

March 22, 2002



Logistics

DoD International Personal Property Shipment Rates (D-2002-068)

Department of Defense
Office of the Inspector General

Quality

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Report Documentation Page

Report Date 22 Mar 2002	Report Type N/A	Dates Covered (from... to) -
Title and Subtitle Logistics: DoD International Personal Property Shipment Rates	Contract Number	
	Grant Number	
	Program Element Number	
Author(s)	Project Number	
	Task Number	
	Work Unit Number	
Performing Organization Name(s) and Address(es) OAIG-AUD(ATTN: AFTS Audit Suggestions) Inspector General Department of Defense 400 Army Navy Drive Arlington, VA 22202-2884	Performing Organization Report Number	
	Sponsor/Monitor's Acronym(s)	
Sponsoring/Monitoring Agency Name(s) and Address(es)	Sponsor/Monitor's Report Number(s)	
Distribution/Availability Statement Approved for public release, distribution unlimited		
Supplementary Notes		
Abstract		
Subject Terms		
Report Classification unclassified	Classification of this page unclassified	
Classification of Abstract unclassified	Limitation of Abstract UU	
Number of Pages 17		

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Acronyms

CONUS	Continental United States
COS	Code of Service
HHG	Household Goods
MTMC	Military Traffic Management Command
SFR	Single Factor Rate
USC	Universal Service Contract



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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March 22, 2002

MEMORANDUM FOR DEPUTY UNDER SECRETARY OF DEFENSE
(LOGISTICS AND MATERIEL READINESS)
COMMANDER IN CHIEF, U.S. TRANSPORTATION
COMMAND

SUBJECT: Audit Report on DoD International Personal Property Shipment Rates
(Report No. D-2002-068)

We are providing this audit report for your information and use. We performed this audit in response to allegations made to the Defense Hotline. No written response to this report was required, and none was received. Therefore, we are publishing this report in final form.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Dennis E. Payne at (703) 604-8907 (DSN 664-8907) (dpayne@dodig.osd.mil) or Mr. Albert L. Putnam at (703) 604-8779 (DSN 664-8779) (aputnam@dodig.osd.mil). See Appendix B for the report distribution. The audit team members are listed inside the back cover.

A handwritten signature in black ink, appearing to read "Thomas F. Gimble", is positioned above the printed name.

Thomas F. Gimble
Acting
Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. D-2002-xxx
Project No. D2001LH-0163

March xx, 2002

DoD International Personal Property Shipment Rates

Executive Summary

Introduction. This audit was initiated in response to a Defense Hotline allegation concerning household goods shipments originating in the Mediterranean region of Europe. The allegation claimed that under current procedures [Code of Service 4] DoD was paying excessive costs for ocean transportation on household goods shipments because a third party company purchased all or most of the cargo space available on U.S.-flag vessels and subsequently resold the space at an inflated price to selected freight forwarders* that participated in the DoD International Personal Property Program. The complainant alleged that the excessive costs were passed on to the Government when the freight forwarders submitted new rates to the Military Traffic Management Command for approval. The Defense Hotline complaint also stated that if DoD implemented Code of Service 3 for household goods shipments, the ocean transportation would be provided under a Government contract negotiated directly with ocean carriers and all freight forwarders would pay the same rate for ocean transportation. The complaint also claimed that using Code of Service 3 would eliminate the third party monopoly and lower the overall cost of DoD household goods shipments. Between October 1, 1999, and August 24, 2002, 51,154 surface shipments of household goods were moved from 9 selected areas of Europe to the continental United States.

Objectives. The objectives of the audit were to: determine the validity of the Defense Hotline allegation that DoD was incurring excessive costs on personal property shipments; evaluate the effectiveness of the codes of service and rates used; determine whether procedures were in compliance with applicable regulations; and evaluate the management control program relative to the objectives. We did not complete the objective to evaluate the management control program relative to the objectives because the allegation was not substantiated and the audit was terminated.

Results. The Defense Hotline allegation was not substantiated. We contacted the complainant who did not provide any substantive information to validate the allegation. We also contacted 18 freight forwarders involved in moving DoD household goods

*Freight forwarder refers to the commercial carrier approved by the Military Traffic Management Command to make international household goods shipments. The freight forwarder has the ultimate responsibility for the entire move.

from Europe to the continental United States and asked questions to determine the validity of the allegation. Of the 18 freight forwarders we contacted, 17 stated that they were not aware of any third party company controlling most or all of the sealift capacity of U.S.-flag vessels sailing between Europe and the continental United States, and they had not experienced any problems booking container space on U.S.-flag vessels. Two of the freight forwarders contacted acknowledged that some companies purchased substantial amounts of container space and resold some of the space to freight forwarders that made DoD household goods shipments. However, those companies do not control all or most of the sealift capacity of U.S.-flag vessels. We also contacted four ocean carrier representatives to determine if their vessels operated at full capacity on voyages between the continental United States and Europe. The ocean carrier representatives' response was that container space on U.S.-flag vessels sailing from Europe was available on the majority of voyages, but depending on economic conditions in effect at the time of a voyage, times exist when a vessel will sail at maximum cargo capacity.

We could not evaluate the cost and operational effectiveness of using Code of Service 3 versus Code of Service 4 because information required for such an evaluation was not available.

Management Comments. We provided management a draft of this report on February 27, 2002. No written response to this report was required. Management informed us on March 6, 2002, that they concurred with the report and would not be providing a written response. Therefore, we are issuing this report in final form.

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Background

Defense Hotline Allegation. This audit was conducted in response to an allegation to the Defense Hotline. The complainant alleged that the DoD was charged excessive costs for ocean transportation on household goods (HHG) shipments originating in the Mediterranean region of Europe. The complainant stated that the excessive costs occurred because a third party company purchased all or most of the container space available on U.S.-flag vessels and resold the space at inflated prices to freight forwarders* who participated in the DoD International Personal Property Program, which allowed the third party company to establish monopolistic control over DoD HHG shipments because the Cargo Preference Act of 1904 requires that DoD shipments be transported on U.S.-flag vessels. The complainant also stated that some freight forwarders were being denied an opportunity to participate in the DoD International Personal Property Program by the third party company because of price gouging. Further, the complainant implied that sealift may not be offered to some freight forwarders who can afford the high rates. Nevertheless, the excessive costs were subsequently passed on to the Government when the freight forwarders submitted new rates [single factor rates] to the Military Traffic Management Command (MTMC) during the biannual rate submission cycles. In addition, the allegation claimed that a case study conducted on HHG shipments originating in the Mediterranean region affirmed that excess ocean costs were being charged for DoD HHG shipments.

The complaint also stated that if DoD implemented Code of Service (COS) 3 for shipments originating in Europe, ocean transportation would be provided under a Government contract and all of the freight forwarders would pay the same rate, thereby eliminating the excessive ocean transportation costs.

Between October 1, 1999, and August 24, 2002, 51,154 surface shipments of household goods were moved from 9 selected areas of Europe (including Belgium, Crete, Germany, Italy, the Netherlands, Portugal, Spain, Turkey, and the United Kingdom) to the continental United States (CONUS).

Codes of Service. DoD uses two codes of service (COS 3 and COS 4) for HHG shipments made by commercial carriers by way of surface transportation. Under COS 3, the freight forwarder is responsible for origin service, line haul to the port, line haul to the destination, and destination services. The ocean transportation under COS 3 is provided under the provisions of a Government contract negotiated directly with the ocean carrier. With the exception that the freight forwarder is responsible for arranging and providing the ocean transportation, COS 4 is identical to COS 3. **Single Factor Rate.** Both COS 3 and COS 4 shipments use a single factor rate (SFR) to charge the Government for HHG shipments. The SFR is a dollar amount applied to each 100 pounds of

*Freight forwarder refers to the commercial carrier approved by the Military Traffic Management Command to make international HHG shipments. The freight forwarder has the ultimate responsibility for the entire move.

cargo. The rate is applied to the total shipment weight to determine the total shipment cost. Freight forwarders develop an SFR for each lane of traffic for which they wish to compete and submit the rates to MTMC during each biannual rate submission cycle. The SFR for COS 3 and COS 4 shipments includes origin, line haul, and destination costs. The SFR for COS 4 shipments also includes the ocean transportation charges. For COS 3 shipments, which use the Government contract for ocean transportation, the freight forwarder pays the ocean carrier directly and then bills the ocean transportation costs as a separate item on the HHG shipment invoice submitted to the Government.

Objectives

The objectives of the audit were to: determine the validity of the Defense Hotline allegation that DoD was incurring excessive costs on personal property shipments; evaluate the effectiveness of the COS and rates used; determine whether procedures were in compliance with applicable regulations; and evaluate the management control program relative to the objectives. We did not complete the objective to evaluate the management control program relative to the objectives because the allegation was not substantiated and the audit work was terminated. See Appendix A for a discussion of audit scope, methodology, and prior audit coverage.

Ocean Transportation Costs

The complaint to the Defense Hotline alleged that DoD was paying excessive ocean transportation costs on HHG shipments originating in the Mediterranean region of Europe. We interviewed the complainant, freight forwarders, ocean carrier representatives, and DoD transportation officials and found no substantive evidence to support the allegation that DoD was paying excessive ocean transportation costs because a third party company had monopolistic control over the sealift capacity of U.S.-flag vessels sailing from the Mediterranean region of Europe. Therefore, the Defense Hotline allegation was not substantiated.

Response From Complainant

We contacted the complainant and requested additional documentation to support the allegation. Specifically, we requested that the complainant provide: the identity of the third party company; a list of HHG freight forwarders being overcharged or denied container space; a copy of the study that validated the effectiveness of COS 3; a list of the ports where the alleged overcharging had occurred; and any other relevant information to support the allegation.

We made several followup requests and were provided no additional information to support the allegation. The complainant provided a point of contact at MTMC who allegedly participated in the case study referenced in the allegation. We discussed the matter with the point of contact and other MTMC officials and were provided with a study performed on HHG shipments originating in the Pacific region. MTMC personnel also told us that they were not aware of any study done on shipments between Europe and CONUS, and that COS 3 had never been used for HHG shipments between Europe and CONUS.

Responses From Freight Forwarders

We contacted senior management personnel at 18 freight forwarding companies that participated in the DoD International Personal Property Program and asked questions to determine the validity of the complaint. We selected six freight forwarders that made HHG shipments from each of the personal property shipping offices located at Aviano, Italy; Naples, Italy; and Grafenwoehr, Germany. We asked each of the freight forwarders the following questions:

- Are you aware of a third party company buying all or most of the available container space on U.S.-flag ocean carriers?
- Has your firm experienced difficulty booking container space?

-
- Have there been substantial increases in the rates charged for shipping containers? In your opinion, are the prices charged fair and reasonable?
 - What COS does your firm prefer, and would your company compete for HHG shipments from Europe under COS 3?

Third Party Buying Container Space. Of the 18 freight forwarders contacted, 17 stated that they were not aware of any third party buying all or most of the available container space and selectively reselling the space at an exorbitant rate. Two of the freight forwarders added that buying container space in volume to receive a discount and then reselling some of that space to other smaller freight forwarders, including those making DoD HHG shipments, is a common industry practice. However, companies that buy container space in volume do not control all or most of the available sealift capacity of U.S.-flag vessels. Of those two freight forwarders that stated buying and reselling container space is a common industry practice, one stated that it uses a third party to book international DoD HHG shipments because it obtains a lower rate from the third party than from the ocean carrier. The freight forwarder added that because it was able to book container space from other high volume freight forwarders, it was able to compete for DoD business. One freight forwarder did indicate that a third party was buying and monopolizing container space, but added that it was at specific CONUS ports. Based on the responses from the freight forwarders contacted, a third party monopolizing sealift capacity of U.S.-flag vessels in Europe does not appear to exist.

Difficulty in Booking Container Space. Of the 18 freight forwarders contacted, each stated that they had no difficulty in booking container space on U.S.-flag vessels for shipments originating in Europe. One respondent stated that it had difficulty booking container space; however, the problems occurred at specific CONUS ports on shipments to Europe. Based on the responses from the freight forwarders, we found no substantive evidence to support that a systemic problem exists in booking container space for HHG shipments on U.S.-flag vessels sailing from Europe to CONUS.

Price of Container Space. Of the 18 freight forwarders contacted, 15 responded to the question about the price of container space. Of the 15 who responded, 14 freight forwarders stated that rates charged for ocean container space were, in their opinion, fair and reasonable. Of those 14 freight forwarders, 3 stated that during the last 5 years the rates had dropped (1 stated by as much as 30 percent). The other freight forwarder who responded to the question stated that container rates were too high and had doubled in the last 3 years. However, that freight forwarder also acknowledged that the fluctuations go both ways. Based on the overall responses, no substantive evidence was present to support the allegation that prices for ocean container space on shipments originating in Europe were unreasonable.

COS Preference. Of the 18 freight forwarders contacted, 13 stated that they would compete for shipments from Europe using COS 3, 2 stated they would not, and 3 did not answer. Regarding preference for a particular COS, 10 of

the 18 freight forwarders stated that they preferred COS 4 to make HHG shipments, 4 stated a preference for COS 3, 1 stated it did not matter, and 3 did not answer. The primary reason given by the freight forwarders that expressed a preference for COS 4 was that it gave them flexibility to provide the best service to the DoD Service member. Under COS 3, the freight forwarder must use specific carriers and ports. Some freight forwarders stated that those specific carriers and ports might not provide the timeliest service, which might result in required delivery dates not being met and the military Service members receiving inferior service.

Responses From Ocean Carriers

We contacted four ocean carriers that operate U.S.-flag vessels the DoD HHG freight forwarders used. Each ocean carrier representative stated that their vessels were not usually filled to capacity for transatlantic voyages. The ocean carrier representatives further stated that freight forwarders obtained volume discounts for booking significant amounts of container space, and subsequently resold the space to other freight forwarders, but not at exorbitant rates. Some ocean carrier representatives and freight forwarders contacted stated that obtaining volume discounts and reselling the space to other freight forwarders is a common industry practice. Based on the information provided by the ocean carrier representatives, no one freight forwarder or third party company appears to control the majority of sealift capacity on U.S.-flag vessels operating between Europe and CONUS.

Effectiveness of Code of Service 3

Transportation officials in the International Personal Property Section at MTMC stated that COS 3 has never been used for HHG shipments in Europe; therefore, no historic baseline data were available to compare the cost effectiveness of using COS 3 versus COS 4 for shipments originating in Europe. To determine the effectiveness of using COS 3, the Universal Services Contract (USC), which is the existing Government freight contract with ocean carriers, would have to be renegotiated to include HHG cargo. MTMC would also have to issue a new solicitation to freight forwarders to obtain SFRs for COS 3 shipments. Because the data were not available, we could not evaluate the cost and operational effectiveness of using COS 3 rather than COS 4.

Universal Services Contract. To implement COS 3 in Europe, the USC would have to be renegotiated to include HHG shipments. The USC contract has a general provisions section and four customer service annexes. The customer service annexes provide the shipping rates and specific shipping requirements for the four largest Defense shippers under the USC contract—the Defense Logistics Agency, the Defense Commissary Agency, the Army Air Force Exchange Service, and the Navy Exchange Command. HHG shipments under COS 3 would be made using the provisions of the general section of the USC contract. Each section of the contract contains cargo minimums and maximums, as well as the steamship companies for the particular routes. To implement

COS 3 between CONUS and Europe, the cargo minimums and maximums would have to be revised to include HHG shipments and the rates renegotiated.

COS 3 Rates. Because COS 3 has never been used for HHG shipments between Europe and CONUS, MTMC would have to solicit SFRs from all of the freight forwarders that wanted to compete on HHG shipments under COS 3. Without knowing which freight forwarders would participate in HHG shipments under COS 3, and the SFR for each particular route, estimating the cost to the Government of an HHG shipment under COS 3 or determining the cost effectiveness of using COS 3 versus COS 4 is not possible.

Conclusion

Based on information from the complainant, freight forwarders, ocean carrier representatives, and various DoD transportation officials, no substantive evidence was present that supported the allegation that DoD paid excessive costs for ocean transportation on HHG shipments originating in Europe. In addition, the cost effectiveness of COS 3 could not be evaluated because the information needed to develop an accurate baseline for comparison purposes did not exist. Because audit results did not identify information to support the allegation, we discontinued further work on this audit and issued the report with no recommendations.

Appendix A. Audit Process

Scope and Methodology

We reviewed applicable policies, procedures, processes, and regulations related to the DoD International Personal Property Program. We met with transportation officials from the Personal Property Division and the Joint Traffic Management Office at headquarters, MTMC and discussed the Defense Hotline allegations, obtained information on a 1998 case study that analyzed the effectiveness of COS 3 and COS 4 HHG shipments in the Pacific region, and collected rate and shipment data for transatlantic HHG movements for FY 1999, FY 2000, and FY 2001. We also contacted the complainant for additional information, as well as representatives of the Maritime Administration, senior management officials at 18 freight forwarding companies, 4 ocean transportation companies, and 4 Transportation Management Offices to discuss the allegation and obtain relevant information.

Scope Limitations. Most of our audit work consisted of preliminary planning research to clarify the broadly written and nonspecific allegation contained in the Defense Hotline. Accordingly, audit conclusions in this report are based on limited contact with the complainant, the Maritime Administration, selected freight forwarders, ocean carriers representatives, and transportation officials at MTMC. We were unable to identify any specific instances of limited competition, unfair pricing, or monopolistic control of container space on U.S.-flag vessels. Because the audit disclosed no evidence to substantiate the allegation, detailed tests of documentation, shipment pricing and payments, internal controls, and compliance with applicable laws and regulations were not performed.

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

Use of Computer-Processed Data. We used computer-processed data from the MTMC Transportation Operational Personal Property Standard System to obtain shipment data. The data were used to identify freight forwarders that moved HHG shipments between Europe and CONUS during the time frames and in the geographical areas we selected. We concluded that the data were sufficient for this purpose; therefore, we did not assess the reliability or accuracy of the computer-processed data.

Audit Type, Date, and Standards. We performed this economy and efficiency audit from August through December 2001 in accordance with generally accepted government auditing standards.

Contacts During the Audit. We visited or contacted individuals and organizations within the DoD, the complainant, the Maritime Administration,

and senior management personnel of ocean shipping companies and selected freight forwarding companies. Further details are available on request.

Prior Coverage

No prior coverage has been conducted on transportation codes of service for international HHG shipments during the last 5 years.

Appendix B. Report Distribution

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Audit Team Members

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

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