being left out of the acquisition cost calculation, and various other minor errors.

Items With No Acquisition Cost. For 10 of the 307 items that were incorrectly priced, no acquisition cost existed even though the NIRF contained on-hand assets. The acquisition cost was missing because no procedures were in place to ensure that all NSNs with on-hand inventory were assigned an acquisition cost. The lack of an acquisition cost resulted in an understatement of the inventory value for the affected items. For example, one item in our review was a brake and clutch re-liner (NSN 4910-01-018-0538) that the DSCC construction commodity managed. At the time of our review, 30 assets were on hand. The NIRF and the SPMF showed an acquisition cost of zero for the item. The last recorded purchase price for the item was \$439, and at our request, the DSCC Pricing Activity established the \$439 acquisition cost for the item. By not assigning a value to the 30 on-hand assets, DSCC understated the total inventory value by \$13,170.

We discussed the issue of items having no acquisition cost with the DLA Systems Integration Office, which told us that SAMMS had processes to ensure that all stocked items contained an acquisition cost in both the SPMF and the NIRF. However, items that were not coded as stocked (identified by a supply status code of 2) were exempt from the process because they generally did not have on-hand assets. Also, as a result of the audit, the DLA Systems Integration Office developed a program to identify all unusually low and high acquisition costs in the SAMMS NIRF and write them to a file. The items with unusually low acquisition costs included those with a zero value. The program was established as a permanent program that could be executed upon request. The DSCC Pricing Activity should use the program to identify all zero value acquisition costs at the end of each reporting period and ensure that they receive a reasonable price.

Quality Assurance Program for Inventory Prices. DSCC did not previously detect the inaccurate acquisition costs we identified because it had not established a quality assurance program to ensure the accuracy of inventory prices. With two pricing analysts responsible for maintaining accurate prices for more than 2 million items, efforts were focused on ensuring the accuracy of prices recommended by the SAMMS Pricing System for fast-moving (active) items before their release. However, many of the items that we found with inaccurate acquisition costs had little sales and procurement activity (were inactive) and were not reviewed. Some of the inaccurate acquisition costs that we identified had resided in SAMMS since FY 1992. For DSCC to ensure continued accuracy of all of its prices, it must establish a quality assurance program for inventory prices. As part of this program, the DSCC Pricing Activity should perform scheduled reviews on inactive items using the procedures described in DLA Manual 7000.2 as well as test the accuracy of prices for active items.

Availability of Obligation History Records

For 218 items with on-hand inventories valued at approximately \$14 million, obligation history records were not available in any of the SAMMS contract history files or the Haystack procurement history database to support the acquisition costs. The obligation history records were not available because they were not obtained during the logistics reassignment process or were purged from the contract history files (see table 2 for details). Without supporting obligation history records, we were unable to determine the accuracy of the assigned acquisition costs.

Table 2. Items Without Supporting Obligation History Records		
<u>Type of Item</u>	<u>Number of Items</u>	<u>Financial Inventory \$</u>
Logistics Gain	171	\$13,497,715
Non-Logistics Gain	<u>47</u>	<u>960,742</u>
Total	218	\$14,458,457

The SAMMS Pricing System contains a purchase trailer section in its SPMF to store current and historical procurement (obligation) records used in the acquisition cost calculation process. The Pricing System uses obligation transactions received from the SAMMS procurement subsystem to establish and update a purchase record resulting from DSCC procurement. A purchase record can also be established and updated by obligation transactions received from the SAMMS distribution subsystem if the transaction is the result of contract history data that another DoD inventory control point provided for an item that DSCC acquired through the logistics reassignment process (a logistics gain).

Each obligation transaction in the purchase trailer of the SAMMS Pricing System contains the following data: obligation document number, quantity, purchase cost per unit, total obligation amount, Government-furnished materiel unit cost, funds classification code, award date, and modification date. When multiple lines for a given NSN are procured on one contract, all lines are consolidated. The purchase trailer has the capability to store a maximum of 25 purchase records, including the latest three direct delivery purchase records, for each stocked item. The number of obligation trailers stored on each SPMF record varies according to the age of the trailer and the type of item. If the item is a logistics gain that has not had any activity, the system should keep trailers that are up to 5 years old. For other items, the system should keep trailers that are up to 3 years old based on the contract modification date provided in the obligation transaction.

Logistics Gain Items. Of the 218 unsupported items, DSCC acquired 171 items during the logistics reassignment process. We researched the SAMMS logistics reassignment data files for the items and found that obligation history data were not obtained during the logistics reassignment process. For logistics

gain items for which the obligation records were not obtained, the SAMMS Pricing System is programmed to set the acquisition cost equal to the standard price that the DoD inventory control point that previously managed the item provided. The standard price should represent the cost incurred by the previous DoD inventory manager to acquire the item plus the applicable cost recovery factor or surcharge. Using the standard price to value on-hand inventory resulted in an overstatement of the financial inventory value.

Other Items. Of the 218 unsupported items, 47 items were not supported by obligation history records and were not identified as logistics gains. For those items, all obligation history data were purged from the purchase trailer of the SAMMS Pricing System. We researched additional automated sources of contract data, but the other sources of contract data were unable to provide support for the assigned acquisition costs.

Availability of Contract Files

For 670 items with on-hand inventories valued at approximately \$30 million, obligation history records existed in the purchase trailer data of the Pricing System or other obligation history databases to support the acquisition costs, but the originating contract files were not available to support the limited information provided on the obligation history record. The supporting contract files were not available because they were destroyed because their age exceeded DLA contract file retention requirements, were not obtained during the logistics reassignment process, or were lost. Details are provided in table 3.

Table 3. Items Without Supporting Contract Files		
<u>Reason For Missing Contract File</u>	<u>Number of Items</u>	<u>Financial Inventory \$</u>
Not Obtained During Logistics Reassignment Process	354	\$25,983,147
Age Exceeded DLA Retention Requirements	290	2,539,831
Lost	26	1,091,719
Total	670	\$29,614,697

DLA Contract File Retention Requirements. The DLA policy for retaining contract files is established in DLA Instruction 5015.1, “DLA Records Management Procedures and Records Schedule,” March 1, 2000. DLA policy defines contracts as individual and subcontract case files accumulated from the administration of individual contracts consisting of purchase orders, contracts, comparable instruments, and other documentation, as applicable, as required by the Federal Acquisition Regulation. According to DLA policy, contracts for more than \$25,000 are to be retained for 6 years and 3 months after final payment. Contracts for \$25,000 or less are to be retained for 3 years after final payment.

The retention criteria are based on the timeframes established in the Defense Federal Acquisition Regulation Supplement.

DSCC Contract Retention Procedures. DSCC did not have local procedures specifying the time period for retaining contract files. The DSCC organizations that we visited to obtain contract files informed us that they relied on DLA policy and the Defense Federal Acquisition Regulation Supplement. Personnel from the DSCC records holding organization informed us that contract files more than 6 years old were generally destroyed unless specific justification was provided for their retention.

Obligation Records for Logistics Gain Items. Of the 670 items that had an obligation history record in the purchase trailer of the SAMMS Pricing System but for which the actual contract file was unavailable, the file was unavailable for 354 items because DSCC did not obtain it during the logistics reassignment process. We could not be reasonably assured that those obligation records were reliable without reviewing the actual contract files. Additionally, the age of the most recent obligation history records that the Military Departments provided that supported the acquisition costs raised concerns about the future utility (likelihood of sales) of the on-hand inventory because the inventory valuation assertion also requires that all slow-moving inventory be properly identified and valued. For 235 items, the date of the most recent obligation was 1990 or earlier. For 21 items, the date of the most recent obligation history record was between 20 and 26 years old.

Obligation Records Exceeding DLA Contract Retention Periods. Of the 670 items that did not have their originating contract file, 290 items had a DLA obligation history record in the purchase trailer of the SAMMS Pricing System or other contract history database but the actual contract file was destroyed because it exceeded the contract retention requirements of DLA. The lack of contract files prohibited us from determining whether the acquisition costs were based on representative stock replenishment buys and were void of abnormal costs, such as excessive handling or rework costs. Additionally, the age of the most recent obligation history records supporting the acquisition costs raised concerns about the future utility of the on-hand inventory. For 193 items, the date of the most recent obligation was 1990 or earlier. For 12 items, the date of the most recent obligation history record was between 20 and 26 years old.

Obligation Records Within the Federal Contract Retention Period. Of the 670 items that had a DLA obligation history record in the purchase trailer of the SAMMS Pricing System, the actual contract files were not available for review for 26 items even though their contract modification dates fell within the contract retention requirements of DLA. The contract files had been lost by the responsible DSCC organization.

Importance of Originating Contract Files. Without being able to review the originating contract files, we could not be reasonably assured that the limited data provided on the obligation records were complete and accurate. For example, one item in our review was an elevation control (NSN 1010-01-258-1473), which the DSCC construction commodity managed. At the time of our review, 44 assets were on hand, valued at an acquisition cost of \$4,317 each. The

Pricing System showed that the acquisition cost was based on an average of two obligation records that were retained in the purchase trailer section. Both obligation records were coded as representative stock replenishment buys. However, the actual contract files showed that the most recent buy included a contract line for the direct shipment of material. The assets on the direct shipment line were each priced at \$449 more than the other assets that were part of a stock replenishment line on the same contract. The direct shipment and stock replenishment contract lines were combined to develop the acquisition cost for the item. Had only the stock replenishment line been used, the acquisition cost would have been calculated at \$4,179 each, which was \$138 less than the assigned acquisition cost. Recalculating the acquisition cost using only the stock replenishment line resulted in a decrease to the on-hand inventory value of \$6,072.

Contracting Initiatives. DSCC started developing a paperless acquisition folder in 1995 and hired a contractor to design an Electronic Contract Folder, which provided a completely electronic and interactive Windows-based electronic procurement folder and was designed to capture all documentation that was provided in the hard copy contract folder. The folder had an automatic archive and storage capability designed to comply with the Federal Acquisition Regulation and the Defense Federal Acquisition Regulation Supplement. The initial phase of the effort provided for an electronic folder for all automated micro-purchase awards starting in November 1997. During our review, the Aerospace Weapons System Group was participating in a testing phase to scan all of its contracts into the Electronic Contract Folder, and if successful, the effort was to be expanded to all weapon system groups. The initiative would eventually eliminate the requirement to physically store hard-copy contracts and should minimize the number of contracts that are lost during the manual storage process.

Actions Taken and Potential Monetary Benefits

During the course of our audit, the DSCC Pricing Activity corrected 261 of the inaccurate acquisition costs brought to its attention. The Pricing Activity did not correct the acquisition costs for which later procurement action had taken place or for which the overall impact to the inventory value was insignificant. We found the actions to be reasonable. In addition, the DLA Systems Integration Office processed systems changes to the SAMMS Pricing System to correct some of the problems identified during the audit.

Impact on Financial Reports. By correcting the inaccurate acquisition costs, DSCC improved the accuracy of its on-hand inventory by \$2.5 million. The amount represented the variance between the acquisition cost in the NIRF at the time of our review and the latest acquisition cost as identified by our audit. The variance between the acquisition costs was multiplied by the number of DSCC-owned assets on the NIRF to arrive at the financial inventory value misstatement for each item. The financial inventory value misstatement for all items was combined to arrive at the \$2.5 million.

Potential Monetary Benefits Resulting From Reduced Selling Prices. By correcting the inaccurate acquisition costs, DSCC reduced the standard (sales) prices charged to customers by \$2 million for on-hand inventory expected to be sold over the 6-Year Future Years Defense Program. The amount represented the standard price variance multiplied by the number of DLA-owned assets on the NIRF. The standard price variance was the difference between the old standard price (the inaccurate acquisition cost multiplied by the applicable DSCC surcharge) and the revised standard price (the corrected acquisition cost multiplied by the applicable DSCC surcharge). The standard price variance for all items was combined to arrive at the \$2 million. We believe that the \$2 million reduction in the selling price for the on-hand inventory will result in funds put to better use by DSCC customers.

Potential for Additional Acquisition Cost Inaccuracies

We believe that the potential for the problems identified during the audit to exist in a material amount in the universe of DSCC inventory is significant. During the audit, we identified 143 items that had acquisition costs that were inaccurately estimated (identified by an ACC of “E”). Additionally, 90 items had acquisition costs that were inaccurately computed during the initial acquisition cost conversion in FY 1992 (identified by an ACC of “C”). Of the 307 items with inaccurate acquisition codes, there were a total of 233 items with inaccurate acquisition costs identified by ACCs of “C” and “E.”

A significant number of items in the FY 2000 DSCC NIRF were coded as being computed in the same manner as those found inaccurate by our audit. As depicted in table 4, there were 445,089 NSNs with on-hand assets had acquisition costs identified by ACCs “C” and “E,” which represented more than 50 percent of the 875,854 DSCC-managed items. Additionally, the \$853 million on-hand inventory value for those items represented about 28 percent of the total \$3.1 billion DSCC inventory value as of September 30, 2000.

Acquisition Cost Code	NSNs With On-Hand Assets	Percent of Total NSNs	Total On-Hand Inventory Value	Percent of Total Value
A	429,786	49.1	\$2,198,966,682	71.8
C	320,796	36.6	496,438,536	16.2
E	124,293	14.2	356,942,194	11.7
Other	979	0.1	10,132,619	0.3
Total	875,854¹	100.0	\$3,062,480,031	100.0

¹ DSCC manages over 2 million items. However, only 875,854 had on-hand assets at September 30, 2000. As a result of DoD inventory reduction initiatives, DSCC manages many items as non-stocked where inventories are shipped directly to DoD customers from contractor facilities.

Summary

The 1,740 items we reviewed represented only a small portion of the total DSCC inventory because they were selected as part of an effort to measure the accuracy of all DLA-owned inventories. However, we believe that items having acquisition costs that were developed in the same manner as those found to be inaccurate by our review exist in a material amount in the total universe of DSCC inventory. Additionally, the system changes implemented by the DLA Systems Integration Office were not retroactive, and we do not know how many additional items exist in the universe of DSCC inventory that were valued using the inaccurate methods identified. DSCC needs to review the NIRF and identify and correct all additional inaccurate acquisition costs.

We also believe that additional inventory valuation problems may have gone undetected because DSCC had not established a quality assurance program to ensure the accuracy of its inventory prices.

Further, we could not determine the reasonableness of the acquisition costs used to value on-hand inventories for items without supporting obligation history records. A significant number of items were valued using acquisition costs that could not be supported by obligation history records in the SAMMS Pricing System or other automated contract history files. In the absence of procurement histories, DoD 7000.14-R permits DoD activities to estimate acquisition costs based upon current manufacturer's price listings or market price quotations. DSCC must identify all items that are not supported by obligation history records and estimate a reasonable price using DoD guidance.

Additionally, we could not be reasonably assured that the acquisition costs used to value on-hand inventories were based on the latest representative stock replenishment buy and were void of any abnormal costs without being able to review the supporting contract files. Contract files will not be available to support the significant number of items that had acquisition costs based on obligation history records that were more than 6 years old or that were provided electronically by the Military Departments during the logistics reassignment process. In the absence of the originating contract files, DSCC must disclose the value of the on-hand inventory that cannot be properly supported, and the disclosures must continually be made until the amount of inventory valued based on unsupported acquisition costs is reduced to an immaterial amount. Also, because on-hand inventory is frequently retained longer than the maximum 6-year time period required for retaining the contract files that support the last purchase price, DSCC must establish that the obligation history records in the SAMMS Pricing System are reliable and contain accurate information based on the originating contract files. Until all of those actions are accomplished, we cannot be reasonably assured that financial inventory values that DSCC reported are free from material misstatement.

While our review showed that 68.7 percent of the items reviewed at the Defense Supply Center Columbus were not accurately computed or were not supported,

similar rates of discrepancy were found in items reviewed at the Defense Supply Centers in Richmond and Philadelphia. Systemic problems found at the three Centers will be addressed in a summary report.

Management Comments on the Finding and Audit Response

Management Comments. The Director, DLA Logistics Operations, provided comments for the Commander, Defense Supply Center Columbus. DLA partially concurred with the finding but stated that the DLA procedure is to compute the latest representative acquisition cost using the weighted average acquisition cost of stocked items using the latest contract and any other buys made in the preceding 44 days. DLA concurred that the audit identified areas where DLA could improve policies and procedures.

Audit Response. We accepted the DLA averaging methodology as accurate during the audit. The acquisition costs we identified as inaccurate differed significantly from the most recent representative purchase price, including the average of the most recent purchase price and all buys made in the preceding 44 days.

Recommendations, Management Comments and Audit Response

We recommend that the Commander, Defense Supply Center Columbus:

1. Develop and implement procedures to accurately compute acquisition costs used to value on-hand inventories based on the latest representative purchase prices. The procedures should require the DSCC Pricing Activity to:

a. Fully document and maintain the methodology used to estimate acquisition costs and use the latest representative purchase prices as a basis.

Management Comments. DLA partially concurred and stated that it uses the weighted-average of costs from recent representative contract prices to determine the cost of an item. DLA agreed to review DLAM 7000.2 and ensure that the DLA inventory valuation methodology is fully documented by July 31, 2001.

Audit Response. The DLA comments were partially responsive to the recommendation. However, the DLA comments did not specifically mention acquisition costs that are estimated. DLA's corrective actions should specifically include procedures to document the supporting data for acquisition costs that are estimated.

b. Use consistent acquisition cost data in the national inventory record file and the standard pricing master file.

Management Comments. DLA concurred and agreed to conduct a review of discrepant prices in the national inventory record file and the standard pricing master file and make necessary corrections by September 28, 2001.

c. Use the program developed by the DLA Systems Integration Office to identify and correct all acquisition costs with a zero value at the end of each reporting period.

Management Comments. DLA partially concurred and agreed to review items with stock on hand without an acquisition cost and update as appropriate by September 28, 2001. DLA stated that the DSIO [DLA Systems Integration Office] program was developed as a one-time effort to provide data for the audit.

Audit Response. We consider the DLA comments to be responsive. However, as stated in the report, the program developed by the DLA Systems Integration Office to identify acquisition costs with a zero value is a permanent “as required” program which can be executed upon request.

d. Identify and correct all acquisition costs residing in the national inventory record file that were computed using the inaccurate methods identified by this audit, including acquisition costs that were incorrectly estimated, acquisition costs incorrectly computed during the FY 1992 conversion to the latest acquisition cost inventory valuation method, and acquisition costs erroneously based on canceled contracts.

Management Comments. DLA partially concurred and agreed to review the current DoD inventory valuation policies by September 28, 2001, to ensure compliance of DLA policies and procedures, especially concerning the appropriateness of eliminating acquisition costs erroneously based on canceled contracts. DLA further stated that its pricing methodology of averaging the most recent contracts results in more accurate pricing for the types of items it manages.

Audit Response. We consider the DLA comments to be partially responsive. DLA did not address acquisition costs that were estimated and those computed during the FY 1992 valuation method conversion. We request that DLA comment on plans to identify and correct those acquisition costs in response to the final report.

2. Establish a quality assurance program to ensure the accuracy of inventory prices. The program must include procedures to test the accuracy of prices for all items including inactive items.

Management Comments. DLA concurred with this recommendation and stated that the Defense Supply Center Columbus will coordinate with the other DLA Supply Centers to develop a sampling program to test the accuracy of inventory prices with emphasis given to stratification by date of last procurement activity. Upon completion, the sampling program will be disseminated to the other supply centers by September 28, 2001.

3. Develop and implement procedures to identify and disclose the value of on-hand inventories where contract data do not support acquisition costs.

The procedures should identify the total inventory value for items with acquisition costs not supported by obligation history records and require that the acquisition costs for those items be estimated based upon current manufacturer's price listings or market price quotations. Additionally, the disclosure should provide the total inventory value for items with acquisition costs based on obligation history records provided by the previous managing inventory control point for logistics gain items and acquisition costs based on Defense Supply Center Columbus obligation history records more than 6 years old.

Management Comments. DLA partially concurred, stating that they agree in principle with the recommendation, but because it will require an intensive manual effort, they will assess the costs and benefits of any changes prior to implementation. DLA stated that the analysis would be completed by July 31, 2001.

- 4. Develop and implement procedures to retain contract data to support the acquisition costs used to value on-hand inventories on the financial statements. The procedures should require the retention of the latest representative obligation history record in the purchase trailer of the standard pricing master file and require the retention of supporting contract files in accordance with Defense Logistics Agency retention requirements.**

Management Comments. DLA partially concurred and stated that DLA retains contract files in accordance with the Federal Acquisition Regulation and that retention beyond those timeframes for items that have not been procured beyond this period would have far reaching impact not only to DLA but the Military Services. Additionally, the Military Services would also be required to retain and pass the records upon logistics reassignments. DLA stated that the recommendation should be addressed to the Under Secretary (Comptroller) for review and comment.

Audit Response. Although DLA partially concurred, we consider the comments to be nonresponsive. Our recommendation does not require that contract files be retained beyond Federal Acquisition Regulation guidelines and it does not apply to the Military Departments. We found that the SAMMS Pricing System did not always retain the latest representative obligation history record (or records if DLA's weighted average methodology applied). Additionally, DLA contracts supporting the acquisition costs for 26 items, with on-hand inventory valued over \$1 million, were unavailable for review even though their dates fell within the retention requirements of the Federal Acquisition Regulation. We believe that DLA needs to address the retention limitations of obligation history records in the SAMMS Pricing System. Additionally, DLA needs to issue procedures to its Inventory Control Points specifying the Federal Acquisition Regulation requirements and ensure that these procedures are incorporated in to any automated contract folder initiatives. Those actions are the responsibility of DLA, not the Under Secretary of Defense (Comptroller). We request that DLA provide comments to the final report.

Appendix A. Audit Process

Scope

We performed this audit as part of the requirements of Public Law 101-576, the “Chief Financial Officers Act of 1990,” November 15, 1990, as amended by Public Law 103-356, the “Federal Financial Management Act of 1994,” October 13, 1994. For this part of the audit, we limited the scope of our review to verifying the accuracy of inventory valuation information at DSCC.

Work Performed. We performed the audit at DLA headquarters, DSCC, and the DLA Systems Integration Office. We analyzed the acquisition costs for 1,740 DSCC-managed items to determine whether the acquisition costs were calculated in accordance with Federal accounting policy. Our analysis included verifying the acquisition costs to the originating detailed transaction data (the contract). As part of our audit, we reviewed numerous inventory-related documents, including the following:

- Federal accounting policy, DoD financial management regulations, and DLA procedures and policies on valuing and reporting inventories;
- file interrogation reports for each applicable item from the SAMMS SPMF, NIRF, logistics reassignment data file, and the contracting technical data file contract history buy data listing;
- DLA Systems Integration Office documents describing the SAMMS Pricing System;
- procurement history reports from the Information Handling Service’s Haystack Windows Online Service for each applicable item;
- DD Form 1155, “Order for Supplies or Services,” and related contracting documents supporting obligation records used in calculating the acquisition cost for each applicable item; and
- SAMMS transaction history file reports (for the maximum 24-month period) for items that were found to be inaccurately priced.

We verified the acquisition cost for each item by obtaining contract data at the managing inventory control point because the acquisition cost in DLA is updated when a contract is awarded and not upon the receipt of goods. In addition, we did not believe that sufficient invoice data would be available at the DLA distribution depots because they are required to retain copies of receipt invoices (DoD Form 250, “Material Inspection and Receiving Reports”) for a period of only 2 years. In addition, we believed that the significant relocation of inventories resulting from Defense base realignment and closure actions would also limit the availability of original invoice data.

Limitations to Audit Scope. Our audit work was limited to determining whether the acquisition costs used to value DSCC inventory were based on Federal accounting policy and supported by contract data. We did not assess the reasonableness of the price paid for the items or the reasonableness of the DSCC surcharge rates.

DoD-Wide Corporate-Level Government Performance and Results Act Coverage. In response to the Government Performance and Results Act, the Secretary of Defense annually establishes DoD-wide corporate-level goals, subordinate performance goals, and performance measures. This report pertains to achievement of the following goal:

FY 2001 DoD Corporate-Level Goal 2: Prepare now for an uncertain future by pursuing a focused modernization effort that maintains U.S. qualitative superiority in key warfighting capabilities. Transform the force by exploiting the Revolution in Military Affairs, and reengineer the Department to achieve a 21st century infrastructure. **(01-DoD-2)**

- **FY 2001 Subordinate Performance Goal 2.5:** Improve DoD financial and information management. **(01-DoD-2.5)**
- **FY 2001 Performance Measure 2.5.2:** Achieve unqualified opinions on financial statements. **(01-DoD-2.5.2)**

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

Financial Management Functional Area. Objective: Reengineer DoD business practices. **Goal:** Standardize, reduce, clarify, and reissue financial management policies. **(FM-4.1)**

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

Methodology

We reviewed Federal accounting standards and DoD and DLA policies and procedures for valuing inventories. We also interviewed various DSCC personnel involved in the inventory valuation process, including procurement specialists and pricing analysts. In addition, we interviewed computer specialists at the DLA Systems Integration Office who were responsible for supporting the SAMMS Pricing System.

We performed a review of the acquisition costs used to value 1,740 DSCC-managed NSNs on the SAMMS NIRF, which serves as the source file for

the on-hand inventory value on the DSCC Stock Fund trial balance. We interrogated the SAMMS SPMF for each item to determine the methodology used to calculate the acquisition cost. We also reviewed the purchase trailer data section of the SAMMS Pricing System to determine whether obligation history records supported the acquisition cost. In addition, we reviewed procurement history reports from the Information Handling Service's Haystack Windows Online Service for each NSN to determine whether obligation history records supported the acquisition cost. We also reviewed the SAMMS logistics reassignment data file and the SAMMS contracting technical data file for each item. For items with obligation records that supported the acquisition cost, we requested the contract folder from the appropriate DSCC organization. We reviewed the contract folder for each item to determine whether the obligation data maintained in the SPMF were complete and accurate and reflected the last representative invoice price as defined by Federal accounting standards. For items that we found to be inaccurately valued, we obtained SAMMS transaction history file reports for the maximum 24-month period available to determine whether any assets had been sold at the inaccurate price. Additionally, we obtained the DSCC surcharge rates for FYs 1999 and 2000 in order to calculate the impact that the inaccurate acquisition costs had on the standard price.

Universe and Sample. Of the 1,740 items that we reviewed, 1,336 items were part of a DLA-wide sample of 3,153 records selected as part of a sampling plan that DLA executed to assess the accuracy of its FY 1999 financial statement inventory value. In June 1999, DLA fielded a sampling plan to test the accuracy of the portion of its inventory stored at 18 DLA distribution depots operating under the Distribution Standard System. As part of that effort, DLA used a two-stage, stratified, random sampling procedure to select a sample of 3,153 records from the Distribution Standard System operating files at 11 DLA distribution depots for the period ending June 30, 1999. NSN by location (all condition codes) served as the unit of analysis or sample record. Inventory values for the 3,153 records were determined using the acquisition cost from the SAMMS operating files at the managing DLA inventory control points.

In our review of the DLA sampling plan, we reported that the plan did not include procedures to test the accuracy of the unit prices in the SAMMS operating files at the managing DLA inventory control points. We decided to test the accuracy of the 3,153 records in SAMMS. Of the 3,153 records, 1,448 were identified in the Distribution Standard System as being managed by DSCC. The 1,448 records consisted of 1,446 individual NSNs. During our review, we found that for 50 of the 1,446 NSNs, management responsibility had transferred from DSCC to another manager. Additionally, we found that 60 items had zero on-hand assets. Removing those items left the total number of DSCC-managed items with on-hand assets that were selected as part of the DLA sampling plan at 1,336.

In addition to the 1,336 items, a judgmental sample of 404 items was selected for review from the SAMMS NIRF, which serves as the source file for the inventory amounts reported on the financial statements. The 404 items were selected as part of our initial survey effort and during the audit to provide greater coverage of the unusually low and high acquisition costs and acquisition costs lacking an ACC.

This report will not project the results from the 1,740 items to the DSCC total inventory universe. However, we will comment on the total 3,153 records selected as part of the DLA sampling plan in a separate summary report.

Use of Computer-Processed Data. To achieve the audit objective, we relied on computer-processed data from the DLA SAMMS. We did not test the general and application controls in SAMMS. Specifically, we analyzed the acquisition costs and obligation history data in the NIRF and the SPMF.

Of the 1,740 items that we reviewed, we determined that the computer-processed acquisition cost data were unreliable for 307 items in the NIRF. We were not able to determine the reliability of the computer-processed acquisition cost data in the SPMF for 888 items because DSCC could not provide the obligation history records (218 items) or the originating contract files (670 items). The computer-processed acquisition cost and supporting obligation history data in the SPMF were reliable for 545 items that we reviewed because we were able to verify the accuracy of the information to source documents.

Audit Type, Dates, and Standards. We performed this financial-related audit from May 1999 through November 2000. Our review was made in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. Accordingly, we included tests of management controls considered necessary.

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

Management Control Program Review

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, and DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, require DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls.

Scope of the Review of the Management Control Program. We reviewed the FY 2000 Annual Statements of Assurance issued by DLA and DSCC to determine whether the issues addressed in this report had been reported as material management control weaknesses.

Adequacy of Management Controls. We identified material management control weaknesses, as defined by DoD Directive 5010.38, related to the valuation of DSCC inventory. The details of the management control weaknesses are provided in detail in the Finding section of this report. All of the recommendations in this report, if implemented, will improve the accuracy and reliability of DSCC inventory values. A copy of the report will be provided to the senior official responsible for management controls.

Adequacy of Management's Self-Evaluation. The FY 2000 DLA and DSCC Annual Statements of Assurance did not identify any material control weakness related to the valuation of DSCC inventory.

Prior Coverage

Inspector General, DoD, Report No. D-2000-138, "Procedures Used to Test the Dollar Accuracy of the Defense Logistics Agency Inventory," June 1, 2000.

Inspector General, DoD, Report No. D-2000-086, "Assuring Condition and Inventory Accountability of Chemical Protective Suits," February 25, 2000.

Appendix B. Acquisition Cost Calculation

As described by DLA Manual 7000.2, volume II, part I, "Standard Automated Materiel Management System Financial Subsystem Operating Procedures," July 1, 1999, the acquisition cost calculation is an automated process that the Pricing System performs within the SAMMS financial subsystem. SAMMS maintains one acquisition cost value for each NSN without regard to the number of assets on-hand. The acquisition cost is recomputed as new procurement actions occur. The acquisition cost for an item is equivalent to its average replacement cost as calculated from obligation history records contained on the SPMF. The acquisition cost is the sum of all eligible obligation amounts divided by the sum of their obligation quantities plus Government-furnished materiel costs and any other applicable costs contained on the SPMF. Acquisition costs for stocked items are calculated using an average of all stock replenishment buys awarded during the past 6 months, plus all other stock replenishment buys that occurred within 45 days of the latest stock buy. The quantity of the buys used must also be at least equal to 1 month's demand based on historical data. All mechanically recommended price changes are held in suspense at least 7 days to enable the Pricing Activity to review, revise, or delete as applicable.

Each item that is assigned an acquisition cost has a corresponding acquisition cost date and acquisition cost code (ACC). The acquisition cost date is the Julian date on which the acquisition cost became effective and should always be the first of the month. The ACC is a one-position field describing how the acquisition cost was developed. The ACCs are defined in the following table.

Definitions of Acquisition Cost Codes

<u>ACC</u>	<u>Definition</u>
A	Acquisition cost was computer generated based on obligation transactions in the SPMF. The transactions may result from a DLA award or from obligation transactions provided by the previous inventory manager if the item was a logistics gain.
C	Acquisition cost was computed during a DLA-wide conversion from standard price to latest acquisition cost in July 1992, and no procurement action took place since the initial conversion.
E	Acquisition cost was estimated.
G	Acquisition cost was based on the standard price provided by the previous manager upon transfer of management responsibility to DLA.

Appendix C. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller)
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)

Department of the Army

Auditor General, Department of the Army

Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy

Department of the Air Force

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

Other Defense Organizations

Director, Defense Logistics Agency
Commander, Defense Supply Center Columbus

Non-Defense Federal Organizations and Individuals

Office of Management and Budget

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Efficiency, Financial Management, and Intergovernmental Relations, Committee on Government Reform
House Subcommittee on National Security, Veterans Affairs, and International Relations, Committee on Government Reform
House Subcommittee on Technology and Procurement Policy, Committee on Government Reform

Defense Logistics Agency Comments



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

IN REPLY
REFER TO J-3

FEB 16 2001

MEMORANDUM FOR DDAI

SUBJECT: Audit Report on Inventory Valuation at the Defense Supply Center Columbus,
Project No. D2000FJ-0067.002 (formerly Project No. OFJ-2102.02)

As requested in your memorandum dated December 18, 2000, attached are J-3's comments on the subject report.

A handwritten signature in black ink, appearing to read "D. H. Stone".

D. H. STONE
Rear Admiral, SC, USN
Director
Logistics Operations

Attachment



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



IN REPLY
REFER TO

J-33

FEB 8 2001

MEMORANDUM FOR J-31

SUBJECT: Audit Report on Inventory Valuation at the Defense Supply Center Columbus,
Project No. D2000FI-0067.002 (formerly Project No. OFJ-2102.02)

Comments to subject audit are attached as requested. Coordination is also provided at Attachment 2. Because the recommendations are regarding pricing, we recommend that any follow-up to the report be forwarded to J-8 for action.

William J. Kenny
WILLIAM J. KENNY
Executive Director
Logistics Policy and Acquisition Management

Attachments

Subject: Inventory Valuation at the Defense Supply Center Columbus,
Project No. D20000FJ-0067.002 (formerly Program No. OFJ-2102.02)

Finding: The Defense Supply Center Columbus assertion that inventory valuation was accurate and supported by contract data was not reliable. Of the 1,740 items selected for review with on-hand inventories valued at \$64 million, the values assigned to 1,195 items with on-hand inventories valued at \$52 million were not accurately computed based on the latest representative obligations or were unsupported. . . . Until the deficiencies leading to the inaccurate and unsupported acquisition costs are corrected and fully disclosed, DSCC inventory valuation data cannot be relied upon to support the inventory amounts reported on the DLA financial statements. (See page 3 of report).

DLA Comments: Partially Concur. The DLA procedure is to compute the latest representative acquisition cost using the weight average acquisition cost of stocked items using the latest contract and any other buys made in the preceding 44 days. For nonstocked items, the weighted average of the prices of all buys in the last 6 month period from the most recent buy is used. DLA uses this weighted average method which dampens the impact of wide fluctuations in quantities and resulting unit prices that can occur within such short timeframes. This methodology is the best approach for the types of items managed by DLA. We do concur that the audit has identified areas where we can improve the policies and procedures. These are addressed in the following recommendations.

Recommendations for Commander, Defense Supply Center Columbus:

1. Develop and implement procedures to accurately compute acquisition costs used to value on-hand inventories based on the latest representative purchase price. The procedures should require the DSCC Pricing Activity to:
 - a. Fully document and maintain the methodology used to estimate acquisition costs and use the latest representative purchase price as a basis.

DLA Comments: Partially Concur. To determine the acquisition cost of an item, DLA uses the weighted average of costs from recent representative contract prices. We agree that the procedure should be fully documented, and included in DLAM 7000.2. We will review the manual and ensure that the current policy is appropriately documented. Action to be completed by July 2001.

Disposition:

- Action is ongoing. ECD: July 31, 2001
 Action is considered complete.

b. Use consistent acquisition cost data in the national inventory record file and the standard pricing master file.

DLA Comments: Concur. This is the DLA practice. The standard pricing master file is the source of the acquisition costs data in the national inventory record file; however, instances can occur when an update to the standard pricing master file has not yet been recorded in the national inventory record file. DLA will conduct a review to identify causes and take any required corrective actions.

Disposition:

Action is ongoing. ECD: September 28, 2001
 Action is considered complete.

c. Use the program developed by the DLA Systems Integration Office to identify and correct all acquisition costs with a zero value at the end of each reporting period.

DLA Comments: Partially Concur. While DSIO has developed a program to provide data to DODIG Teams, this has been done on one time basis. There is no recurring report at this time. Although the report shows that this is a minor issue (10 items resulting in a net overstatement of the inventory value of \$20,599), DLA will review items with stock on hand that show no acquisition cost and update as appropriate. In addition, we will refer this requirement to our Business Systems Modernization office for inclusion in the new automated system.

Disposition:

Action is ongoing. ECD: September 28, 2001
 Action is considered complete.

d. Identify and correct all acquisition costs residing in the national inventory record file that were computed using the inaccurate methods identified by this audit, including acquisition costs that were incorrectly estimated, acquisition costs incorrectly computed during the FY 1992 conversion to the latest acquisition costs inventory valuation method, and the acquisition costs erroneously based on canceled contracts.

DLA Comments: Partially Concur. DLA has found that our pricing methodology of averaging the most recent contracts to compute the prices results in more accurate pricing for the types of items that we manage. DLA will review the current DoD inventory valuation policies to ensure compliance of DLA policies and procedures, especially concerning the appropriateness of eliminating acquisition costs erroneously based on canceled contracts. Based on this review, DLA will take action as appropriate.

Disposition:

Action is ongoing. ECD: September 28, 2001
 Action is considered complete.

2. Establish a quality assurance program to ensure the accuracy of inventory prices. The program must include procedures to test the accuracy of prices for all items including inactive items.

DLA Comments: Concur. The Defense Supply Center Columbus will develop a sampling program to test accuracy of inventory prices. Particular attention will be given to stratification by date of last procurement activity. We will coordinate with the other DLA Centers to ensure a sampling program is already being utilized. Upon completion, a sampling program will be disseminated to the other Centers for use as appropriate.

Disposition:

- Action is ongoing. ECD: September 28, 2001
 Action is considered completed.

3. Develop and implement procedures to identify and disclose the value of on-hand inventories where contract data do not support acquisition costs. The procedures should identify the total inventory value for items with acquisition costs not supported by obligation history records and require that the acquisition costs for those items be estimated based upon current manufacturer's price listings or market price quotations. Additionally, the disclosure should provide the total inventory value for items with acquisition costs based on obligation history records provided by the previous managing inventory control point for logistics gain items and acquisition costs based on Defense Supply Center Columbus obligation history records more than 6 years old.

DLA Comments: Partially Concur. We agree in principle with the recommendation but because this will require an intensive manual effort, we will assess the costs and benefits of changes prior to implementation.

Disposition:

- Action is ongoing. ECD: July 31, 2001
 Action is considered complete.

4. Develop and implement procedures to retain contract data to support the acquisition costs used to value on-hand inventories on the financial statements. The procedures should require the retention of the latest representative obligation history record in the purchase trailer of the standard pricing master file and require the retention of supporting contract files in accordance with Defense Logistics Agency retention requirements.

DLA Comments: Partially Concur. DLA retains contract files in accordance with the Federal Acquisition Regulation. Retention beyond these timeframes for items that have not been procured beyond this period would have far reaching impact not only DLA but the Military Services. The Military Services would also be required to retain and pass these records upon logistics reassignments. This recommendation should be readdressed to the Under Secretary (Comptroller) for review and comment.

Disposition:

- Action is ongoing. ECD:
 Action is considered complete.

Audit Team Members

The Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD, prepared this report. Personnel of the Office of the Inspector, DoD, who contributed to the report are listed below.

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