DOD EXCESS PROPERTY SYSTEMS: THROWING AWAY MILLIONS

HEARING

BEFORE THE

SUBCOMMITTEE ON NATIONAL SECURITY, EMERGING THREATS, AND INTERNATIONAL RELATIONS

OF THE

COMMITTEE ON GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED NINTH CONGRESS

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DOD EXCESS PROPERTY SYSTEMS: THROWING AWAY MILLIONS

TUESDAY, JUNE 7, 2005

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON NATIONAL SECURITY, EMERGING THREATS, AND INTERNATIONAL RELATIONS,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 2:15 p.m., in room 2154, Rayburn House Office Building, Hon. Christopher Shays (chairman of the subcommittee) presiding.

Present: Representatives Shays, Duncan, Dent, and Waxman.

Staff present: Lawrence Halloran, staff director and counsel; J. Vincent Chase, chief investigator; Robert A. Briggs, clerk; Sam Raymond, intern; Andrew Su, minority professional staff member; Earley Green, minority chief clerk; and Jean Gosa, minority assistant clerk.

Mr. SHAYS. A quorum being present, the Subcommittee on National Security, Emerging Threats, and International Relations hearing entitled, "DOD Excess Property Systems: Throwing Away Millions" is called to order.

Following the frugal maxim, "One man's trash is another man's treasure," the Department of Defense [DOD], sells or donates equipment and commodities determined to be in excess of military needs. But now we find the Pentagon is throwing out a great deal of treasure with the trash, disposing of items at steep discounts through one program while other offices within DOD buy the same things new and at full price.

Problems in the DOD excess property system are chronic, they're dangerous, and extensive. Three years ago this subcommittee discovered DOD continued to sell top-grade chemical protective suits on the Internet while military units were waiting to acquire exactly the same gear at 10 times the on-line cost. In 2003, we revealed the indiscriminate sale of biological lab equipment by DOD without an assessment of the risks it might be used against us by terrorists. Today, the true scope and costs of systemic weaknesses in the surplus supply chain come into clearer view.

At the subcommittee's request, the Government Accountability Office [GAO], extensively audited and tested DOD excess property systems. Their report released this afternoon finds substantial waste and inefficiencies intractably embedded in sloppy, uncoordinated management and inventory control processes. The numbers we will hear are staggering. Each year DOD disposes of property that costs billions to acquire, yet GAO found at least $400 million

spent over 2 fiscal years on the purchase of items that need not have been bought at all because they were already paid for and available in that surplus pool. Many of the items here today fit that description, good-as-new or serviceable equipment that DOD sold to GAO for a fraction of the price it was paying to buy the same material.

This isn't just a matter of bad bookkeeping, lax management or weak inventory controls, these numbers measure major systemic weaknesses in critical combat support machinery. Waste on this scale affects our ability to meet the immediate needs of men and women in uniform. The $400 million spent on unneeded equipment could have bought body armor, medical supplies, or more than 1,700 fully armored Humvees to protect Coalition forces against deadly improvised explosive devices.

Simply put, DOD buys too much and then cannot, with any accuracy, track where the excess property is or who might need it. Once dropped into the multi-billion dollar slurry of the excess property system, good equipment can mix with bad, get left out in the rain, or disappear altogether. Such an unaccountable system easily hides malfeasance and invites theft.

Some broken links in this clumsy and costly chain of custody are well known. For more than a decade, GAO has found that DOD asset visibility and inventory management weaknesses pose a huge risk of waste, abuse and fraud. Now we find DOD's bargain basement is leaking badly, hemorrhaging on a scale that no business could or would tolerate.

The time is long past for standard approaches and marginal fixes to a fundamentally broken system. As supplier to the warfighter and stewards of immense fiscal resources, DOD must have end-to-end visibility and control over the purchase, transportation, storage, use and final disposition of military inventory. Those who buy too much this year have to know they will pay a price when the equipment appears for sale on the Internet next year for one-tenth the acquisition cost.

We are grateful to the GAO team for an in-depth report on a very serious problem, and we look to our DOD witnesses for a discussion of equally serious solutions.

At this time, the Chair would recognize the ranking member of the full committee, Mr. Henry Waxman.

[The prepared statement of Hon. Christopher Shays follows:]

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Statement of Rep. Christopher Shays
June 7, 2005

Following the frugal maxim "One man's trash is another man's treasure," the Department of Defense (DOD) sells or donates equipment and commodities determined to be in excess of military needs. But now we find the Pentagon is throwing out a great deal of treasure with the trash, disposing of items at steep discounts through one program while other offices buy the same things new and at full price.

Problems in the DOD excess property system are chronic, dangerous and extensive. Three years ago, this Subcommittee discovered DOD continued to sell top-grade chemical protective suits on the Internet while military units were waiting to acquire exactly the same gear at ten times the on-line cost. In 2003, we revealed the indiscriminate sale of biological lab equipment by DOD without an assessment of the risks it might be used against us by terrorists. Today, the true scope, and costs, of systemic weaknesses in the surplus supply chain come into clearer view.

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The numbers we will hear are staggering. Each year, DOD disposes of property that cost billions to acquire. Yet GAO found at least four hundred million dollars spent over two fiscal years on the purchase of items that need not have been bought at all because they were already paid for, and available, in that surplus pool. Many of the items here today fit that description: good-as-new or serviceable equipment that DOD sold to GAO for a fraction of the price it was paying to buy the same material.

This isn't just a matter of bad bookkeeping, lax management or weak inventory controls. These numbers measure major systemic weaknesses in critical combat support machinery. Waste on this scale affects our ability to meet the immediate needs of men and women in uniform. The four hundred million dollars spent on unneeded equipment could have bought body armor, medical supplies or more than 1700 fully armored HUMVEES to protect Coalition forces against deadly improvised explosive devices.

Simply put: DOD buys too much and then cannot with any accuracy track where the excess property is or who might need it. Once dropped into the multi-billion dollar slurry of the excess property system, good equipment can mix with bad, get left out in the rain or disappear altogether. Such an unaccountable system easily hides malfeasance and invites theft.

Some broken links in this clumsy and costly chain of custody are well known. For more than a decade, GAO has found that DOD asset visibility and inventory management weaknesses pose a high risk of waste, fraud and abuse. Now we know DOD's bargain basement is leaking badly, hemorrhaging on a scale that no business could tolerate.

The time is long past for standard approaches and marginal fixes to a fundamentally broken system. As supplier to the warfighter, and stewards of immense fiscal resources, DOD must have end-to-end visibility and control over the purchase, transportation, storage, use and final disposition of military inventory. Those who buy too much this year have to know they will pay a price when that equipment appears for sale on the Internet next year for one-tenth the acquisition cost.

We are grateful to the GAO team for an in-depth report on a very serious problem. And, we look to our DOD witnesses for a discussion of equally serious solutions.

Mr. WAXMAN. Thank you very much, Mr. Chairman. I'm glad the subcommittee is holding this hearing today on procurement problems at Defense, and I commend you for your leadership on this issue.

I'm going to be blunt in my remarks. This administration is squandering literally billions of dollars on wasteful Federal contracts. Private contractors are reaping a bonanza while taxpayers are being gouged. Whether the explanation is gross incompetence or deliberate malfeasance, the result is the same: Taxpayers are being vastly overcharged.

The litany of this administration's mismanagement of Federal contracts is long and costly. The value of no-bid contracts has skyrocketed under the Bush administration. Oversight of Federal contracts has been turned over to private companies with blatant conflicts of interest, and when government auditors do find abuse their recommendations are ignored.

Nearly every week the papers are full of stories of contract abuse. The Department of Homeland Security has wasted hundreds of millions of dollars on security contracts that have produced virtually no result. The FBI has spent $170 million on virtual case file software that doesn't work. And in Iraq, Halliburton has overcharged by hundreds of millions of dollars, yet the administration continues to shower the company with Federal funds, bonuses and special treatment.

Unfortunately, these are not isolated incidences, they are a pattern of wanton abuse and mismanagement.

In today's hearing we will hear about a particularly egregious example of abuse. GAO tells us that the Pentagon has squandered $3½ billion in valuable new equipment by selling it off at fire-sale prices. But in Iraq, our soldiers are dying because we cannot find the resources to buy the proper armor for our troops and their vehicles.

But here in the United States, the Pentagon has sold off billions of dollars worth of medical equipment, power supply units, helicopters, vehicle parts, combat boots, and even military medals at salvage prices.

And these examples are the rule, not the exception. According to GAO, the Defense Department gets fair value for surplus Federal property just 12 percent of the time. The rest of the time the Defense Department has destroyed perfectly good equipment or sold it for pennies on the dollar.

Congress has a responsibility to do oversight to prevent these abuses. That's why I commend Chairman Shays for holding this hearing. But we also need legislation, and for this reason I will soon be introducing the Clean Contracting Act to stop these indefensible procurement and disposal practices.

I want to thank the chairman for requesting the GAO report that is the subject of today's hearing, as well as the ranking member of the subcommittees, and I especially want to thank Greg Kutz and the other members of the GAO, the investigative team, for their excellent work on this important report.

Thank you, Mr. Chairman.

[The prepared statement of Hon. Henry A. Waxman follows:]

Statement of
Rep. Henry A. Waxman, Ranking Minority Member
Committee on Government Reform
Before the Subcommittee on National Security, Emerging Threats, and International Relations
Hearing on "DOD Excess Property: Throwing Away Millions"

June 7, 2005

Mr. Chairman, I am glad the Subcommittee is holding this hearing on procurement problems at the Department of Defense. And I commend you for your leadership on this issue.

I am going to be blunt in my remarks. This Administration is squandering literally billions of dollars on wasteful federal contracts. Private contractors are reaping a bonanza, while taxpayers are being gouged. Whether the explanation is gross incompetence or deliberate malfeasance, the result is the same: taxpayers are being vastly overcharged.

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But we also need legislation. For this reason, I will soon be introducing the Clean Contracting Act to stop these indefensible procurement and disposal practices.

Fundamentally, what's wrong is a question of priorities. When the President proposes tax cuts, the largest benefits go to the rich, not the middle class. And when the Administration hands out federal contracts, the most important constituency becomes the well-connected private contractors, not the average taxpayer. The result is minimal oversight and exorbitant waste, fraud, and abuse.

I thank the Chairman and Ranking Member for requesting the GAO report that is the subject of today's hearing. And I especially want to thank Greg Kutz and the other members of the GAO investigative team for their excellent work on this important report.

Mr. SHAYS. Thank you, Mr. Ranking Member. The Chair would now recognize Mr. Duncan.

Mr. DUNCAN. Well, thank you very much, Mr. Chairman. Once again you're out in front of and on top of a very important subject. I commend you for calling this hearing.

I don't know the full details, but I do understand that the report shows that during fiscal years 2002, 2003 the GAO found that the Department of Defense disposed of $2.2 billion worth of materials that were reported to be in A condition, that were either brand new and unused or barely used, and that those things were in new or excellent condition. And I know that we talk about billions up here like it's so much that it becomes meaningless, but that is a lot of money. It is an unbelievable, staggering amount of money.

I understand further that on July 30, 2003 the report says the Department of Defense sold 172 pairs of new cold weather boots, valued $23,220, for $69, less than a cost of one pair of shoes; that during those years surveyed the Department of Defense destroyed $73.7 million in circuit cards, $10.2 million in radio sets, $9.1 million in aircraft parts, $3.4 million worth of power supply units, on and on and on; that the Department purchased at least $400 million of identical items during this time instead of using available excess A condition items.

The Pentagon, the Department of Defense, seems to have the idea that this Congress will give them anything it wants no matter how terrible the job is that they do, how wasteful the job is that they do, and maybe that's the case but it shouldn't be. The report says the Defense Reutilization and Marketing Services offices that has the responsibility for handling the express property have experienced losses of $466 million from 2002 to 2004, and that one DRMO holding excess property had an error rate of 47 percent.

Let me tell you this: Anybody who is not horrified by this does not deserve to call themselves a conservative; anybody that is not horrified by this does not deserve to be called a friend of the taxpayer; anybody who is even remotely connected to this should be ashamed. Any large business with this kind of record, their stock would drop dramatically, heads would roll, people would be gotten rid of.

I know that the cause of this civil service system that gives way too much protection to people who screw up horribly, that nothing will be done or very little will be done, but hopefully somebody will act on this and do something about this because this type of record should not—this type of activity should not continue to go on.

Thank you very much, Mr. Chairman.

Mr. SHAYS. I thank the gentleman very much. And just to announce that it's our intention, as we said before, to hold a hearing on June 21st on the U.S. Stewardship of the Development Fund for Iraq [DFI], the successor fund to the U.N. Oil for Food Program, which is basically Iraqi money under our stewardship. And we know we need to be looking at that and will be.

At this time, the Chair would just welcome our first panel. We have one speaker, Mr. Gregory Kutz, Managing Director of Forensic Audits and Special Investigations, U.S. Government Accountability Office, accompanied by Ms. Gayle Fischer, Assistant Direc-

tor; Mr. John J. Ryan, Assistant Director/Special Agent; and Mr. Keith Rhodes, Chief Technologist. We welcome all of you.

Is there anyone else that might be responding to questions, Mr. Kutz?

Mr. KUTZ. One other.

Mr. SHAYS. So we will ask that individual to stand as well as I administer the oath.

[Witnesses sworn.]

Mr. SHAYS. Note for the record our primary witness and those accompanying him have responded in the affirmative. And let me just take care of one—I ask unanimous consent that all members of the subcommittee be permitted to place an opening statement in the record, and that the record remain open for 3 days for that purpose. Without objection, so ordered. I ask further that all witnesses be permitted to include their written statement in the record. Without objection, so ordered.

And if I can, before you start, congratulations on a document that helps us do our job better and will help the DOD do its job better. We thank you for being here.

Mr. Kutz, we're going to have a 5-minute period, and then we'll roll it over for another 5 minutes, but within 10 minutes I'm sure you can cover what you need to. And then we will start with questions.

STATEMENT OF GREGORY D. KUTZ, MANAGING DIRECTOR, FORENSIC AUDITS AND SPECIAL INVESTIGATIONS, U.S. GOVERNMENT ACCOUNTABILITY OFFICE, ACCOMPANIED BY GAYLE L. FISCHER, ASSISTANT DIRECTOR, FORENSIC AUDITS AND SPECIAL INVESTIGATIONS; JOHN J. RYAN, ASSISTANT DIRECTOR/SPECIAL AGENT, FORENSIC AUDITS AND SPECIAL INVESTIGATIONS; AND KEITH RHODES, CHIEF TECHNOLOGIST, APPLIED RESEARCH AND METHODS

Mr. KUTZ. Mr. Chairman, Ranking Member Waxman and Congressman Duncan, thank you for the opportunity to discuss the sale of DOD excess property.

Previously we testified that DOD was selling excess property that could be used to produce and disseminate anthrax. We also testified that DOD was selling new chem-biosuits on the Internet for $3, while at the same time buying them for $200.

Based on these findings, you asked us to conduct a broader study of the economy and efficiency of this system. Our bottom line today is that ineffective management oversight and controls have resulted in hundreds of millions of dollars of waste and inefficiency in the DOD excess property system.

My testimony has two parts: First, the magnitude of waste and inefficiency, and, second, the root causes of these problems.

First, DOD reported that $29 billion of the $33 billion in excess commodity disposals for 2002 through 2004 were unusable items, or junk. By junk, I mean items that are in need of significant repair, obsolete, or that need to be destroyed. However, the remaining $4 billion related to items that were in new, unused and excellent condition, referred to by DOD as A condition. Of the $4 billion, we determined that $3½ billion was waste because A condition

items were given away, sold on the Internet for pennies on the dollar, or destroyed.

Part of the $3½ billion of waste is caused by a chronic DOD problem, buying more inventory than it needs. When this happens inventory items are warehoused until they are obsolete and ultimately declared excess. By the time these items get to the excess property system they are no longer in demand, and thus are basically worthless.

However, we also identified, as you mentioned, at least $400 million of new, unused inventory that was sold or given away at the same time DOD was buying the same items. By definition, new unused inventory that DOD is still buying is not excess to its needs. This is where the excess property system failed, which resulted in one part of DOD selling, giving away or destroying the very same items that were needed to support our military forces.

To illustrate this waste, GAO ordered several new items at little or new cost. Also, using our undercover credit card, we purchased other DOD items on the Internet from govliquidation.com. We have these items here today as the exhibits you see labeled and also on the table, and we will show some of those on the monitors as I walk through this.

The items that GAO ordered included a new medical instrument chest, which is on my left, two circuit cards, which are on my right, and two power supply units, also on my right. The power supply units are currently used in the electronic warfare system of the Seawolf fast attack nuclear submarine. The circuit cards are used in secure satellite communications gear by the Navy.

We also purchased on the Internet new extreme cold weather boots, tents, gasoline burner units, portable suction apparatus, bandages and medical supplies, badges and insignias, Cooper tires, and Class A military uniforms.

Let me spend a few minutes discussing the boots and the tents so I can bring these case studies to life for you. The boots were advertised on govliquidation.com as being 30 pair that were condemned. However, when we received our order, we found that our purchase included 42 pairs of boots of which 37 were in new, unused condition like the ones you see on my right. We paid about $12 per pair for these boots, while DOD paid $135 per pair. Shortly after our purchase we found that DOD had placed an order to purchase over 30,000 pair of the very same boots. In another case we found 172 pairs of boots were sold to the Robinson Trading Co. for 40 cents a pair.

We also purchased 27 tents on the Internet for $548 that DOD paid over $2,100 for. Although the tents were also advertised as being condemned, when we received our order we found that our purchase included 21 new, unused tents like the one at my left. At the same time we made our purchase, an order had been placed for 35,000 of these same tents at a cost of $2½ million. In total, we paid about $3,000 for the items that we obtained, DOD paid over $80,000 for these same items. All of the items displayed here today were still being purchased and were in demand by the military services.

Second, the causes of waste and inefficiency included unreliable data, inadequate management oversight and physical control, and outdated systems.

We found significant data reliability problems, including errors in quantity, description and condition of excess property items. Military units have lost confidence in the reliability of excess property data and thus purchase new items instead of using items that are in the excess property system.

With respect to automated systems, we found the lack of integration of purchasing systems and the excess property systems was a major issue. In effect, these systems do not share data that prevents the purchase of new items that DOD already has available in the excess property system.

Our related report included 13 recommendations to DOD related to people, processes and automated systems. DOD is taking actions to address all of our recommendations.

In conclusion, with the serious fiscal challenges facing our Nation and with our forces fighting the global war on terrorism, the government can't afford to be giving away inventory that it's buying at the same time. No doubt many of the businesses that profit from this hidden subsidy would like to see DOD continue selling new, unused items for pennies on the dollar. We believe improvements in management of the excess property system could save taxpayers hundreds of millions of dollars annually.

Mr. Chairman, this ends my statement. Mr. Rhodes, Special Agent Ryan, Ms. Fischer and I would be happy to answer your questions.

[NOTE.—The GAO report entitled, "DOD Excess Property, Management Control Breakdowns Result in Substantial Waste and Inefficiency," may be found in subcommittee files.]

[The prepared statement of Mr. Kutz follows:]

United States Government Accountability Office

GAO

Testimony

Before the Subcommittee on National Security, Emerging Threats and International Relations, Committee on Government Reform, House of Representatives

For Release on Delivery
Expected at 2:00 p.m.
Tuesday, June 7, 2005

DOD EXCESS PROPERTY

Management Control Breakdowns Result in Substantial Waste and Inefficiency

Statement of Gregory D. Kutz
Managing Director
Forensic Audits and Special Investigations

GAO-05-729T

June 7, 2005

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Highlights

Highlights of GAO-05-729T, a testimony before the Subcommittee on National Security, Emerging Threats and International Relations, Committee on Government Reform, House of Representatives

DOD EXCESS PROPERTY

Management Control Breakdowns Result in Substantial Waste and Inefficiency

Why GAO Did This Study

GAO was asked to assess the overall economy and efficiency of the Department of Defense (DOD) program for excess property reutilization (reuse). Specifically, GAO was asked to determine (1) whether and to what extent the program included waste and inefficiency and (2) root causes of any waste and inefficiency. GAO was also asked to provide detailed examples of waste and inefficiency and the related causes. GAO's methodology included an assessment of controls, analysis of DOD excess inventory data, statistical sampling at selected sites, and detailed case studies of many items.

What GAO Recommends

Today, GAO is issuing a report (GAO-05-277) with 13 recommendations to improve the economy and efficiency of DOD's reutilization program for excess commodities in the areas of (1) data reliability; (2) oversight, accountability, and physical inventory control; and (3) the functional design of DOD's future commodity inventory systems. In commenting on GAO's report, DOD concurred that actions are needed to improve the reutilization program and noted a number of improvement initiatives that were taken during fiscal years 2004 and 2005. However, DOD has not yet addressed the fundamental, conceptual weaknesses that have resulted in waste and inefficiency.

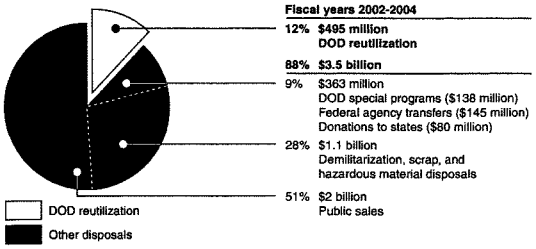
www.gao.gov/cgi-bin/getrpt?GAO-05-729T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Gregory D. Kutz (202) 512-9095 or Kutzg@gao.gov.

What GAO Found

DOD does not have management controls in place to assure that excess inventory is reutilized to the maximum extent possible. Of $33 billion in excess commodity disposals in fiscal years 2002 through 2004, $4 billion were reported to be in new, unused, and excellent condition. DOD units reutilized only $495 million (12 percent) of these items. The remaining $3.5 billion (88 percent) includes significant waste and inefficiency because new, unused, and excellent condition items were transferred and donated outside of DOD, sold for pennies on the dollar, or destroyed. DOD units continued to buy many of these same items. GAO identified at least $400 million of fiscal year 2002 and 2003 commodity purchases when identical new, unused, and excellent condition items were available for reutilization. GAO also identified hundreds of millions of dollars in reported lost, damaged, or stolen excess property, including sensitive military technology items, which contributed to reutilization program waste and inefficiency. Further, excess property improperly stored outdoors for several months was damaged by wind, rain, and hurricanes.

Waste and Inefficiency Related to $3.5 Billion in Fiscal Year 2002-2004 Disposals of Excess DOD Commodities Reported To Be in New, Unused, and Excellent Condition



Source: GAO analysis.

GAO ordered and purchased at little or no cost several new and unused excess commodities that DOD continued to buy and utilize, including tents, boots, power supplies, circuit cards, and medical supplies. GAO paid a total of $2,898, including tax and shipping cost, for these items, which had an original DOD acquisition cost of $79,649.

Root causes for reutilization program waste and inefficiency included (1) unreliable excess property inventory data; (2) inadequate oversight and physical inventory control; and (3) outdated, nonintegrated excess inventory and supply management systems. Procurement of inventory in excess of requirements also was a significant contributing factor. Improved management of DOD's excess property could save taxpayers at least hundreds of millions of dollars annually.

Mr. Chairman and Members of the Subcommittee:

Thank you for the opportunity to discuss the results of our audit and investigation of the economy and efficiency of the Department of Defense (DOD) program for reutilization (reuse) of excess property. Our related report,[1] released today and developed at the request of this Subcommittee, Senator Collins, and Representative Schakowsky, describes significant breakdowns in management controls that have resulted in substantial waste and inefficiency in DOD's excess property reutilization program. Our previous, limited work identified several examples of waste and inefficiency in DOD's excess property reutilization program. Our November 2003 report[2] identified several examples that showed that at the same time DOD excessed biological laboratory equipment items in good or excellent condition and sold many of them to the public for pennies on the dollar, it was purchasing the same or similar items. In June 2002, we testified[3] that the lack of asset visibility over the Joint Service Lightweight Integrated Suit Technology (JSLIST)[4] resulted in DOD selling new, unused JSLIST for $3 per suit (coats and trousers) while at the same time procuring hundreds of thousands of JSLIST annually at a cost of over $200 per suit. You were concerned that these limited examples could indicate systemic problems.

Our current work focused on whether and to what extent we found waste and inefficiency in DOD's excess property reutilization program and the root causes of any waste and inefficiency. You also asked us to determine whether the Defense Logistics Agency (DLA) was purchasing new items when identical items in new, unused, and excellent condition were available at Defense Reutilization and Marketing Service (DRMS) field

[1] GAO, *DOD Excess Property: Management Control Breakdowns Result in Substantial Waste and Inefficiency*, GAO-05-277 (Washington, D.C.: May 13, 2005).

[2] GAO, *DOD Excess Property: Risk Assessment Needed on Public Sales of Equipment That Could Be Used to Make Biological Agents*, GAO-04-15NI (Washington, D.C.: Nov. 19, 2003).

[3] GAO, *DOD Management: Examples of Inefficient and Ineffective Business Processes*, GAO-02-873T (Washington, D.C.: June 25, 2002).

[4] JSLIST is a universal, lightweight, two-piece garment (coat and trousers) that when combined with footwear, gloves, and protective mask and breathing device, forms the warfighter's protective ensemble. Together, the ensemble is to provide maximum protection to the warfighter against chemical and biological contaminants without negatively impacting the ability to perform mission tasks. JSLIST is the current model protective suit used by the military forces.

offices (DRMO). As DOD's combat support agency, DLA has a mission to provide best-value logistics support to America's armed forces. In carrying out its mission, DLA manages inventory valued at about $83 billion, consisting of more than 5 million items of food, fuel, clothing and other textiles, medical supplies, industrial use items, and spare and repair parts supporting over 1,400 weapon systems. Within DLA, DRMS is responsible for excess property disposals. Federal regulations[5] require executive agencies to ensure that personal property not needed by their activity is offered for use elsewhere within the agency. In accordance with federal regulations, DOD 4160.21-M, *Defense Materiel Disposition Manual*, chapter 5, calls for reutilization of excess property to the extent feasible to fill existing needs and to satisfy additional needs before initiating new procurement or repair.

In performing our work, we reviewed applicable laws and regulations; DOD policies and procedures; and current and planned systems, processes, and management controls. To identify potential waste and inefficiencies, we analyzed the universe of recorded commodity purchase and disposal transactions and compared DOD commodity purchases to disposals of identical items in new, unused, and excellent condition (A condition). To assure ourselves that DOD data were sufficiently reliable for the purpose of our work, we performed a number of electronic and statistical tests of DOD databases and excess inventory and data used in our work. We conducted our work, including follow-up work related to this testimony, from November 2003 through May 2005 in accordance with U.S. generally accepted government auditing standards and investigative standards prescribed by the President's Council on Integrity and Efficiency. We obtained DOD comments on a draft of our report, and we briefed DOD officials on new findings included in this testimony.

Today, my testimony will focus on (1) summarizing the results of our audit and updating our analysis for fiscal year 2004 excess commodity disposal activity; (2) describing additional case study acquisitions of new, unused excess DOD commodity items from December 2004 through April 2005; and (3) discussing management control breakdowns that contributed to reutilization program waste and inefficiency and the results of our investigations of selected excess property losses noted in our audit report.

[5] *Federal Management Regulation*, 41 C.F.R. ch. 102 (2004).

Summary

DOD does not have effective management processes, systems, and controls in place to assure that it is reutilizing excess inventory to the maximum extent possible and safeguarding excess items from damage, loss, and theft, as required by federal regulations, DOD policy, and GAO internal control standards.[6] Our analysis of DRMS excess commodity disposal activity identified substantial waste and inefficiency related to DOD's excess property reutilization program. For example, of the $33 billion in reported excess commodity disposals in fiscal years 2002 through 2004, $4 billion related to items in new, unused, and excellent condition. Of the $4 billion, we determined that $3.5 billion (88 percent) included substantial waste and inefficiency because new, unused, and excellent condition items were being transferred or donated outside of DOD, sold on the Internet for pennies on the dollar, or destroyed rather than being reutilized. As discussed in our report,[7] our analysis of fiscal year 2002 and 2003 data on commodity purchases and disposal activity found that DOD purchased at least $400 million of identical commodities instead of reutilizing available A-condition excess items. Further, the extent of reutilization waste and inefficiency may be greater due to incomplete and inaccurate data that are key to identifying excess items for reutilization. In addition, the DRMS reported $466 million in excess property losses from fiscal years 2002 through 2004, such as missing, damaged, and stolen property, adding to reutilization program waste.

Our monitoring of DRMS disposal activity found continuing reutilization program waste and inefficiency. We ordered several excess DOD items at little or no cost and purchased other items at minimal cost. Overall, we paid $2,898 for items with a listed acquisition cost of $79,649. For example,

- As discussed in our report, from May through October 2004, we ordered and purchased at little or no cost several new and unused excess commodity items that DOD continued to buy and utilize, including tents; boots; power supplies; circuit cards; gasoline burners; and a medical instrument chest, suction device, and medical supplies and bandages.

[6] *Federal Property Management Regulations*, 41 C.F.R. ch. 101 (2004) and the *Federal Management Regulation*, 41 C.F.R. ch. 102 (2004), issued by the General Services Administration; DOD 4160.21-M, *Defense Materiel Disposition Manual*; and GAO, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).

[7] GAO-05-277.

We paid a total of $1,471, including tax, buyer's premium, and shipping cost, for these items, which had an original DOD acquisition cost of $68,127.

- In addition, from December 2004 through April 2005, we purchased over the Internet several additional new, unused excess commodity items that DOD units are continuing to purchase and utilize. These items included military badges, medals, and insignias; Cooper Trendsetter SE automobile tires; and military dress uniforms. Although these items had an original DOD acquisition cost of $11,522, we paid a total of $1,427 for them, including tax, buyer's premium, and shipping cost.

Our analysis, statistical tests of excess inventory accuracy, case studies, and interviews showed that the root causes for the billions of dollars in waste and inefficiency related to management control breakdowns across DOD, including weaknesses in DOD's excess property reutilization program, stemmed from

- unreliable excess property inventory data;
- inadequate oversight, accountability, and physical control of excess property; and
- inadequate processes and outdated, nonintegrated inventory systems that do not provide adequate visibility of excess property available for reutilization at the time military units order and purchase commodity items.

In addition, as we have reported for many years,[8] long-standing DOD logistics management weaknesses that resulted in purchases that exceeded actual requirements resulted in the disposal of unused items due to obsolescence and contributed indirectly to reutilization program waste and inefficiency. Further, DOD reutilization program waste and inefficiency is symptomatic of the inventory and supply chain management issues that have been considered high risk by GAO since 1990.

[8] GAO, *Defense Inventory: Analysis of Consumption of Inventory Exceeding Current Operating Requirements Since September 30, 2001*, GAO-04-689 (Washington, D.C.: Aug. 2, 2004), and *Major Management Challenges and Program Risks: Department of Defense*, GAO-03-98 (Washington, D.C.: January 2003).

Our investigations of selected reports of losses of excess DOD commodity items identified a pervasive lack of physical accountability over excess inventory, which leaves DOD vulnerable to the risk of theft and fraud, waste, and abuse. The lack of accountability makes it impossible to complete an investigation. Specifically, the failure to verify and accurately document transactions and events at the beginning of the disposal process and report and investigate losses when they occur obscures or eliminates the audit trail. Because DRMO personnel did not always verify turn-in documentation at the time they received excess items and recorded them in excess inventory, in many cases it is not possible to determine whether discrepancies represent sloppy recordkeeping, the loss or theft of excess property, or where or when the loss or theft occurred. This lack of accountability encourages theft and fraud because there is little likelihood of detection.

We found that DRMS investigative reports are generally inconclusive with regard to the causes of the lost property. For example, the investigative reports on the loss of 75 chemical and biological protective suits at the Jackson DRMO and 20 units of body armor at the Meade DRMO each stated that the items were recorded in inventory, placed in the DRMO warehouse, and subsequently disappeared. According to the investigative reports, no determination was made as to what happened to these items. Our follow-up investigations on DLA supply depot reports of missing aircraft parts at two DLA depots found that depot personnel did not aggressively research events related to the missing items because they assumed that the missing items related to recordkeeping errors, such as the failure to record inventory issues.

In commenting on the recommendations in our audit report, DOD concurred that actions are needed to improve the reutilization program and noted a number of improvement initiatives that were taken during fiscal year 2004 and early in fiscal year 2005. While these actions have made some marginal improvements in the reutilization program, DOD has not yet addressed the fundamental, conceptual weaknesses that have resulted in substantial waste and inefficiency in the excess property reutilization program.

Analysis of Reutilization Program Identifies Billions of Dollars in Waste and Inefficiency

Overall, our analysis of the $33 billion in reported excess commodity disposals in fiscal years 2002 through 2004 showed that $4 billion related to items in new, unused, and excellent condition. Of the $4 billion, we determined that $3.5 billion (88 percent) included substantial waste and inefficiency because new, unused, and excellent condition items were being transferred or donated outside of DOD, sold on the Internet for pennies on the dollar, or destroyed rather than being reutilized. As discussed in our report, our analysis of $18.6 billion[9] in fiscal year 2002 and 2003 excess commodity disposal activity identified $2.5 billion in excess items that were reported to be in new, unused, and excellent condition (A condition). Although federal regulations and DOD policy require reutilization of excess property in good condition, to the extent possible, our analysis showed that DOD units only reutilized $295 million (12 percent) of these items. The remaining $2.2 billion (88 percent) of the $2.5 billion in disposals of A-condition excess commodities were not reutilized, but instead were transferred, donated, sold, or destroyed. Similarly, our analysis of $14.3 billion in fiscal year 2004 disposal activity identified $1.5 billion in excess commodity items that were reported to be in A condition. Of the $1.5 billion in A-condition excess items, DOD units reutilized $200 million (13 percent) and transferred, donated, sold, or destroyed the remaining $1.3 billion (87 percent). We also found that during fiscal years 2002 and 2003, DOD purchased at least $400 million (over $200 million each year) of identical items instead of reutilizing available excess items in A condition. To illustrate continuing reutilization program waste and inefficiency, we purchased several new and unused excess DOD commodity items that were being purchased by DLA, were currently in use by the military services, or both. Our analysis of transaction data and our tests of controls for inventory accuracy indicate that the magnitude of waste and inefficiency could be much greater due to military units improperly downgrading condition codes of excess items that are in new, unused, and excellent condition to unserviceable and the failure to consistently record national stock numbers (NSN)[10] needed to identify like items.

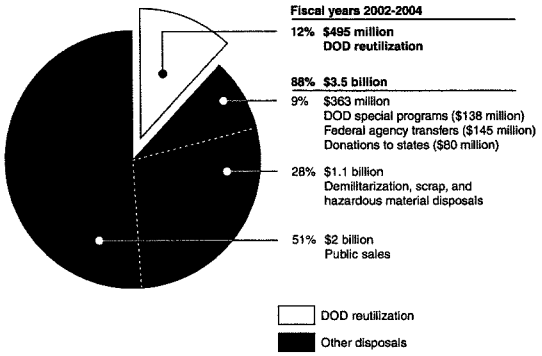
[9] The reported acquisition value at the time the items were turned in as excess.

[10] An NSN is a 13-digit number that identifies standard use inventory items. The first 4 digits of the NSN represent the Federal Supply Classification, such as 8430 for men's footwear, followed by a 2-digit North Atlantic Treaty Organization (NATO) code (to indicate user countries) and a 7-digit designation for a specific item, such as a cold weather boot.

Fiscal Year 2002-2004 Excess Commodity Disposal Activity

DRMS is responsible for disposing of unusable items, often referred to as "junk," as well as facilitating the reutilization of usable items. Although the majority of DOD's excess property disposals relate to items in unserviceable condition, DOD also disposed of billions of dollars of serviceable items, including excess commodities in A condition from fiscal years 2002 through 2004. Our analysis of DRMS data showed that $28.1 billion of the $33 billion in excess DOD commodity disposals from fiscal year 2002 through fiscal year 2004 consisted of items listed in unserviceable condition, including items needing repair, items that were obsolete, and items that were downgraded to scrap. The remaining $4.9 billion in excess commodity disposals consisted of items reported to be in serviceable condition, including $4 billion in excess commodities reported to be in A condition. However, of the $4 billion, DOD units reutilized only $495 million (12 percent) of these items during the 3-year period. The data reliability issues noted above and our interviews, case studies, and statistical sample results indicate that the magnitude of waste and inefficiency associated with disposals of A-condition items could be much greater. As shown in figure 1, items that were not reutilized by DOD were transferred to federal agencies or special programs, donated to states, sold to the public, or destroyed by demilitarization or through scrap and hazardous materials contractors.

Figure 1: Waste and Inefficiency in Fiscal Year 2002 through Fiscal Year 2004 Disposals of Excess DOD Commodities Reported To Be in New, Unused, and Excellent Condition



Source: GAO analysis.

We found that the percentage of DOD reutilization of excess property was higher in fiscal year 2002 than in fiscal years 2003 and 2004. According to DRMO officials, reutilization was higher in fiscal year 2002 because excess items were pulled back to support deployment to Afghanistan and Iraq. In fiscal year 2003, procurement to support the war on terrorism began to keep up with the demand for supplies, and reutilization of excess property decreased. DRMS officials attribute the fiscal year 2004 increase in DOD reutilization to the establishment of the Joint Services Nuclear, Biological, and Chemical Equipment Assessment Program (JEAP) to inspect excess military clothing, tents, and other textile items and reissue items in good condition. The increase in disposal activity in fiscal years 2003 and 2004 relates to turn-ins of property used in support of Operation Enduring Freedom and Operation Iraqi Freedom. Table 1 shows disposal activity related to A-condition excess commodities for fiscal years 2002 through 2004.

Table 1: Fiscal Year 2002 through 2004 Disposals of Excess DOD Commodities in New, Unused, and Excellent Condition

Dollars in millions

Disposal method	Fiscal year 2002	Fiscal year 2003	Fiscal year 2004	Total
DOD reutilization	$145 (14%)	$150 (10%)	$200 (13%)	**$495 (12%)**
Special programs	45	46	47	**138**
Federal agency transfers	58	45	42	**145**
Donations to states	28	26	26	**80**
Subtotal, special programs, transfers, and donations	**$131 (12%)**	**$117 (8%)**	**$115 (8%)**	**$363 (9%)**
Demilitarization, scrap, and hazardous material disposals	$102 (10%)	$532 (37%)	$480 (32%)	**$1,114 (28%)**
Public sales	$672 (64%)	$645 (45%)	$703 (47%)	**$2,020 (51%)**
Total disposals	**$1,050 (100%)**	**$1,444 (100%)**	**$1,498 (100%)**	**$3,992 (100%)**

Source: GAO analysis.

Unnecessary Commodity Purchases

Our analysis of fiscal year 2002 and 2003 DLA commodity purchases and DRMS excess property inventory data identified numerous instances in which the military services ordered and purchased items from DLA at the same time identical items—items with the same NSN—that were reported to be in new, unused, and excellent condition were available for reutilization. We found that DOD purchased at least $400 million of identical items during fiscal years 2002 and 2003—over $200 million each year—instead of using available excess A-condition items. The magnitude of unnecessary purchases could be much greater because NSNs needed to identify identical items were not recorded for all purchase and turn-in transactions. For example, we determined that DLA buyers and item managers did not record NSNs for 87 percent (about $4.9 billion) of the nearly $5.7 billion in medical commodity purchases by military units during fiscal years 2002 and 2003. Further, as discussed later, improper downgrading of condition codes to unserviceable could also result in an understatement of the magnitude of unnecessary purchases. While our statistical tests found a few instances of inaccurate serviceable condition codes, most condition code errors related to the improper downgrading of condition to unserviceable.

Fiscal Year 2004 and 2005 Requisitions and Purchases Demonstrate Continuing Waste and Inefficiency

To determine whether the problems identified in our analysis were continuing, we monitored DRMS commodity disposal activity from May 2004 through April 2005. We found that DOD continued to transfer, donate, and sell excess A-condition items instead of reutilizing them. To illustrate these problems, we requisitioned several excess new and unused items at no cost and purchased other new and unused commodities at minimal cost. We based our case study selections on new, unused items that DOD continued to purchase. As discussed in our report,[11] we used the GSA Federal Disposal System, available to all federal agencies, to requisition several new and unused excess DOD commodity items during our audit in fiscal year 2004 and the first half of fiscal year 2005, including a medical instrument chest, two power supply units, and two circuit cards, at no charge. These items had an original DOD acquisition cost of $55,817, and we paid only $5 shipping cost to obtain all of them. We also purchased, at minimal cost, several excess DOD commodity items in new and unused condition over the Internet at govliquidation.com—the DRMS liquidation contractor's Web site.[12] The items we purchased included tents, boots, three gasoline burners (stove/heating unit), a medical suction apparatus, and bandages and other medical supply items with a total reported acquisition cost of $12,310. We paid a total of $1,466 for these items, about 12 cents on the dollar, including buyer's premium, tax, and shipping cost.

From December 2004 through April 2005, we purchased several new, unused excess DOD commodity items, including over 8,000 military badges, medals, and insignias; 8 new, unused Cooper Trendsetter SE tires; and Class A military uniforms. Although these items had a total reported acquisition cost of $11,522, we paid a total of $1,427 for these items, including tax, buyer's premium, and shipping cost.

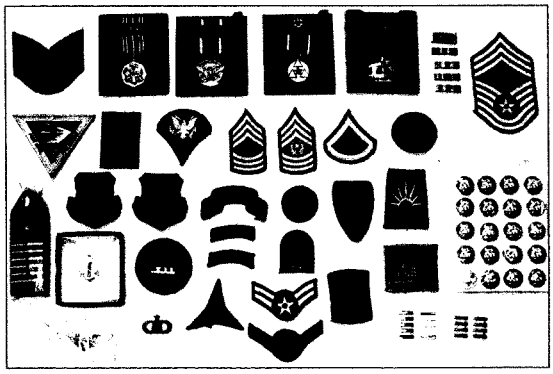
New, unused DOD badges, medals, and insignias. On December 6, 2004, we purchased 8,526 excess DOD badges, medals, and insignias that are used to indicate rank, the unit or program to which a military member or civilian employee is assigned, or service awards. These items had a reported acquisition cost of $9,518. We paid a total of $1,102, including buyer's premium and tax, for these items—about 12 cents on the dollar. Units and program areas designated by the badges and insignias include

[11] GAO-05-277.

[12] Government Liquidation, LLC is the DRMS commercial venture partner (contractor) for public sales of excess DOD property.

Army Rangers, Mountain, and Airborne; Air Force Air Traffic Controller; and DOD Scientific Consultant. Rank insignias include Air Force Chief Master Sergeant and Air Force Technical Sergeant; Navy Captain, Midshipman Lieutenant, and Midshipman Lieutenant Commander; and Army Command Sergeant Major and Master Sergeant. The listed condition code of these items ranged from A4 (serviceable, usable condition) to H7 (unserviceable, condemned condition). However, our inspection of the badges and insignias that we purchased showed that none of them had been used, and many of them were in original manufacturer packages. Further, DOD is continuing to purchase and use most of these items. The photograph in figure 2 shows examples of some of the badges, medals, and insignias that we purchased.

Figure 2: Examples of Excess DOD Badges, Medals, and Insignias Purchased over the Internet in December 2004

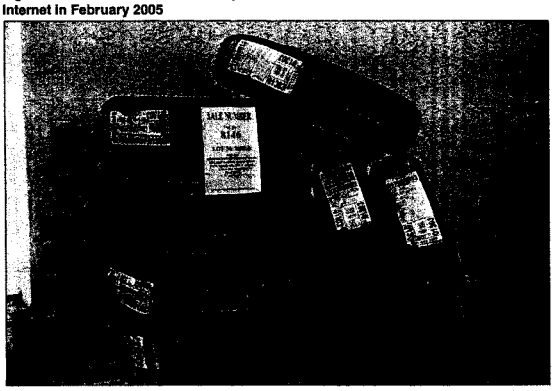


Source: GAO.

New, unused excess DOD tires. We purchased eight new, unused Cooper Trendsetter SE 13-inch steel-belted radial tires on February 18, 2005. According to the Army project officer, these tires are used on over-the-road passenger vehicles, and one customer ordered them for use on a

forklift. DOD units are continuing to purchase and use these same tires. The most recent purchase of 50 of these tires was made in April 2005. The eight tires had a total reported acquisition value of $404. We paid $113 for the tires, including buyer's premium and tax, and an additional $154 shipping cost. The tires were listed in A4 condition (usable, with some wear). However, we found that the tires still had manufacturer labels on the tread and blue paint over the whitewalls, indicating that they were new and unused. The tires were turned in as excess by the North Island Naval Air Station's Aircraft Intermediate Maintenance Detachment. According to the Army Tank Automotive and Armaments Command Project Officer,[13] the NSN listed on the turn-in document was incorrect. We found that inaccurate item descriptions, including NSNs, prevent items from being selected for reutilization. Figure 3 is a photograph of the excess DOD tires that we purchased over the Internet in February 2005.

Figure 3: New, Unused Excess Cooper Trendsetter SE Tires Purchased over the Internet in February 2005

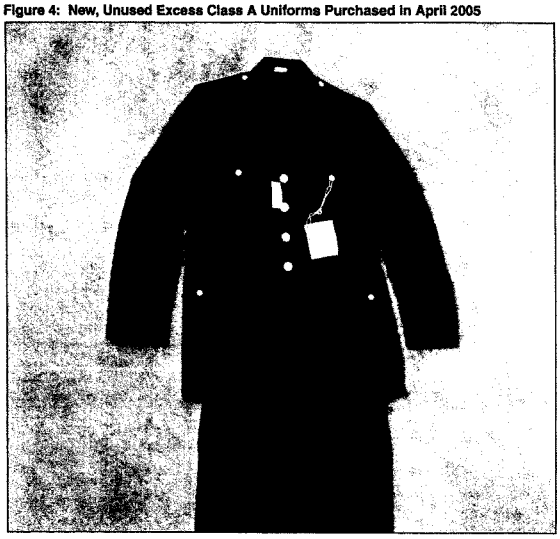


Source: GAO.

[13] The Army has product management responsibility for these tires.

New, unused Class A military uniforms. We purchased several Class A military uniforms over the Internet on April 7, 2005. The uniforms were listed as being in H7 (unserviceable, condemned) condition. Although the uniforms that we purchased over the Internet from DOD's liquidation contractor had a listed acquisition cost of $1,600, we paid a total of $58, including buyer's premium and sales tax, to acquire them—about 4 cents on the dollar. After receiving our purchase we determined that we had in fact purchased 27 new, unused uniform coats; 4 pairs of new, unused uniform trousers; 54 jackets in excellent condition; 45 pairs of trousers in excellent condition; and 5 women's uniform skirts and 1 pair of slacks in excellent condition. DOD is continuing to purchase and issue two of the four types of trousers that we purchased over the Internet. According to the DLA clothing and textiles product manager for dress uniforms, the Army switched from a matte finish gold button to a shiny sta-brite™ gold button on October 1, 2003. Although the Army ordered and paid for the new replacement buttons for existing dress uniforms, it later determined that hiring a contractor to replace the buttons or sending the coats back to the manufacturers for button replacement would be very expensive. The Army decided to use the coats with the older buttons to fill Reserve and Junior Reserve Officer Training Corps (ROTC and JROTC) orders until current supplies are exhausted. However, our monitoring of DOD liquidation sales found that many class A uniforms with the older buttons are being sold over the Internet for pennies on the dollar instead of being issued to ROTC and JROTC. In addition, we observed the new sta-brite™ buttons being sold over the Internet in May 2005. Figure 4 is a photograph of one of the excess new, unused Class A uniforms with the matte finish buttons that we purchased over the Internet in April 2005.

Figure 4: New, Unused Excess Class A Uniforms Purchased in April 2005



Source: GAO.

We also purchased an earlier sales lot of the same Class A military uniforms over the Internet on February 16, 2005. Our winning bid was $81 for 166 uniform jackets and trousers, which had a listed acquisition cost of $10,424. However, when we arrived at the Great Lakes sales location near Chicago to pick up the uniforms, DOD liquidation contractor personnel were unable to locate them. Contractor personnel explained that our purchase may have been mistakenly given to another customer. To compensate, we were offered other items available for sale. However, these items were not in A condition. Instead of accepting them, we requested and received a refund. As discussed later, another of our Internet purchases was damaged due to a leaky roof at the Norfolk liquidation sales location.

Management Control Breakdowns Resulted in Reutilization Program Waste and Inefficiency

The $3.5 billion in DOD waste and inefficiency that we identified in our analysis of fiscal year 2002 through 2004 excess property disposal activity stemmed from management control breakdowns across DOD. Key factors in the overall DRMS management control environment that contributed to waste and inefficiency in the reutilization program included (1) unreliable excess property inventory data; (2) inadequate DRMS oversight, accountability, physical control, and safeguarding of property; and (3) outdated, nonintegrated excess inventory and supply systems. In addition, for many years our audits of DOD inventory management[14] have reported that continuing unresolved logistics management weaknesses have resulted in DOD purchasing more inventory than it needed. DOD reutilization program waste and inefficiency is symptomatic of the inventory and supply chain management issues that have been considered high risk by GAO since 1990. Our analysis of fiscal year 2002 through fiscal year 2003 excess commodity turn-ins showed that $1.4 billion (40 percent) of the $3.5 billion of A-condition excess items consisted of new, unused DLA supply depot inventory. Our analysis of fiscal year 2004 excess commodity turn-ins showed that $1.3 billion (48 percent) of the $2.7 billion of A-condition excess items consisted of new, unused DLA supply depot inventory.

Unreliable Data Impair the Economy and Efficiency of the Reutilization Program

Our interviews, case studies, screening visits, and statistical tests of excess commodity inventory led us to conclude that unreliable data are a key cause of the ineffective excess property reutilization program. GAO's internal control standards[15] require assets to be periodically verified to control records. In addition, DRMS policy[16] requires DRMO personnel to verify turn-in information, including item description, quantity, condition code, and demilitarization code, at the time excess property is received and entered into DRMO inventory. However, we found that DRMS and DLA supply depot management have not enforced this requirement. Further, Army, Navy, and Air Force officials told us that unreliable data are a disincentive to reutilization because of the negative impact on their

[14] GAO-04-689 and GAO-03-98.

[15] GAO, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).

[16] DRMS-I 4160.14, vol. II, *Instructions for Warehousing for DRMS and the Defense Reutilization and Marketing Offices*, ch. 2, "Receipt and Storage," § 1 (A) (9).

operations. DLA item managers told us that because military units have lost confidence in the reliability of data on excess property reported by DRMS, for the most part they have requested purchases of new items instead of reutilizing excess items. Military users also cited examples of damage to excess items during shipment that rendered the items unusable. In addition, other reutilization users advised us of problems related to differences in quantities and the types of items ordered and received that could have a negative impact on their operations.

Problems with Excess Inventory Items Noted by Military Services and Other Users

Military service officials also told us about the types of problems they have experienced with property acquired from DRMOs. Army, Navy, and Air Force medical officials, in particular, told us that they do not reutilize excess medical items stored at DRMOs because items can become damaged during shipment to and movement within the DRMO warehouses. Other users of excess DOD property, including special program, federal agency, and state officials gave us numerous examples of problems they encountered with requisitions of excess DOD property. Several officials noted that these problems have caused them to lose confidence in the reutilization process. The following examples are typical of what we were told.

- An Army official told us that he requisitioned 20 excess padlock sets. When he received the padlocks the keys were missing. After his second attempt to requisition excess DOD padlocks with keys failed, he threw the padlocks in a dumpster because they were useless to him and it would cost too much to return them to the DRMO.

- An Army official told us that items may be in new, unused condition when they leave the DRMO, but are damaged during shipment. The official cited his experience with an order of thin copper sheets for use in testing electronic equipment. The sheeting was shipped on a pallet that was too small and other material was stacked on top of it.

- A Fairchild Air Force Base official told us that the 92nd Logistics Readiness Squadron requisitioned 80 sleeping bags from the Hawaii DRMO but only received 56 of them. The official told our investigators that the sleeping bags were sealed in heavy-duty plastic bags and were in excellent condition. However, some of the boxes the sleeping bags were shipped in had been damaged by rain and handling by the time he received them.

Statistical Samples Identified Problems with Excess Inventory Accuracy

Our statistical tests found significant problems with controls for assuring the accuracy of excess property inventory. Estimated error rates for the five DRMOs we tested ranged from 8 percent at one DRMO to 47 percent at another,[17] and estimated error rates for the five DLA supply depots we tested ranged from 6 percent to 16 percent,[18] including errors related to physical existence of turn-ins and condition code.[19] Our condition code tests determined whether the condition code was accurately recorded as serviceable or unserviceable. We estimated that errors related to condition code accuracy ranged from 6 percent to 26 percent at the 5 DRMOs we tested.[20] Overall, we found that DRMO errors were caused by erroneous turn-in documentation prepared by military units and the failure of DRMO personnel to verify turn-ins at the time they were received and correct errors before recording the receipts in excess inventory. Most DLA supply depot errors related to untimely recording of transactions for changes in inventory status and inaccurate quantities. We did not find problems with condition codes at the DLA depots.

An example from our Norfolk DRMO statistical sample illustrates how erroneous inventory data can result in waste and inefficiency. On June 30, 2004, the Navy's Environmental Health Center in Portsmouth, Virginia, turned in six new, unused Level III biological safety cabinets[21] with a total acquisition cost of $120,000. The Navy unit turned in the Level III cabinets as excess because of erroneous specifications that resulted in ordering cabinets that were too large and cumbersome to meet deployment needs.

[17] Sampling errors for our DRMO estimates did not exceed 10 percentage points at the 95-percent confidence level.

[18] Sampling errors for our DLA supply depot estimates did not exceed 7 percentage points at the 95-percent confidence level.

[19] Our physical existence tests included whether turn-ins recorded in inventory could be located, whether inventory changes were recorded within 7 days, and the accuracy of item descriptions (including item name(s) and NSN(s)) and quantities. Although some transactions included more than one type of error, we only counted one failure for a transaction.

[20] Sampling errors for our DRMO estimates did not exceed 11 percentage points at the 95-percent confidence level.

[21] The technical name for these safety cabinets is closed loop containment isolators.

The Navy unit improperly used a local stock number (LSN)[22] to describe the safety cabinets on the turn-in document and a demilitarization code that indicated there were no restrictions on the disposal of these items. However, Level III safety cabinets are subject to trade security controls,[23] and therefore they are required to be identified by an NSN or other information that accurately describes the item, the end item application, and the applicable demilitarization code.[24] Further, the DOD risk assessment performed in response to a recommendation in our November 2003 report[25] called for Level III biological safety cabinets to be destroyed when no longer needed by DOD. Although Norfolk DRMO personnel advised DRMS officials of the need to correct the turn-in document errors in July 2004, as of the end of our audit in February 2005, the information had not been corrected and the safety cabinets had not been posted to the DRMS reutilization Web page to indicate that they were available for reutilization.

Our in-house scientists who often meet with DOD scientists at the U.S. Army Biological Warfare Research Center at the Dugway Proving Ground learned that the DOD scientists were planning to purchase a Level III safety cabinet and informed them of the availability of the six Level III safety cabinets at the Norfolk DRMO. The DOD scientists told us that they were unaware the Navy had excessed the safety cabinets and said that they could use all six of them. We subsequently confirmed that as a result of our efforts, the DOD scientists at Dugway had requisitioned the six Level III safety cabinets for reutilization.

[22] An LSN consists of the four-digit federal supply classification number, a two-digit NATO code (user country code), and up to a seven-character description, such as "monitor" for a computer monitor and "boots" for cold weather boots.

[23] Commerce Control List, 15 C.F.R. pt. 774, supp. 1, category 2, Materials Processing, para. f (2), Protective and Containment Equipment (2005).

[24] DOD 4160.21-M-1, *Defense Demilitarization Manual*, ch.1, § D (6), and app. 5 (B), and DRMS-I 4160.14, vol. VII, ch. 3, "MLI/CCLI – Disposal Processing and Demilitarization," para. A (2)(d).

[25] GAO-04-15NI.

Weaknesses in Reutilization Program Oversight and Physical Inventory Control

We found hundreds of millions of dollars in potential waste and inefficiency associated with the failure to safeguard excess property inventory from loss, theft, and damage. As previously discussed, our statistical tests of excess commodity inventory at five DRMOs and five DLA supply depots identified significant numbers of missing items. Because the DRMOs and DLA supply depots had no documentation to show that these items had been requisitioned or sent to disposal contractors, they cannot assure that these items have not been stolen. According to DRMS data, DRMOs and DLA supply depots reported a total of $466 million in excess property losses related to damage, missing items, theft, and unverified adjustments over a period of 3 years. However, as discussed below, we have indications that this number is not complete. Also, because nearly half of the missing items reported involved military and commercial technology that required control to prevent release to unauthorized parties, the types of missing items were often more significant than the number and dollar value of missing items.

`xcess Property Losses

Weaknesses in accountability that resulted in lost and stolen property contributed to waste and inefficiency in the excess property reutilization program. As shown in table 2, our analysis of reported information on excess property losses at DRMOs and DLA supply depots found that reported losses for fiscal years 2002 through 2004 totaled $466 million. Because 43 percent of the reported losses related to military technology items that required demilitarization controls,[26] these weaknesses also reflect security risks. GAO *Standards for Internal Control in the Federal Government*[27] require agencies to establish physical control to secure and safeguard assets, including inventories and equipment, which might be vulnerable to risk of loss or unauthorized use. Our investigations of reported losses found that the failure to verify and accurately document transactions and events at the beginning of the disposal process and report and investigate losses as they occur obscures or eliminates the audit trail. Weaknesses in accountability leave DOD vulnerable to the risk of theft, and fraud, waste, and abuse with little risk of detection.

[26] DOD 4160.21-M-1, *Defense Demilitarization Manual*, ch. 1.

[27] GAO/AIMD-00-21.3.1.

Table 2: Reported DRMS Excess Property Losses and Adjustments

Dollars in millions

Location	Fiscal year 2002	Fiscal year 2003	Fiscal year 2004	Total
DRMOs	$81	$47	$62	**$190**
DLA supply depots	67	95	114	**276**
Total	**$148**	**$142**	**$176**	**$466**

Source: Unaudited DRMS data.

DRMO losses. Our statistical samples identified missing turn-ins at two of the five DRMOs we tested and missing quantities at all five DRMOs tested, including many items that were in new, unused, and excellent condition. Because DRMO officials did not have documentation to show whether these items had been reutilized, transferred, sold, or destroyed, there is no assurance of whether the missing items reflected bookkeeping errors or if they related to theft. Missing items in our statistical samples included turn-ins of 72 chemical and biological protective suits, 21 pairs of chemical and biological protective gloves, 47 wet weather parkas that were subject to demilitarization controls, and 7 sleeping bags, a cold weather coat, computer equipment, and various other items. Reported DRMO losses included 76 units of body armor, 75 chemical and biological protective suits (in addition to those identified in our Columbus DRMO sample),[28] 5 guided missile warheads,[29] and hundreds of military cold weather parkas and trousers and camouflage coats and trousers. Three DRMOs—Kaiserslautern, Meade, and Tobyhanna—accounted for $840,147, or about 45 percent, of the nearly $1.9 million in reported fiscal year 2004 losses of military clothing and equipment items requiring demilitarization.

Our follow-up investigations found a pervasive lack of physical accountability over excess inventory, which leaves DOD vulnerable to the risk of theft and fraud, waste, and abuse. In many cases, it is not possible to determine whether discrepancies represent sloppy recordkeeping or the

[28] The missing chemical and biological protective suits are not the current JSLIST, and the missing body armor is not the ceramic technology currently in use by deployed troops.

[29] In accordance with DOD 4160.21-M, ch. 4, "Property Requiring Special Processing," § B, and DRMS-I 4160.14, vol. VII, "Instructions for Demilitarization for DRMS and the Defense Reutilization and Marketing Offices," ch. 1, para. G, such items are required to be inert before turn-in to a DRMO.

loss or theft of excess property due to the failure to verify turn-in documents and correct errors at the time excess items were received at the DRMOs.

In the case of our Columbus DRMO sample, we found that inventory records were not adjusted for missing quantities in our sample. Instead, DRMO personnel recorded the entire amount of the listed quantities as being transferred to either the liquidation sales contractor or the Joint Service Nuclear Biological and Chemical Equipment Assessment Program (JEAP) for inspection and reissue of military clothing and equipment. Our review of transaction data for Columbus DRMO transfers showed that JEAP did not confirm most of the items reported as transferred. For example, JEAP confirmed receiving only 7 of the 17 turn-ins of clothing and textile items. Further, the Columbus DRMO recorded a transaction to show that the 72 chemical and biological protective suits identified as missing during our statistical tests of Columbus DRMO inventory were transferred to JEAP on November 10, 2004. However, our follow-up with JEAP officials found that they have no record of receiving the protective suits. The Columbus DRMO's apparent manipulation of the inventory data avoided reporting the missing items as losses.

Our follow-up investigations of other selected DRMO losses found the following.

- An Air Force turn-in of 75 chemical and biological protective suits was received, placed in the Shaw RIPL (a receipt in place location under authority of the Jackson DRMO) warehouse on May 28, 2002, and subsequently disappeared. DRMO personnel told DRMS investigators that the 75 protective suits may have been included in a November 15, 2002, shipment to the Jackson DRMO in South Carolina. However, because DRMO personnel recorded box counts instead of turn-in document numbers and item counts, there is no detailed record of the items that were shipped between the two excess property warehouses.

- Twenty units of body armor reported lost at the Meade DRMO initially had been ordered by Israel on November 8, 2000. Our investigators confirmed that the body armor was never picked up for shipment to Israel. According to the loss report, the items were relocated from the shipping area to the demilitarization storage area of the DRMO on May 8, 2002. A loss investigation was initiated by the Area Manager for the Meade DRMO in March 2004. However, because the Meade DRMO

contractor had improperly destroyed inventory records after 2 years, attempts to determine the events surrounding the loss were fruitless.

- Our investigation of 18 reports on a total of 52 units of body armor missing from the Hood DRMO during fiscal years 2002 and 2003 determined that these items were stored outside in an unsecure area resulting in the theft of at least 48 units of body armor. A DRMS investigative report noted that items requiring demilitarization had been stored in this area over a 2-year period, even though the security fence had barbed wire that was cut or missing and the high ground level outside the fence provided easy access. According to a DRMO official, a work order for the fence repair had been submitted but the repairs had not been made.

- The Naval Operational Logistics Support Center-Ammo, which was responsible for a turn-in of guided missile warheads, the DRMO that received these items, and the Demilitarization Center each recorded a different quantity for the turn-in. However, quantity discrepancies were not resolved at any point during the turn-in and disposal process. As a result, there is no audit trail to determine whether or where, when, or how the reported loss or a recordkeeping error occurred. For example, the Navy unit reported a turn-in of 24 warheads that had been used in testing but were certified as inert. DRMO personnel counted canisters and loose components and determined there were 32 warheads. The Anniston Demilitarization Center reported that a total of 27 warheads were received for destruction.

DLA supply depot losses. Our statistical samples showed missing items at four of the five DLA supply depots that we tested. Because depot officials did not have documentation showing that these items had been reutilized or sold, there is no assurance that the missing items did not relate to theft. Missing items in our DLA depot statistical samples included several sensitive items, such as classified radio frequency amplifiers and circuit boards, aircraft parts, and computer equipment that required trade security or demilitarization controls.

We obtained DRMS data on DLA supply depot reports of excess property losses, including missing and damaged property and unverified adjustments. We investigated reported losses of selected aircraft parts at two DLA supply depots—Oklahoma City and Warner Robins—that reported the largest amount of depot losses. DLA Directive 5025.30, *DLA One Book*, includes a section on Inventory Adjustment Research (dated

October 21, 2004), which sets inventory accuracy goals for DLA supply depots and requires causative research—an in-depth investigation—of adjustments for selected items[30] and suspected fraud, waste, and abuse to determine why they occurred. A Financial Liability Investigation of Property Loss is required if the adjustment meets specific criteria, including (1) gains or losses of classified or sensitive material; (2) an adjustment in excess of $2,500 for pilferable material; and (3) a loss where there is a suspicion of fraud, theft, or negligence. However, we found that DLA depot personnel did not thoroughly investigate most adjustments related to reported losses of sensitive items with demilitarization controls that we selected for investigation. Supply depot officials told us that they assumed the losses represented inventory recordkeeping errors, even though causative research results were inconclusive.

Property Damage

In addition to reported losses, we found significant instances of property damage at DRMS liquidation contractor sales locations. Because the terms and conditions of liquidation sales specify that all property is sold "as is" and assigns all risk of loss to buyers, the buyers have no recourse when property is damaged after being sold or is not in the advertised condition. As a result, customers who have lost money on bids related to damaged and unusable items might not bid again, or they may scale back on the amount of their bids in the future, affecting both the volume of excess DOD items liquidated and sales proceeds. On October 7, 2004, we purchased numerous usable items in original manufacturer packaging, including 35 boxes of bandages, 31 boxes of gauze sponges and surgical sponges, 12 boxes of latex gloves, and 2 boxes of tracheostomy care sets. We paid a total of $167, including buyer's premium, tax, and transportation cost, for these items, which had a reported total acquisition cost of $3,290. However, these items had become damaged due to rain and a leaky roof at the Norfolk, Virginia, liquidation sales location.

The majority of property damage that we observed at liquidation contractor sales locations is primarily the result of DRMS management decisions to send excess DLA supply depot property to two national liquidation sales locations without assuring that its contractor had sufficient human capital

[30] DOD 4000.25-2-M, *Military Standard Transaction Reporting and Accountability (MILSTRAP)*, (Change 2, Apr. 28, 2003), Ch. 7, "Physical Inventory Control," Section C7.9.3.2, identified selected items as classified and sensitive items regardless of dollar value, pilferable items, controlled inventory items, with an extended value greater than $2,500, and all adjustments with an extended value of greater than $16,000 or greater than 25 percent unit variance and greater than $5,000.

resources and warehouse capacity to process, properly store, and sell the volume of property received. For example, excess DOD property sent to the Huntsville, Alabama, liquidation sales location was stored outside unprotected from weather, including sun, wind, rain, and hurricanes during the summer and fall of 2004. The liquidation contractor's failure to record these items in sales inventory at the time they were received, when combined with lost and illegible property labels due to weather damage, resulted in a significant loss of accountability for many of these items.

Outdated, Nonintegrated Systems Impair Economy and Efficiency

Inefficient, nonintegrated excess inventory and supply management systems lack controls necessary to prevent waste and inefficiency in the reutilization program. For example, because the DRMS Automated Inventory System (DAISY) and DLA's Standard Automated Materiel Management System (SAMMS) are outdated and nonintegrated, they do not share information necessary to (1) identify and alert DLA item managers of excess property that is available to fill supply orders and (2) prevent purchases of new items when A-condition excess items are available for reutilization. We have continued to report[31] that long-standing weaknesses with DLA's inventory systems related to outdated, nonintegrated legacy systems and processes result in DOD and military units not knowing how many items they have and where these items are located. DLA has acknowledged serious deficiencies in its automated inventory management systems. Although DLA has an effort under way to replace SAMMS with the Business Systems Modernization (BSM) and DRMS has a Reutilization Modernization Program (RMP) under way to upgrade DAISY, so far these have been separate, uncoordinated efforts and they do not adequately address identified process deficiencies. While the systems improvement efforts are intended to integrate supply and excess inventory systems to support the reutilization program, they are not focused on resolving long-standing problems related to unreliable condition code data and incomplete data on NSNs. The accuracy of these two data elements is critical to the ability to identify like items that are available for reutilization at the time purchases are made.

[31] GAO, *DOD Business Systems Modernization: Billions Continue to Be Invested with Inadequate Management Oversight and Accountability*, GAO-04-615 (Washington, D.C.: May 27, 2004); *DOD Business Systems Modernization: Longstanding Management and Oversight Weaknesses Continue to Put Investments at Risk*, GAO-03-553T (Washington, D.C.: Mar. 31, 2003); and *DOD Management: Examples of Inefficient and Ineffective Business Processes*, GAO-02-873T (Washington, D.C.: June 25, 2002).

Concluding Comments

To effectively address problems with reutilization program waste and inefficiency, DRMS and DLA will need to exercise strong leadership and accountability to improve the reliability of excess property data; establish effective oversight and physical inventory control; and develop effective integrated systems and processes for identifying and reutilizing excess property. In addition, the military services will need to provide accurate information on excess property turn-in documentation, particularly data on condition codes, and item descriptions, including NSNs that are key to identifying items for reutilization. Improved management of DOD's excess property and a strong reutilization program would help save taxpayers hundreds of millions of dollars annually.

Mr. Chairman and Members of the Subcommittee, this concludes my prepared statement. We would be pleased to answer any questions that you may have.

ontacts and Acknowledgments

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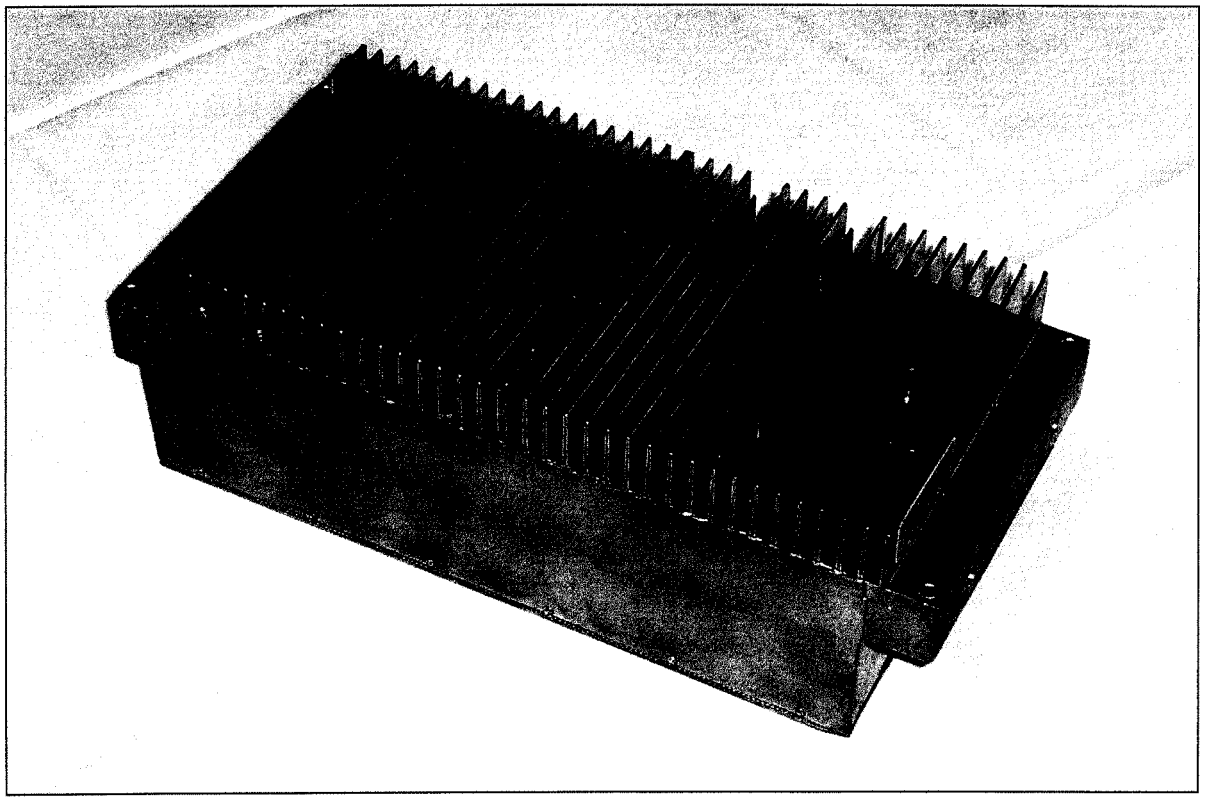

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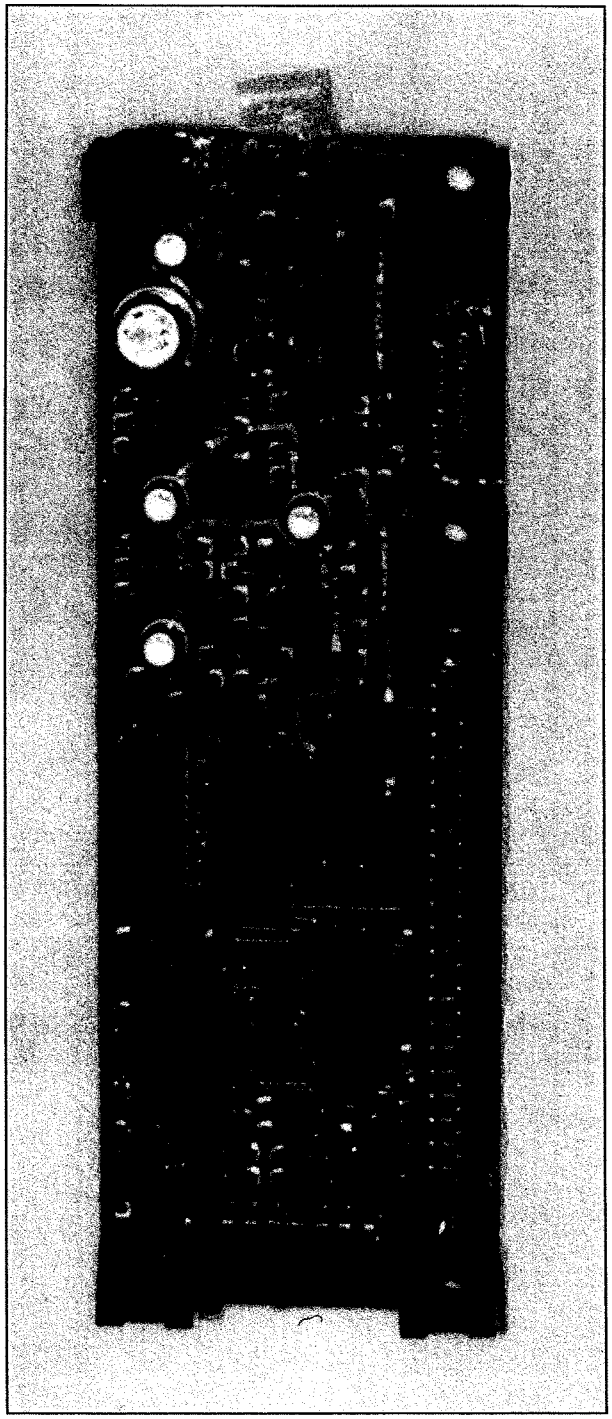

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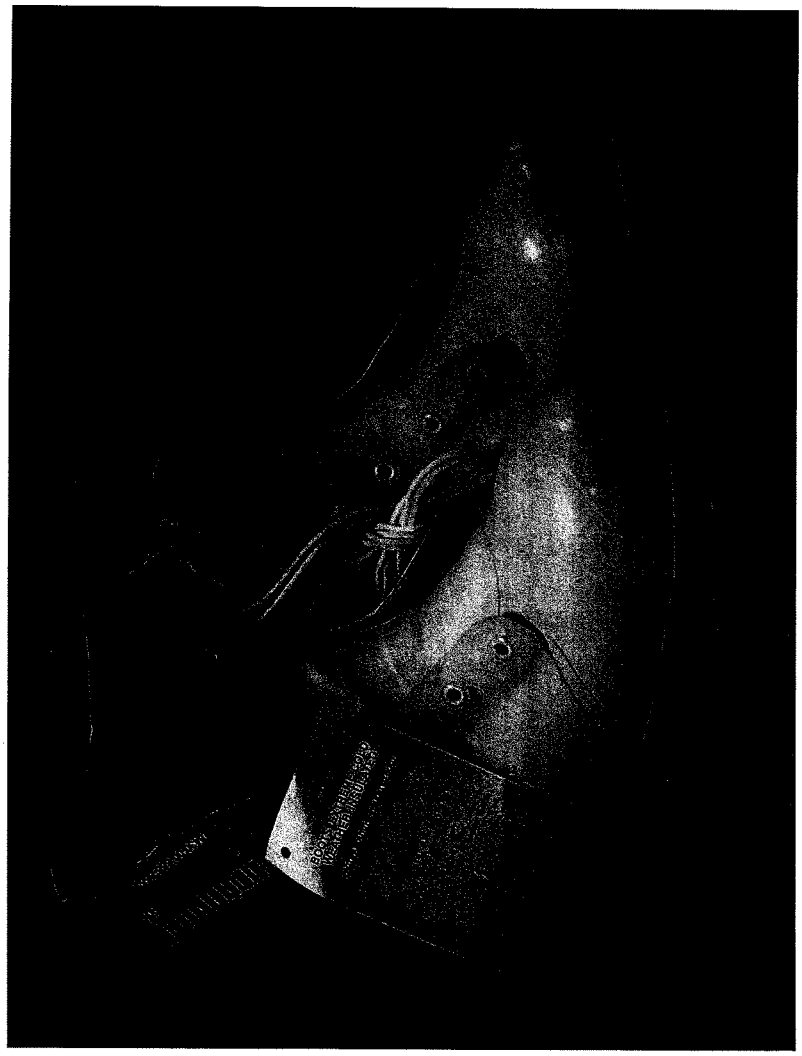

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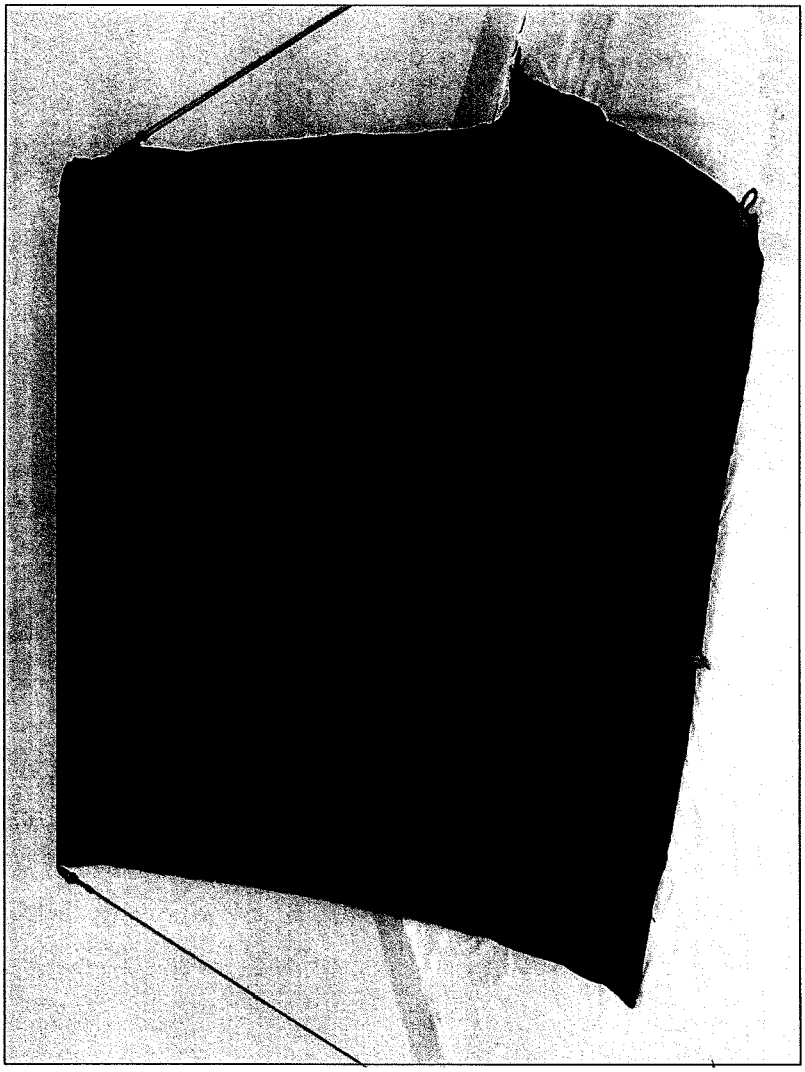

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Mr. SHAYS. Thank you, Mr. Kutz.

First off, how long was this investigation?

Mr. KUTZ. A little over a year.

Mr. SHAYS. And tell me, were you surprised by anything you found, or was your opinion such that you just weren't surprised?

Mr. KUTZ. Well, we had suspicions. In my opening statement I had mentioned the chem-biosuits from your hearing several years ago where they were selling them for $3 at the same time they were buying brand new JS List suits, which are the ones that the soldiers are using in Iraq, for example. So we had suspicions that this could be a broader problem, and after discussing this issue with your staff we decided it would be a good idea to take a broader look at the entire system to see how significant the waste and efficiency could be.

Mr. SHAYS. Well, I'll use the answer to my question by saying I wasn't surprised because of that, and is that your response?

Mr. KUTZ. That would be my response, yes.

Mr. SHAYS. All of the equipment that we see here, it's your testimony it is still being used by DOD?

Mr. KUTZ. I don't know if it still is. At the time that we ordered it or requisitioned it, it was still in demand by the services, that is correct.

Mr. SHAYS. Of these, which ones do you find the hardest to comprehend—well, I use the word—which ones here do you find are the most alarming; in other words, alarming you can use in terms of threatening national security, or just alarming because of the magnitude of the issue? I have my own personal choice, I'm just curious what yours is.

Mr. KUTZ. I think we probably have the same one. The power supply units for nuclear attack submarines, we're not sure why DOD would be letting GAO have them. We don't have any nuclear submarines at GAO, so there would be no reason for us to get those. The same thing with the circuit cards that are for cryptologic satellite communications. We have no need for that, yet we were able to get that.

Now, whether there is any security issues——

Mr. SHAYS. When you say "we," in other words, why would anyone buy it?

Mr. KUTZ. Well, we didn't buy those. We requisitioned those as GAO. The medical chests, the power supply unit and the circuit cards, we requisitioned those. They knew we were GAO for those. The rest of them we used our undercover card to buy on the Internet from the contractor, govliquidation.

Mr. SHAYS. Now why did you do the requisition? Did you try first to see if you could buy them?

Mr. KUTZ. No. We wanted to check both parts of the system. The way the system works is, first of all, DOD units and some other entities get a first shot at these items, and then they go to GSA, and governmentwide other agencies get a chance, State and local governments, local law enforcement, and once they go through that they go to governmentliquidation.com and can be sold on the Internet. And so we wanted to check out various stages of the process to see what we could requisition versus what we could buy at the end.

Mr. SHAYS. I'll add another one, the uniforms and the insignias that you could buy; is that the extent of the insignias that you could buy or do you think you could buy others as well?

Mr. KUTZ. We bought others; I mean, we didn't have enough room to put them on the board. We had 8,000 of them.

Mr. SHAYS. You can get 8,000?

Mr. KUTZ. Yes.

Mr. SHAYS. Not just duplicates, but other insignias as well?

Mr. KUTZ. We have some others, yes.

Mr. SHAYS. So it is possible for someone to just basically look like a soldier or sailor, Marine.

Mr. KUTZ. Yes.

Mr. SHAYS. Just as an aside, I would imagine some of these uniforms are sold to our troops. Do they have to pay full price when they buy them?

Ms. FISCHER. Chairman Shays, the military has a uniform allowance, so within that allowance they're issued a number of uniforms, shirts, trousers, jackets, camouflaged clothing as well.

Mr. SHAYS. But they're priced at the going rate; I mean, they are given an allowance——

Ms. FISCHER. Correct. The units will pay for them, yes.

Mr. RYAN. I just want to add, if a soldier goes online he can buy that uniform. So the difference here is the government liquidators is selling large quantities, where you have your e-Bay, which is selling more one or twosies. So in this particular case, in regard to your original question, from a national security perspective, yes, that is a problem in my opinion, the uniform, because it can be purchased, and someone who would like to take advantage of the situation could manipulate the facts, put that uniform on and cause some discomfort for other people I would believe.

Mr. SHAYS. One of the most alarming things when you're visiting in Iraq is the concern that someone could basically wrap themselves in so-called body armor, but it is really a plastic explosive device, it would look identical. And the concern is that they would walk in looking like an Iraqi soldier or an American soldier. And what you're saying is this is easily ordered.

Mr. RYAN. You can buy them, that's for sure.

Mr. SHAYS. OK. Walk me through it, and then I will yield to Mr. Waxman—we have as much time, Mr. Waxman, as you want to have, and Mr. Duncan—walk me through the significance of the $400 million. It seems like a lot of money.

Mr. KUTZ. What we did to get the $400 million is these were exact matches of items that were being purchased that were available in new or unused condition or excellent condition in the excess property system for 2002 and 2003. So we did exact matches of what is called national stock numbers. So to the extent that the data was reliable in the system, which is an issue I mentioned in my opening statement, much of the data is not reliable. We had exact matches of items being bought in the same fiscal year that were available in the excess property system in new condition in the same fiscal year.

Mr. SHAYS. And this is equipment supplies worth $400 million that was excess—viewed as excess, and yet was being continually purchased by DOD?

Mr. KUTZ. When I say excess, it went outside of the DOD system. It was not reutilized within DOD. It was either sold on the Internet, given away or destroyed.

Mr. SHAYS. So—but at the same time they were buying that very same equipment?

Mr. KUTZ. Correct, the identical items. It had to be an identical match to be part of the $400 million.

Mr. SHAYS. Just so I know, before I yield to Mr. Waxman—not yield, give him his time—Mr. Rhodes, tell me each of your roles in this so we understand a little bit of your expertise here. Did you each have different assignments?

Mr. RHODES. My assignment was to review some of the technical equipment to make certain, one, that it had not been used; two, that it was actually what it was described to be; and three, that there was some value to the equipment. For example, let's go to your original point about the power supplies. Just on the facts, item No. 1, it is true, GAO does not have a nuclear attack submarine. Second point is that this is still to this day labeled a critical shortage item by the U.S. Navy relative to the Seawolf attack submarine.

Mr. SHAYS. It's labeled as—say that again.

Mr. RHODES. It's a critical shortage item.

Mr. SHAYS. That was put as excess property.

Mr. RHODES. Yes. And third part is it had never been used, it had never even been screwed into something. So power supply in the possession of the Government Accountability Office and, one, we have no reason to have it and, two, it's a critical shortage item.

Relative to the cryptographic gear, they had not been used, they had not even been plugged in because there was no wear on the pins where they're supposed to meet with the satellite calling system. There is no cryptographic keys inside of it, but you can understand the frequency that it runs at and things like that, the kinds of power that they're going to use. The other part is that is an NSA controlled item. The U.S. military is supposed to respond back to the NSA and not destroy it. They're supposed to go back to the National Security Agency about the cryptogear as part of the Uniform Cryptographic Architecture and say this is——

Mr. SHAYS. So your point is it's one thing to have certain things that are dangerous and being shared, it's another thing to say it's excess and we no longer need it. But what you're saying is there is actually a specific requirement that be returned.

Mr. RHODES. Yes, sir.

Mr. SHAYS. Tell me your focus, Ms. Fischer.

Ms. FISCHER. Chairman Shays, I was responsible for leading the audit portion of our work. That included the assessment of the data in the purchasing system and the excess inventory system and leading the work to test the inventory accuracy at five DMOs and five DLA supply depots.

Mr. SHAYS. Mr. Ryan.

Mr. RYAN. My job here was to help coordinate audit investigations, to identify items that we should purchase, to do investigations on seeing how they were excessed, why they were excessed, who purchased them, what happened to those items afterward. We had three agents, Agent Rodriguez, Agent Newbolt and Agent

Brown, traveling around the country doing interviews with the people who were excessing them and the people who were buying them at the same time.

We provided support in using our undercover capability to make the purchases through the governmentliquidation.com. And we also worked with Ms. Fischer's team to do some testing on shipments that were short of numbers, quantities, and track them through the system to see if anywhere along the way the DOD would have made some type of adjustments for missing items that were not part of original shipments.

Mr. SHAYS. When I was in the Peace Corps, I was in Molokai, and I was invited to spend Christmas at a friend that I had met. His wife was an unbelievable cook, but at any rate he showed me—and I'm going back 30 years ago, and he showed me his freezer. And if you lifted up his freezer, it all said U.S. Government, and it appeared to me to be products that really were part of our military that were somehow in his possession. He wasn't showing me to boast about U.S. Government, he was just showing me that they had a lot of different food and they ate well.

Mr. Waxman.

Mr. WAXMAN. Thank you, Mr. Chairman. I want to thank each of you for the work you have done. This is really breathtaking to imagine that the equipment that I presume still can be used by our own military is being bought for pennies on the dollar, and if they're not being used by the military and they're being bought for pennies on the dollar, we're shortchanging the dollars we should be getting so that we can use it for the needs of our military in Iraq.

Let me just verify. Are we talking about equipment that could be used right now by military people, our military people in Iraq?

Mr. KUTZ. Yes.

Mr. WAXMAN. Give me a quick few examples of that.

Mr. KUTZ. Oh, I would say probably several of these things; certainly the medical supplies could be, the gas burner units possibly, the suction apparatus, and I guess the insignias and the uniforms possibly. So a number of these things could be.

Mr. WAXMAN. So they could be used by our military in Iraq, and you have also testified that they could be used by our enemies in Iraq if they are purchased by just going on the Web and getting a bunch of uniforms to appear like they're American soldiers. Is that something we need to be worried about, Mr. Ryan?

Mr. RYAN. I think that is a concern. I think the DOD should take a serious look at what they're excessing in regards to uniforms and insignias, determine if that uniform is still being used by our soldiers today, why are we getting rid of it. If it is so blatant that the uniform can be recognized by the humans in charge of security that it is not a current uniform, then I think they ought to excess it. But I think a lot of consideration should be given to—DOD should give a lot of consideration to what they're doing with the disposal of these uniforms, yes.

Mr. WAXMAN. There are two agencies at the Department of Defense who are involved; is that correct, Mr. Kutz?

Mr. KUTZ. There is the Defense Logistics Agency and the Defense Reutilization Marketing Service, which is under DLA's control basically.

Mr. WAXMAN. And what are they supposed to be doing; are they supposed to be getting rid of stuff we can no longer use and selling it for the most money that can make?

Mr. KUTZ. Well, DLA is in charge of buying the new items and supplying the troops; they do a lot of the logistic support for our military forces. The excess property system has many functions, one of them being to reutilize new and usable items like the ones we see here today. They also do things such as demilitarizing or destroying items that could be used, should not be having technology transferred outside of DOD. So certain things now like the chem-bio suits that we testified on before are now typically destroyed if they are, rather than sold to the public, which is a result of this subcommittee's prior hearings, a positive result of them.

Mr. WAXMAN. Ms. Fischer, let me ask you this question, because I think it fits in with what you said was your focus. How is it that an ordinary retail establishment or grocery store in this computer age can keep track of their inventory, but it doesn't appear that our Defense Department can do the same?

Ms. FISCHER. That's a good question, Congressman Waxman, and you're absolutely right. But DOD has systems that are not integrated, it doesn't know where its various pieces of property are at any given time, and the systems don't give adequate visibility over those items for reutilization.

Mr. KUTZ. And Congressman, I'm going to be testifying tomorrow on that very topic before Chairman Platts and Representative Towns. DOD had reported over 400 duplicative stovepipe business systems, and of those, 2000 of them, they report are logistic systems. So you can imagine 2000 systems out there that do logistics. It's a very, very difficult situation for the Department to be effective with supply chain management with that kind of technology environment.

Mr. WAXMAN. Have you given thoughts for recommendation of what we ought to do in Congress?

Mr. KUTZ. With respect to systems modernization?

Mr. WAXMAN. Yes. These agencies are part of the Defense Department, we fund the Defense Department, we expect them to be using this property in a reasonable way, they use some common sense, if nothing else, but at least they have their systems in place. What do we need to do, scrap the system and recreate it, or is it fixable?

Mr. KUTZ. I think you need to do what you're doing today. You need to have hearings like this, and when issues like this are out there you need to have oversight hearings, you need to stick with these issues and hold DOD accountable. It's really a management issue. It's not really—I don't think there is any legislation that's not in place right now that will prevent them from being successful here. It's really a matter of leadership and management.

Mr. WAXMAN. So if Congress does its oversight job, it keeps them honest?

Mr. KUTZ. I think that's the right thing for you to be doing.

Mr. WAXMAN. And if we didn't do our oversight job, isn't there somebody in the administration that's supposed to be watching what goes on in the Defense Department?

Mr. KUTZ. Well, certainly the management within the Department of Defense is responsible, and I guess OMB also has some oversight over some of the systems issues governmentwide, whether they're e-gov initiatives and other types of oversight efforts. So there are other people responsible.

Mr. WAXMAN. How easy are we talking about the purchase of these items? You've mentioned a Web site, it sounds like a government e-Bay service where you can go on there and pick and choose medals, uniforms. Can you get rocket launchers, Mr. Rhodes? What is the most serious thing——

Mr. RHODES. We were not able to procure rocket launchers.

Mr. WAXMAN. What is the most serious thing that you were able to procure that could really endanger our security?

Mr. RHODES. From my technical perspective, it's difficult to say. I mean, I look at a tent and I see a soldier that's getting wet. I look at that medical equipment and I see a soldier that's bleeding. I look at that gasoline burner and I see a soldier that's cold. I look at those boots, and that's a soldier who's barefoot. I look at that suction apparatus, and there's a soldier with a chest wound from an improvised explosive device on the road into downtown Baghdad.

So, I mean, all of these have their own weight and they have their own measure. I can't pick any one of them and say it's the most catastrophic.

Mr. WAXMAN. Well, let me ask Mr. Ryan, because I heard something about an investigation of missing warheads. Do you know anything about that? Or circuit cards, what would those be used for? Do you have something—some information on——

Mr. RYAN. Well, I defer to Mr. Rhodes in regards to identifying the specific purposes of the items. We were given the leads and we followed the investigation that we were told to do. So I will defer to him in relationship to the degree of importance or——

Mr. RHODES. The relative importance of a warhead. The argument is made that they were inert; however, the warheads were sitting on the back of a flatbed truck and were not protected nor covered. If warheads are missing, even if they're inert and you cut them open, then you can find out how they work. Inert just means they don't have explosive in them; it doesn't mean that you don't understand the shape of the charge, it doesn't mean you don't understand how they fragment, it doesn't mean you don't know how they fuse and arm.

Mr. WAXMAN. Could somebody get a missile warhead that is inert through any of these systems of procurement?

Mr. RYAN. I think in that particular case, if it's not coded correctly when it's going into the disposal system, much like these items were, then someone could requisition it. It all depends on the coding, the de-MIL coding of the power supply or the circuit card. These are examples which we were not supposed to get, but we did.

Mr. WAXMAN. I see. So you found a lot of miscoded information on those things?

Mr. KUTZ. Well, let's use the example of the tent. The tent was coded as condemned. These boots were coded as condemned, and they're new and unused.

I think what we're talking about too, before, was items that were lost, or losses if you will, and there were some things that were lost that when we did our statistical sample we tried to find aircraft parts, helicopter parts and chem-bio suits and they were gone. And body armor also was reported as missing. And so we did report $466 million of items that DOD themselves reported losses. But we became concerned about that because when we did our random statistical samples, when we looked for some of these items they were just gone and there was no explanation of where they had been. And Special Agent Ryan is doing some followup investigations on that, but we're not sure we're going to be able to come to resolution as to what happened.

Mr. WAXMAN. Mr. Kutz, you suggested that we have congressional oversight. Do you think Congress needs to revisit the procurement laws themselves to spell out what can and cannot be contracted, either contracts, government contracts, obviously for services and we hear a lot about that, but these are government contracts for sale of items, do you think that ought to be covered by changes in procurement law?

Mr. KUTZ. I'm not a procurement expert. I would defer that question.

Mr. WAXMAN. Well, it was really amazing that we're seeing from you these kinds of examples that are really horrifying when we know that our troops are not fully equipped and we're told we don't have the money for it. We know we have these huge budget deficits in this country, and yet we're finding our own Defense Department so wasteful in the management, maybe not intentionally, but wasteful nevertheless, of the costs and equipment and the use of items that we've purchased to make our country stronger. And their inefficiency I think is making our country weaker and our country also poorer as a result.

Thank you very much.

Mr. SHAYS. I thank the gentleman.

Before going to Mr. Duncan, I just want to have you clarify a little bit. There is so much that we could be talking about we could keep you here a long time. And I'm going to make an assumption that some of what you are doing is triggering additional investigations; is that correct, Mr.——

Mr. KUTZ. That's correct. We are looking at some of the lost and potentially stolen items.

Mr. SHAYS. And so just explain to me—and you said in excess property loss, in other words, it's literally property that should have been there that isn't?

Mr. KUTZ. Correct.

Mr. SHAYS. And when you talk about the property loss of $466 million, that is what you discovered or what DOD acknowledges?

Mr. KUTZ. No. That's what they reported. When we became concerned about it was when we were doing random statistical samples at 10 of the locations, and some of the lots we went to observe basically were gone, complete lots were gone.

Mr. SHAYS. Was that an infrequent occurrence? Was most of the time it there?

Mr. KUTZ. Most of the time things were there, but certainly it was enough for us to be concerned. I mentioned aircraft parts,

chem-biosuits, helicopter parts, some of the things were not just concerns because of the frequency but for the types of things that were missing.

Mr. SHAYS. But they acknowledged $466 million unaccounted for.

Mr. KUTZ. Correct. And again, whether they're recordkeeping issues or stolen or lost, nobody knows for sure.

Mr. SHAYS. And we don't even know how accurate that number is?

Mr. KUTZ. Correct. That could be understated, overstated.

Ms. FISCHER. Because in the sample we had at the Columbus DRMO there were 23 examples of either entire turn-ins that were missing or quantities of other turn-ins that were missing, and they only recorded losses for two of those. They never recorded the losses we identified in our test work.

Mr. SHAYS. So what you're telling us is, when you asked DOD their losses, they said $466 million, which is a very high number, I mean it really is. I mean, it's not $466,000, it's not $4.6 million, it's not $46 million, it's $466 million. You're saying that you encountered—a majority of those losses that they couldn't account for were not being stated as losses?

Ms. FISCHER. Correct. And that includes those 72 chem suits at the Columbus DRMO that weren't there when we did our testing.

Mr. SHAYS. So when you identified losses just randomly, most of the time they weren't included as losses by DOD?

Ms. FISCHER. At the Columbus DRMO that is correct. We don't know across DOD because we didn't test every warehouse.

Mr. SHAYS. I understand. Thank you.

Mr. Duncan, you have the floor for 10 minutes.

Mr. DUNCAN. Thank you, Mr. Chairman. I will be very brief. I've got some constituents waiting on me. But Mr. Kutz, how long have you been with the GAO?

Mr. KUTZ. A little over 13 years.

Mr. DUNCAN. Have you seen any worse examples of waste in the time that you have been there?

Mr. KUTZ. I've seen a lot of examples of waste, that's kind of what we do. I'm in charge of our team that does forensic audits and special investigations. And so we look at fraud, waste and abuse across the government and there is lots of it, and DOD has its share.

Mr. DUNCAN. Well, let me ask you this, a witness on the second panel will try to defend this by saying that their primary focus should not be on how much we made on the resale of these items, the important point is getting the right items to the warfighters when they need them while simultaneously providing optimal return on the investment of the American people. Do you regard what you found as providing optimal return on the investment of the American people?

Mr. KUTZ. No. The $400 million I mentioned would be a waste of taxpayer money directly related to the excess property system. The other part of the $3½ billion of waste that we talked about is not the fault of the excess property system; it is back to the logistics overbuys that are a chronic DOD problem, where they just buy more than they need. And by the time it makes it to the excess property system, you could have a 5 or 10-year-old computer that's

really not worth much by that time. It's still brand new in the box, but after 5 years that computer is not worth a whole lot of money.

Mr. DUNCAN. Well, I think most people, if they heard you were buying boots for less than $12 a pair on an advertisement in which you thought you ordered 30 boots and you ended up with 42, 37 of which were brand new, never used before, and you bought them for less than $12 at the same time the Pentagon was ordering what, 21,000 new pairs at $135 a pair?

Mr. KUTZ. Correct.

Mr. DUNCAN. Something like that. I mean, if I told that to people in my district they would think it's terrible.

Mr. KUTZ. I wish I could tell you that I was shocked but I'm just not because I have seen this kind of thing across the government.

Mr. DUNCAN. Well, I can tell you this, most of these examples that you've given here today would shock most of the people in my district, I can tell you that. They may not be a shock to you because you have seen so much of it over the years. I mean, when you're talking about buying these half tents, you know, and these—all these other things that just—sometimes pennies on the dollar. In fact the boots, I saw someplace where the boots were later sold to a trade company for 40 cents on the dollar.

Mr. KUTZ. Right. 172 pair of these extreme cold weather boots were sold to the Robinson Trading Co. They sold them to a place called Mad Dog Wholesalers in California for $5 a pair. Mad Dog sold them to other entities, excess property entities for $30 a pair, and the trail ended there, we didn't follow it any further, but in all likelihood they retailed them for something greater than $50. And that's an example where everybody made out but the American taxpayer.

Mr. DUNCAN. Well, all I can say is, I mean, when I read all this about these chemical—this was from the earlier hearing, the chemical suits that you bought for $5 were, these items had an original DOD acquisition cost of $55,817 and GAO paid only $5 shipping cost to obtain all of them; I mean, this is just ridiculous. And in fact, I think that anybody who didn't work for the Federal Government would be embarrassed and ashamed to come up here and try to defend something like this like the witnesses on the next panel are apparently going to try to do.

Thank you, Mr. Chairman.

Mr. SHAYS. I thank the gentleman.

Mr. Dent, do you have any questions?

Mr. DENT. No questions.

Mr. SHAYS. What I would like to do is have our counsel ask a few questions before we get on to our next panel, and I may have a few more.

Mr. HALLORAN. Thank you. In the course of this work did you discern followup or implementation from your previous work in this realm? Did you see a risk assessment process for biological lab equipment?

Mr. RHODES. There is a risk process that is labeled interim. It is not, we aren't seeing anything finished in it. There was an interim process for it. It does not include coordination, as our recommendation made, with the scientific community inside or outside

of DOD. Therefore, we have some pretty strong reservations and some strong concerns about the veracity of the risk assessment.

For example, some of the equipment that we were able to get was just being held. That's the entire risk plan was just to hold on to it, once it comes in to park it and leave it.

Mr. HALLORAN. To what extent would the success of even that interim proposal rely on data feeding it?

Mr. RHODES. Well, it wouldn't in this place because, one, it's the interim risk assessment, and the other is it didn't actually take in the veracity of the scientific community that we recommended, both inside and outside of DOD.

Mr. HALLORAN. Mr. Rhodes, would you characterize the DOD response to the report? The DOD has seen this and had time to react to it; could you characterize their response?

Mr. KUTZ. I would say it's responsive, and that they're taking action on all 13 of the recommendations in this report.

Mr. HALLORAN. I'm going to ask you to do a little better than that. They're taking actions such as they've said they did before. Are they actions that are likely to yield results in the near term?

Mr. KUTZ. Well, I think there's two things. In the short term they can't deal with the systems issue. In the short term they're going to have to improve human capital and processes. In other words, when the excess property items come into the system people are going to have to do a better job of validating the data. Right now that was one of the problems we saw at some of the systems at excess property locations, is that they were not validating data when it came into the system.

So they can improve the human capital and the processes, but the systems is one that is a long-term situation, and history shows that they have not been real successful implementing new systems that provide integrative solutions.

Mr. HALLORAN. So you're saying that based on the quality of the data you saw, the most critical near term thing they could do is improve the training of the intake of those creating the data at the start?

Mr. KUTZ. Yes. Validation of data and improvement of the quality of the data in the system is the most immediate thing they can improve.

Mr. HALLORAN. And that's pretty doable; it doesn't require a multi billion dollar computer system——

Mr. KUTZ. Correct. I mean, it doesn't give you the integration of the excess property system in the purchasing system, but it at least gives you good data so you can do exact matches and determine what's available before you buy it.

Mr. HALLORAN. Well, speaking of integration, who wants to tell the story of the biological safety cabinets? Because you saved the money on this, didn't you?

Mr. KUTZ. Mr. Rhodes can discuss that.

Mr. RHODES. There were a set of—it was a full set of six biolevel 3 safety cabinets. At an earlier hearing we came up and talked to you about—these are safety cabinets that are one level below biolevel 4. Biolevel 3, you can work with some extremely dangerous pathogens. We found out that this equipment was available. And I have a friend, a scientific friend, who is the head of the Biolife

Sciences Center out at Dugway Proving Ground, and I asked him if he would like six biolevel 3 safety cabinets for just basically for free, DOD had to pay the shipment to, and he said of course I would because in the process—he was actually in the process of trying to set up the procurement of three biolevel 3 safety cabinets, and now he was going to get six for nothing, somebody else had to pay the shipping. And this is an example of equipment that was just being held. It had come in, had been excessed, but the DLA——

Mr. HALLORAN. It had been miscoded, so it wasn't even visible to him, had he not looked in there——

Mr. RHODES. It wasn't on the Web page, it was sitting in a Norfolk site. And so we parlayed, we did the deal, as it were, we put the folks at DLA in touch with the folks at Norfolk. The deal was closed, and it ended up not just being three biolevel 3 safety cabinets, but they got a whole series of absolutely pristine scientific equipment, including some extraordinarily expensive microscopes, as well as tools and cabinets and controls and all that.

So I guess we returned some money to the taxpayer by making certain the deal got closed or something. But it was a matter of we knew someone, and there was no system in place for DLA to know the same person.

Mr. HALLORAN. Your report discusses, it seems to me, significant extent of kind of downcoding of surplus material when it's turned in, and you found it, it was marked condemned and it's good as new. And your report refers to a broader phenomenon of downcoding material. Why is that? Is it error, or is there some incentive to do it? Mr. Ryan mentioned this aftermarket that likes the stuff that way. Is there some incentive to mark it as condemned and keeping it moving?

Ms. FISCHER. There is actually confusion I think on the part of the military units about what the definition of unserviceable is. In the interviews we did with the people that are turning in the excess equipment, they view unserviceable as meaning an item is unserviceable or unusable to them, they don't have a need for it. So it is unserviceable even if it's new and unused, so they use one of the condemned codes or codes that says it needs repair or something in the unserviceable category.

We did talk to DOD about this even a week ago, and they recognized that there is training needed to resolve this problem, and they have started a training program.

Mr. HALLORAN. That's training a lot of people. Who in the unit can excess something, to declare something excess?

Ms. FISCHER. Well, the people that are using the equipment first off. When they turn it in, they know what condition it's in. They know whether they have used it or not or if it needs repair. And we saw things at the DRMO that had signs on it or tags on it that said needs repair or broken. They can certainly identify the equipment that way.

And then the supply and logistics units that actually process the turn-ins can observe it, look at it, test it, or ask the turn-in unit the condition of the property. And they're in the best position to record the condition before they turn it into the DRMO. And then DRMO personnel should inspect it and verify that the information

they're getting is correct before they enter it in inventory. And then you would have a good process. You can rely on the condition, the item description, the quantity that's advertised as available. You wouldn't order something and come up short later or come up with the wrong item later.

Mr. RYAN. I might add, also, that there is some success in coding also. I will give you an example. Up at NSA they disposed of several hundred computers because they changed systems. These computers were brand new, in a box, hadn't been used, but they were there for a year or two because of the systems change. The individual there responsible for property decided they were no longer serviceable, so they sent them to DRMO. Well, when DRMO saw them, they saw they were brand new in a box, and quite honestly those computers were a lot better than what other Federal agencies had or were using right now, so they upcode. They change the code to make it a very good product. Well, because we have special programs in this process, they're constantly hawking the Web site to see what items are coming up for new.

Mr. SHAYS. Who is "they?"

Mr. RYAN. I'll give you an example——

Mr. SHAYS. I don't understand who "they" is.

Mr. RYAN. It's the Law Enforcement Sharing Organization [LESO]. They basically saw these computers, and they went ahead and requisitioned them, all of them, as soon as they became available. And they came and got them. And what we did is we followed up on those computers and we found out that they were warehousing these computers and did not distribute them.

So they took them out of the hands of people that could actually use them. They were warehousing them for the future. So what it is——

Mr. SHAYS. Let me understand. They are warehousing technology that can be dated every moment for the future?

Mr. RYAN. Well, what the law enforcement did is they took them for the whole State of Kentucky. And in this particular case, they put them there until people needed them. And then they distributed them as they needed them. So it was a success in regards to realization if the special programs are to get the DOD property.

Mr. HALLORAN. Finally, the testimony on the next panel is going to suggest that the waste in the system is somewhat marginal or within an almost inevitable boundary because of the size and scope of the DOD acquisition and operation. Do you concur with that?

Mr. KUTZ. If you talk about the lost and stolen, we wouldn't concur otherwise. There is simply shrinkage in a retail entity, but isn't a retail entity. This is a warehousing entity. And I believe if they had integrated systems, that they could eliminate several hundred million dollars of this waste.

With respect to the lost property, if that is what they're talking about, we probably wouldn't agree with that. We are not talking about Charmin and toothpaste here. You're talking about things like body armor and chem-bio suits that are missing. So that is not a relevant apples and apples comparison.

Mr. RYAN. I might add, too, that I'm not sure that the numbers—the numbers are understated. I think that there is more missing than what is reported because just in—we had a hard time initiat-

ing investigations. Because we didn't know what number to start with, when we tried to validate what the generator was putting in a box, we couldn't do it. The numbers didn't follow through. Using the example with Ms. Fischer that we used in Ohio, there were numerous shipments that were missing items.

The generator put down 100, but when we counted the box when it was received, there might have only been 80. But they passed it through. They don't count numbers. It is a pass-through system. So they don't spend time counting.

So you can't tell really how much is missing, how much has been stolen. It is just, it is very hard to do from an investigator's point of view because you have no starting point. You need a starting point, and we didn't have one.

Mr. KUTZ. And back to the $400 million, too, again, if you consider the fact that the boots and tents were in the system as condemned, we didn't count those in the $400 million because those showed up as items that were unserviceable.

We only counted items toward that were exact matches that were shown in the system to be new and unused or in excellent condition. So that number is probably larger.

Mr. RHODES. I just wanted to make one point about the difficulty in the numbers in those systems. Mr. Kutz and I have testified on several occasions about problems in the systems. If we go to our example of the dummy warheads, that is a hard example where we couldn't figure out what the number is. So we don't know if any were missing or not. Because the driver had one number; the deliverer had another number; the people who originated it had another number.

The point I would make is that, yes, if somebody wants to say there is something on the margins, fine, they can go ahead and say that. But when you're talking about inert warheads, I don't know that anybody in the private sector sells inert warheads. Likewise with the power supply. I don't know that there is—we aren't talking about the margins there. We're talking about a critical shortage item. Also, I would make the point that, the fact that we were able to get that power supply is listed as a successful reutilization.

So the fact that the Government Accountability Office, that has no Sea Wolf nuclear attack submarine, got the power supply for the electronic warfare system for that very same submarine as a critical shortage item is now listed as a successful reutilization.

Mr. SHAYS. As I listen to this, I think that we don't have to make it sound worse than it is. Because it is really bad.

And I'm also thinking that I can't imagine anyone in DOD wanting it to work this way. So I'm now trying to struggle with why it's happening.

And I'm trying to think of what I would do if you asked me to be put in charge of this program. I mean, is it almost without certain resources and support, is it almost in your judgment—Mr. Kutz, if you were asked to be put in this program, how long do you think it would take for you to straighten it out.

And I don't mean it in an arrogant way. In other words, if you used the best of your skills and so on, if you were coming, we said OK, you are going to be in charge of this program, and I say, OK, you're in charge, and you have this amount of time to do it, and,

then heads roll if you don't, what amount of time should I give you to straighten out this problem?

Mr. KUTZ. Well certainly accountability is an issue, and I think there is a lot of turnover in the leadership of some of these areas like the DRMOs, so turnover would be an issue. I don't know if I'm the right person. I don't know if I could ever fix it any better than anybody else. DOD has some of the best people in world. And I'm no better or worse necessarily than any of those people. So I think it is a difficult system.

Mr. SHAYS. Let me ask you in this way, we have extraordinarily capable people in DOD, but we do have Government limits in what they can be paid.

Mr. KUTZ. That is true.

Mr. SHAYS. My understanding is that the $18 billion figure that is over a 2-year period is excess goods, excess material, correct?

Mr. KUTZ. Correct. That is the original acquisition cost for items. So they could be 5, 10-year-old items, but that is what they originally cost.

Mr. SHAYS. So they originally cost $18 billion, and so some of them might have been used?

Mr. KUTZ. Absolutely. Most of the items are, as I mentioned in my opening statement, used items, in need of repair or kind of junk basically. The $4 billion we're talking about is some of the nuggets going through the system of brand new items or new unused items. So this is the minority of the stuff.

Mr. SHAYS. Let's focus on this, on the $4 billion. And I hear, you know, some of my colleagues who rail against contracting, and Lord knows we need to do good supervision of contracting. But if you could get a contractor and you paid them $10 million, but he solved the problem with an organization of people, it would be money well spent. We don't have that capability. So we are limited, it seems to me. Correct me if I'm wrong. Are we able to go outside DOD and contract this all out potentially?

Mr. KUTZ. Yes, I mean, we do contract things out, if you look at the other hearings we have had with you on business systems modernization, and I'll say DOD right now is spending $13 billion a year on its business systems or $35 million a day for the 4,100 stovepipe duplicative systems they have, that is not a very good return on investment for taxpayers. And I would say a vast majority of that money is probably going to private-sector contractors who are not able to or have not been able to solve DOD's problems. So I think some of the best minds in the world are working on this, and it really has been a very tough thing to resolve.

Mr. SHAYS. So then let me, you had pages and pages of recommendations. List to me what you think are the most important recommendations.

Mr. KUTZ. Well, I'll give you mine, and I'll let the other folks here chime in, but I would say the issue related to validation of data would be No. 1 where items that are turned in are correctly recorded, because if you don't record them correctly at the very start of the process, often times we see that they go through the entire process in error.

So for example, these boots or the tents that were coded as condemned, someone should have caught that along the process.

Mr. SHAYS. When we code them, do we have the name and the number, or do we just have a number?

Mr. KATZ. It would be the national stock number which is a unique identifier for these items, a description of the items, the quantity, the condition code, all that.

Mr. SHAYS. So someone should be able to look at it and say, you know, these sure as hell aren't boots.

Mr. KUTZ. Correct. And they're not doing that. That is the policy. The policy is, when items are turned in, they are supposed to be validated for the most part, and we found that was one of the biggest issues that wasn't happening.

Mr. SHAYS. So validation of data is one. What is another one?

Mr. KUTZ. I'll use one more and let the other folks talk. The long-term integration of the purchasing system and the excess property system where, if someone is going to buy the new boots, the system does not let them buy the new boots because it tells them that we already have boots in the warehouse. To me, the integration of systems like that would be a major improvement of what they have and could really eliminate a lot of the waste I'm talking about.

Mr. SHAYS. I'm not sure I fully grasp what you're saying, so say it over again.

Mr. KUTZ. Let's say you have an acquisition system that tells me that the military units need 10,000 of these boots. When I go to buy those 10,000 boots, the system doesn't tell me that there is 2,000 boots in the excess property warehouse. So I go buy 10,000, but I already had 2,000. If I had known there were 2,000, I would have only had to have bought 8,000.

Mr. SHAYS. And you would have had the others right away?

Mr KUTZ. I would have had the others right away. They were already in the DOD warehouse.

Mr. SHAYS. I'll take some other recommendations that you would want?

Mr. RYAN. I think the two that I have are very similar to Greg's. I think there has to be some type of accountability. Someone has to be held responsible in the beginning of this process when you're entering the excess property stage. You have to be able to verify numbers and the conditions.

My second recommendation is to have a complete modernization of this coding system, make it more user-friendly so that people understand it. Just because NSA can't use that computer, they shouldn't declare it unserviceable. Because when people go into the system and they see an unserviceable computer, they're going to back away from it because they don't want to get stuck with scrap. So I think it is incumbent upon DOD to do a better job of modernizing the coding system and the situations in which they're going to advertise this equipment.

They're my two.

Ms. FISCHER. I agree 100 percent with the concern over data reliability and the first step being to get accurate data in the system because that would impair the reutilization process from the very beginning.

In addition, I have a concern about an interim solution. The integrated systems effort is targeted for completion in July 2009 if it

doesn't slip from that. So there is another 4 years or so that we could be wasting a couple hundred million dollars a year.

And something as simple as coming up with a way to list NSNs that are being purchased as well as NSNs that are flowing into the excess property process and being able to match those up——

Mr. SHAYS. And NSNs are national stock numbers?

Ms. FISCHER. National stock numbers. Yes. They identify like items, you know, standard-use items so you know what it is.

I am concerned, that they need to come up with a workable interim process for matching that up so that DRMOs, when they get something in a condition, know if that is still being purchased during that fiscal year. And they can let the DLA supply center know they have those items so they don't turn around and purchase the same items.

Mr. RHODES. My No. 1 concern, of course, would be the data reliability because all of these things are supposed to be junk. We bought junk. Well, it is not junk. It is all good.

Mr. SHAYS. I want to clarify. When you say all of them should be junked, no, you have certain excess material that is excess. It is not necessarily junk. Are you saying all of these you bought were told were junk, were labeled as junk.

Mr. RHODES. Right. Yes, this was all garbage.

Mr. SHAYS. Define junk and garbage to me. I'm sorry.

Mr. RHODES. It is considered unserviceable. It is considered——

Mr. KUTZ. In the system, it is recorded as unserviceable.

Mr. SHAYS. Every one of these items?

Mr. RHODES. Every one of these items: Those sterilized medical supplies in packages that have never been opened, those circuit cards that were in sealed containers, that power supply that was sealed up, that suction apparatus if we break the seal on the pad, it will no longer be sterile. But right now, it is considered sterile until you break the seal. All this, these unused boots, this unused gas can.

Mr. SHAYS. Well then how would they have—never mind.

Mr. RHODES. The point that I would add in to the data reliability, which is actually a function of the other recommendations had that have been made, goes back to earlier recommendations that we have made about understanding the value of the equipment. And I don't mean dollars and cents. I'm talking about, what does this mean? Who can use this?

Part of that is tied into, somebody's already buying it. But I can't, I can't understand how I in the GAO am able to buy a critical shortage item, even if it is labeled as junk.

How do I get a critical shortage item, one that I can't use? And the other is, it is a critical shortage item that someone else can use.

Mr. SHAYS. Well, having been a Member of Congress for 18 years and doing oversight for as long as I have, and as I get older, I get a little more impatient.

If you were making a recommendation to the panel that followed to be a part of a story of success given what you think are the most important issues, what would be your advice? And then we will go to the next panel.

Mr. Kutz leaned to you, Mr. Ryan, because he doesn't know what he was going to say. You're allowed to laugh, Mr. Kutz. That was my best attempt to be funny today.

Mr. Ryan.

Mr. RYAN. For the next panel that follows, I'm not really sure what you say to them. I think they're in a culture that needs to be changed. I think they're fighting an uphill battle with trying to live in today's modern economic world. They're also in an area where we as society trust people to do the right thing.

Some people have a tendency to take advantage of that trust. From my perspective, from the law enforcement perspective, that is what I'm looking at. I'm looking at, how does someone compromise a system to get ahead? And because there are so many people involved in the process and the trust factor from point A to point B to point C must be there, that is something that they have to live with at that level.

So I don't know what this panel can do at that beginning level to make this happen except have more accountability maybe for their managers. And that would be the point that I have to them.

Mr. SHAYS. OK, thank you.

Mr. Kutz.

Mr. KUTZ. I would say again hearings like this are very good to hold people accountable. It helps sharpen their focus on what needs to be done to fix problems, and they have to study up to be ready to face questions and be prepared to answer them. And these are tough questions. And they are going to be difficult to answer. But as I've said, DOD has some of the very best people I have dealt with in the Federal Government. And I know they have tried their best, and they do many things well at DOD. And it's always been a very ironic situation or difficult situation to understand how we can have cruise missiles that can strike within a certain distance in Baghdad, and we can't deal with some of these business systems. It is just very hard. We have talked about this before, how hard it is to understand how you can have that dichotomy.

Mr. SHAYS. Fair enough.

Ms. Fischer.

Ms. FISCHER. Of course, I agree with what has been said. I think the issue, as they move forward, because they agree with our recommendations—they recognize their process, improvements needed and systems improvements and human capital issues to deal with. But I think as they move forward, oversight and accountability is key to keep moving in the direction they need to move to solve this problem.

Mr. SHAYS. Thank you.

Mr. RHODES. I would say, build the hard linkage between the acquisition system and the excess property system so that you don't—each one locks the other one out relative to an item. Obviously, that requires the data reliability and the internal controls to be very strong. But until and unless they get to the point where I can't buy a gasoline burner unit because there is one sitting over in the warehouse or I can't buy all these boots, because they're sitting in the warehouse—I mean, if you were Wal-Mart, Wal-Mart doesn't do that.

So it is not impossible.

RiteAid doesn't do it. All these places don't buy stuff they don't need, because they already have it. So, OK, there is a margin. We all understand that. But there is no lockout system currently. There is no tie between acquisition and excess.

Mr. SHAYS. Thank you. Is there any question that we should have asked that we didn't ask that you want to put on the record? And that is a serious question.

Is there something that you thought of and if there is a question that you wanted me to ask, so you don't have to volunteer it, because you want to say you were asked it, just assume I asked it.

Mr. KUTZ. I want to followup on the last hearing you had on the biological equipment and the chem-bio suits. We did not see anything of those going out the door since your last hearing. So that was a very positive from the hearing you had a little over a year ago.

Mr. SHAYS. Thank you all. You have done a yeoman's work, and I know that you appreciate the cooperation you got from DOD. And I know that they appreciate your giving concrete recommendations besides just exposing what is not working.

So thank you for your service. And we will get to our next panel.

Let me welcome Alan F. Estevez, Assistant Deputy Under Secretary of Defense, Supply Chain Integration, Department of Defense; Major General Daniel Mongeon.

Am I saying that correctly, sir?

General MONGEON. Mongeon, sir.

Mr. SHAYS. Pardon me, Mongeon. I'm sorry.

And Colonel Patrick E. O'Donnell, Commander, Defense Reutilization and Marketing Service.

Thank you very much.

If you would raise your right hands.

[Witnesses sworn.]

Mr. SHAYS. Let me say from the outset that I know that all of you are very capable, and very dedicated, and we are blessed to have your service to our country. And I think you're in charge of something that is a mammoth undertaking.

I will just, before you make your testimony, say, in asking a question of our previous panel, what they would recommend and the challenges, I think there is a culture, I accept in a very strong way that there is a culture in government that requires you to be a good team player. And sometimes, being a good team player, in my judgment, impels people who testify before a committee to understate the task, to not want to blame someone else, to take the hit, be a good soldier. And I think that sometimes impedes our capability to get this done.

And so what I request is really a candid conversation about the tasks that you're encountering, the challenges you face, the lack of resources that you may have in some cases, the mistakes that were made, that have been made, whether by you or people before you.

Not with the intention of throwing stones, but just to help us know how we can break through this thing, because it is, it is very serious. I would like to know where you think the progress is, but I'll be very up front with you in saying that I don't see the progress. I think this is a record that is just going around saying the same thing.

That is the way I feel. And I do appreciate each and every one of you. And I know that you are doing a job I wouldn't want to do because I don't think I could do it.

So, why don't we start.

General—Mr. Estevez, am I saying your name correctly?

Mr. ESTEVEZ. Estevez, yes, sir.

Mr. SHAYS. Let me just say, and I will throw stones at someone else. I always ask my staff how to pronounce names. And the last two hearings, they've gotten one name wrong each time. And they've had me practice the wrong way to say it. So I no longer ask them with much faith.

STATEMENTS OF ALAN F. ESTEVEZ, ASSISTANT DEPUTY UNDER SECRETARY OF DEFENSE (SUPPLY CHAIN INTEGRATION), DEPARTMENT OF DEFENSE; MAJOR GENERAL DANIEL MONGEON, DIRECTOR FOR LOGISTICS OPERATIONS, DEFENSE LOGISTICS AGENCY; AND COLONEL PATRICK E. O'DONNELL, COMMANDER, DEFENSE REUTILIZATION AND MARKETING SERVICE, DEPARTMENT OF DEFENSE

STATEMENT OF ALAN F. ESTEVEZ

Mr. ESTEVEZ. Thank you, Chairman Shays. And thank you for the opportunity to appear before you to discuss the Department's excess property systems.

I'm grateful for the opportunity to provide the Department's views of the Government Accountability draft report, DOD Excess Property: Management Control Breakdowns Result in Substantial Waste and Inefficiency.

Mr. SHAYS. I'm going to ask you to move the mic a little closer.

Mr. ESTEVEZ. Yes, sir. My written statement, which I provided for the record, captures the number of the solutions we were implementing to improve the return supply chain as it applies to reutilization and disposal.

Before I summarize a few key efforts that we have underway, I wish to commend the Government Accountability Office and specifically the audit team for the positive recommendations contained in the report. The Department is working to make those improvements in our excess property operations a reality.

However, we are confident that our published policies regarding the Defense Reutilization and Marketing System across the system are sound. DOD policy states that material available in the disposition system will be used to the extent feasible to prevent buying and disposing of the same material simultaneously. While the return supply chain is the subject of this hearing, the return process is only a part of the supply chains that operate in the Department of Defense. The return process must be examined in the context of these DOD supply chain processes.

Today, the Department's energies are focused on the front end of the supply chain where we have the greatest impact in supporting our forces. That is getting the warfighter what he or she needs as quickly as possible. Making sure that the right item is available causes us to stock inventory and safety stock worldwide, such as parts for airplanes that first flew in the 1950's, to leading-edge electronics and medical devices.

I would like to highlight some of our successes in balancing support for the warfighter with efficient management of our resources over the last 3 years. We are supporting a deployed weapon systems quickly and effectively achieving 30 to 40 percent increases in material availability, a 70 to 80 percent reduction in lead times, and historically high levels of readiness for systems deployed in Iraq today, mostly through the use of performance-based logistics contracts.

Material availability has increased for those items which the Department manages across the key supply chains that support weapon systems, commodity items and our deployed forces.

Today, material availability for the Defense Logistics Agency is 88 percent, versus a target of 85 percent, and backorders has hit a historic low in March 2004.

Through aggressive partnering with industry, DLA's cost recovery rate, as seen on the chart on the right, entitled DOD-DLA Cost Recovery Rates, are declining and are projected to continue this downward trend.

Our inventory has decreased from a high of over $100 billion in the 1990's to slightly over $70 billion today, even with increased operations. The bottom line, we are improving all aspects of our inventory management process. The impact can be seen in the increasing levels of support provided to the warfighter. For example, I brought a chart that shows that we are decreasing Air Force non mission-capable rates by reducing backorders which are down 55 percent for Air Force items in the past 4 years. There are similar results for naval aviation as well.

The Department also has numerous initiatives under way to increase support levels to the warfighter that will also reduce obsolete and excess inventory. For example, readiness-based sparing uses advanced information technology to make better sparing decisions and allocate our inventory investment to best support readiness.

We have established commodity teams at the services and Department level to work with our supply base to reduce lead times and improve quality which will reduce the amount of safety stock we carry.

We continue to push forward with continuous process improvement and Lean/Six Sigma across the Department. We also have significant efforts underway to upgrade and integrate our logistics systems.

In the areas addressed by the report, our performance is comparable to commercial firms who consider excess and obsolete write-offs the necessary cost of satisfying customers. The audit pointed out that over $2.2 billion of items in A condition—those are serviceable items that are new, used repaired or reconditioned—was reported to disposal as excess for fiscal year 2002 and fiscal year 2003. The reserve actually represents 1.65 percent of our average inventory values for those years, which is comparable to industry figures. In most large companies, inventory reserves ranged from 2 to 4 percent depending on the industry, and we do well in comparison considering the challenging environment we work in.

The report stated that we had $156 million per year in material losses. At 1 percent of the Defense Reutilization and Marketing

Systems total volume, this is less than our commercial counterparts, as you see in the third chart.

However, we realize there is much room for improvement, even though our excess property performance benchmarks well against industry.

Let me highlight those actions I believe can better result in our reutilization supply chain. I had asked the military services and the Defense Logistics Agency to evaluate their training materials and practices so we can better assess root causes of the various documentation errors addressed by GAO. We will review the current processes and procedures to determine if there are opportunities for tighter controls and capture of information at point of return which will enable DMRS to better categorize inventory for potential reutilization.

We are also investigating whether to create new condition codes that will allow us to track condition code A items that are obsolete.

In addition, one way we are addressing GAO's finding that we purchase at least $400 million of identical items in fiscal year 2002 and 2003 by using available excess items in A condition is by linking DLA and service systems with our reutilization system as they undergo modernization.

Each of these actions is a step toward improvement in the Department. I expect that the synergy of all of them together will go a long way toward addressing the GAO report's recommendations, improve our performance and, most important of all, enhance our support to our warfighters.

Thank you for the opportunity to testify before the committee. I'd be happy to answer any questions.

[The prepared statement of Mr. Estevez follows:]

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TESTIMONY OF

ALAN ESTEVEZ

ASSISTANT DEPUTY UNDER SECRETARY OF DEFENSE

SUPPLY CHAIN INTEGRATION

BEFORE

SUBCOMMITTEE ON NATIONAL SECURITY, EMERGING THREATS, AND

INTERNATIONAL RELATIONS

OF THE

HOUSE COMMITTEE ON GOVERNMENT REFORM

June 7, 2005

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Overview of the Department of Defense

Excess Property Systems

Mr. Alan Estevez
Assistant Deputy Under Secretary of Defense
Supply Chain Integration

Chairman Shays, Congressman Kucinich, and Members of the Committee:

Thank you for the opportunity to appear before you and discuss the Department's Excess Property Systems. I am Alan Estevez, Assistant Deputy Under Secretary of Defense for Supply Chain Integration. In my position, I am responsible for developing Supply Chain Materiel Management Policy in the Department of Defense (DoD), which includes policy on reutilization of excess assets. The Defense Reutilization and Marketing Service (DRMS), a part of the Defense Logistics Agency (DLA), and the Military Services are charged with implementing and executing our policy.

I appreciate the opportunity to provide our views of the Government Accountability Office (GAO) draft report, *DoD Excess Property: Management Control Breakdowns Result in Substantial Waste and Inefficiency*. I will discuss the solutions we are implementing to improve the Return supply chain as it applies to reutilization and disposal.

Before we do that, I wish to commend the GAO audit team for the positive recommendations contained in the report. I appreciate any assistance that helps us improve support to our forces. I also appreciate the opportunity to tell you what the Department has done and what the Department is doing to improve our processes. We

are actively engaged in making the recommendations reality and are working to improve how we buy, position, and manage inventory, ensuring our warfighters have what they need to fight and win the global war on terrorism.

While this particular report focuses primarily on the Return portion of the supply chain, it is only a small, but significant portion, of the Department's logistics mission. All supply chains have three primary ingredients: people, processes, and technology. Ideally, we want all three aspects of this supply chain to be in perfect balance. During the course of my testimony, I will discuss what we are doing to address all three of these enablers as they relate to disposal and reutilization. The return supply chain is truly dependent on the integration of these three factors.

While the Return supply chain is the subject of this hearing, the return process is only a part of the three supply chains that operate in DoD; the return process must be examined in the context of these DoD supply chain processes. The first supply process supports complex weapons systems, the second is for commercially available materiel such as petroleum, food, construction materiel and medical supplies, and the third supply chain supports our deployed troops in hostile and dangerous environments. Each of these supply chains has its own challenges in terms of the reutilization and disposal process.

The bulk of the Department's energies are focused on the front end of the supply chain where it has the greatest impact in supporting our forces, that is, *getting the warfighter what he or she needs before they ask for an item*. That is and must be my primary focus.

Policy Guidance is Sound

However, we do not take lightly our responsibility to monitor the Return process and make long lasting improvements. To that end, we need to implement the recommendations as outlined in the GAO Audit Report. The report pointed out that over $2.2 billion of items in 'A' condition was reported to disposal as excess for FY 2002 and FY 2003. While that seems like a lot, our results actually represents 1.65% of our average inventory value in FY 2002 and 2003, which is comparable to industry figures. In most large companies, inventory reserves range between 2 and 4 % depending on industry, and we do well in comparison considering our challenges. However, our primary focus should not be on how much we made on the re-sale of these items; the important point is getting the right items to the warfighters when they need them, while simultaneously providing optimal return on the investment of the American public.

While there is room for improvement, we are confident that our published policies regarding DRMS across the Department are sound. DoD policy states that material available in the disposition system will be used to the extent feasible, to prevent buying and disposing of the same materiel simultaneously. At the same time, under Title X authority (organize, train, and equip), the Services as well as DLA are responsible to ensure that they are following those regulations, instructions, and manuals as they go about their daily work.

Inventory Management at DoD

I think it would be useful if we spent some time discussing how we see the inventory management side of the business. DoD Logistics activities do a good job of

getting things to where they need to be given the challenges of our operational environment, and we are making significant improvements in that area. The logistical support of operational readiness for the war fighter is complex. Inventory levels for more than 5 million parts are set to maximize readiness within budget constraints.

The Services and DLA have made substantial investments of human resources in systems designed to determine the allowances and stocking levels required to support a given operational baseline. Our inventory levels reflect the recommendations of these systems and models as to the appropriate quantity of inventory required to support war fighter readiness and weapons system availability, given our current business practices. Purposefully, our models drive us to hold levels of materiel in support of a high level of readiness, which we optimize by appropriate use of safety stock and buffers. The assumptions in most models are conservative, resulting in higher levels of safety stock for key weapons systems than a commercial enterprise might accept. We are striving to improve our business practices that support weapons systems readiness and, of course, we will update our models accordingly.

Our approach to safety stock reflects the difference between the cost of a stock out in a commercial enterprise, and the cost of a back order for the military. A stock out in the commercial world results in the lost of profit from a foregone sale, and potential customer dissatisfaction. A stock out on a weapons system means a plane not available for mission support. Thus, the calculus for setting inventory levels drives us to set higher safety stock levels.

As previously noted, we face challenges in setting inventory levels not normally experienced in industry. For example, we hold $7.4 billion in secondary item war reserve materiel, particularly for items which have significantly higher usage in contingencies and wartime. If that scenario does not materialize, and their usefulness passes, they would be turned into the reutilization process. In addition, some of these items such as medical items have limited shelf life, while others are rendered obsolete by technical progress. All of these factors contribute to our obsolescence and scrap rates, and drive lower recovery rates from the sale of DoD excess materiel than in the commercial world.

We also operate in a challenging and diverse environment with the three major supply chains as previously described. We support a range of weapons platforms, some of which have been in operation for many years. For example, the B-52 made its first flight in 1952, and is still flying. Many of the parts for these platforms are no longer made, and we have made end of life cycle buys to ensure operational availability of the weapons platform. When a technological upgrade is made to the platform, these parts may be rendered obsolete and would then be transferred to DRMS.

On the other end of the spectrum, we want to ensure that our soldiers, sailors, airman and marines have the best technology available in areas of great technological advances, including avionics, communications, and medical equipment. In such areas as personal armor, radio communications, medical devices, and battlefield C^3I, technology advances they have rendered previous devices obsolete and of little market value. On that same B-52, designed over 50 years ago, we are using state of the art electronics capable of delivering ordinance on target in ways that were unimaginable when the

airframe was developed. Therefore, to fulfill our mission we need to provide parts that are both very old and state of the art. We need to manage inventory to meet both needs.

Comparison to Industry

Any organization that uses inventory to meet demand will have write-offs and obsolete inventory. The Department's write-offs of $1.05 billion per year is 1.65 % of total inventory averaged at year end ($63 billion is 2002, $67 billion in 2003). It is difficult to compare the DoD experience to any one commercial industry, because we are a combination of industries; high tech, aerospace, automotive and many other supply commodities. The comparison is even harder to make because we value our inventory at latest acquisition cost, not its market value. If we normalized our write-off percentages to commercial standards, our excess and obsolete percentages would be even lower.
Let me give you a couple of examples from our commercial counterparts. The average car dealer's parts inventory will have 20% defined as excess (more than one year's usage), and 20% as slow moving (more than six months supply). As you read the financial news, you'll see companies announcing large write-downs in inventory value. The most striking was Cisco, the widely admired provider of networking equipment, which wrote off $2.25 billion of inventory, or 20% of their cost of sales for the year in 2001.

The report also points out that DRMS was unable to account for $466 million of inventory over three years. Compared to $31 billion turned over to DRMS over the two year audit period, this is 1.0% of the total volume handled. While there are differences in our business models, a variety of retail industries, including clothing, convenience and

electronics stores, will show that "shrink," as this type of loss is called, averages between 1.7% and 1.9% per year. However, we are focused on making our results much better.

How are we Doing?

Our performance in supporting the warfighter's requirements is good, but will always need improvement. Operational availability and fill rates, two indicators of the performance of the Department's supply chain, are high and improving while operating costs are decreasing.

1. Supporting deployed weapons systems quickly and effectively. We are achieving 30 to 40 percent increases in materiel availability, a 70 to 80 percent reduction in lead times, and historically high readiness levels for systems deployed in Iraq today. Part of this improvement is due to our Performance Based Logistics (PBL) strategy, in which we work with suppliers of key systems to buy performance, not piece parts. We have over 100 PBL contracts in place currently, and the impact on cost and operational availability for such platforms as the F/A-18 has been significant.
2. Increasing materiel availability. For those items which the Department manages, across the three key supply chains we discussed, we have expanded our level of responsiveness. Today, materiel availability for the Defense Logistics Agency is 88 percent (versus a target of 85 percent) and backorders hit a historic low in March 2004.

3. Cutting costs. Through aggressive partnering with industry, DLA's cost recovery rate -- the cost of the services DLA provides to military services as a percentage of DLA sales -- is at a historic low of 15 percent this year.

4. Decreasing inventory. Our inventory has decreased from a high of over $100 billion in the 1990's, to slightly over $70 billion today with increased operations.

There are numerous factors that affect these metrics, but, the bottom line is, we are improving all aspects of our inventory management process.

What are we Doing to Improve?

However, there is still more to do. The best approach to any problem is to prevent it before it occurs. In the case of disposal, the greatest opportunity lies in re-examining how we bring assets into the inventory, and in lowering the amount of this materiel purchased and maintained in the supply pipeline without impacting readiness. To that end, we have several programs underway to improve support levels to the warfighter that will reduce obsolete and excess inventory as well:

Readiness Based Sparing (RBS) is a methodology to enhance equipment readiness by applying advance mathematical modeling techniques to setting inventory levels. This initiative will leverage the work the Services and DLA have already done in RBS by using newer technology and off the shelf software. Organizations which have implemented RBS have seen an increase in service levels as similar or lower levels of investment in inventory, and we expect similar results across the Department.

Commodity Management is a strategy to address long lead times, and uncertainty of supply drive higher inventory safety stock. There are several commodity teams across the Services currently, doing excellent work in rationalizing our procurement and supply chain management in areas critical to the warfighter such as jet engines, Auxiliary Power Units, and other key commodities. DoD has also established teams to look at our purchase of services such as telecommunications and temporary help at the Department level. Since our true leverage across the Department comes from looking at our spending as a whole, DoD has two cross-Service commodity teams currently underway, tasked with understanding the entire Department's usage patterns and requirements, and the capabilities of the supply base in that commodity. Based on the findings from these initial Department level teams, we will determine how to best implement commodity management across the Department. A comprehensive commodity management approach will allow us, among other benefits, to identify strategies to diminish lead times and deal with suppliers with a proven track record for delivery and quality, thus decreasing requirements for safety stock.

Continuous improvement. The Departments is actively engaged in Lean/Six Sigma programs to drive process improvement, and have already seen the results in NAVAIR, the F-15 program and other platforms. Lean will lead to lower inventories, and processes which are more capable. As a result, we will see shorter cycle times, and less buffer stock to cover demand uncertainty over the purchase lead time.

Improved asset visibility. There are currently has significant efforts across the Department to upgrade and integrate logistics systems. This will lead to the ability to integrate purchasing systems and reutilization systems Department-wide. Integrated systems, built on modern technology, will make it easier to give item managers visibility into DRMS Automated Information System (DAISY) and other reutilization systems, allowing them to check for available excess parts before placing new orders. Likewise, RFID implementation will also help manage our inventory.

As representatives of DLA will describe in their testimony, DLA will modernize the disposal information process over the next few years, incorporating it into their Enterprise Resource Planning system.

We will continue to prioritize our efforts towards improving readiness. The primary mission of our logistics enterprise is to ensure the warfighter has the materiel to fight and win wars, and all of our programs and initiatives have this as a primary objective.

We Can Still do Better

Major General Mongeon will address many of the specifics of what DRMS is doing to increase its effectiveness. However, I will focus on some of the actions which we believe can lead to better results in our reutilization supply chain. These are:

1. I have asked the Military Services and the Defense Logistics Agency to evaluate their training materials and practices so we can better assess the root causes of the various documentation errors addressed by GAO. The Services and DLA are in

the early process of the assessment and will respond with any and all actions taken or planned. Once completed, I will ask the DoD Inspector General to follow-up and let me know how the military Services and DLA are progressing. Upon review of their assessments and the results of an IG look, we will re-evaluate our policies.

2. We are also investigating whether to create a new condition code that will allow us to track condition code "A" items (serviceable items that are new, used, repaired, or reconditioned materiel) that are obsolete. However, we need to be careful in assigning that designation, because if we mark something obsolete none of the Service customers are likely to accept the item for reutilization. The audit team found a number of condition code "A" items that although useable, were identified as obsolete for the application. As stated previously, it is not unusual for DoD to end up with a number of "new and unused parts" still in inventory, when an engineering change order or upgrade requires the installation of a new part in an aircraft or tank to correct some design problem or to make an improvement in performance.
3. We will review the current process and procedures for turn-ins to determine if there are opportunities for tighter controls and capture of information at point of return which will enable DRMS to better categorize its inventory for potential reutilization.
4. Additionally, the GAO report cited that the Department purchased at least $400 million of identical items during FY 2002 and 2003 and it reported we should have

used available excess items in A condition. Assets in DRMS will be reviewed by inventory managers to ensure DRMS does not have like items in stock. DLA plans to ensure visibility of excess inventory across the Department by linking the Reutilization Management System (RMS) to the modernized component logistics systems, as part of the DoD logistics systems modernization effort. Since January 2000, DoD has focused on the modernization of information systems to support modern supply chain practices and to improve department-wide financial accountability. The task remains challenging both in integrating all logistics information into logistics processes within each of the Military Services and the Defense Logistics Agency and linking these systems across Services.

Conclusion

In conclusion, my primary objective is to support the warfighters, while carefully considering the interest of the taxpayers. Having said that, our focus from a policy perspective is on our two customers. Our first focus in on the soldiers, sailors, airmen, and marines, who are out on the front line defending our country. We need to get them the best equipment and supplies that permit them to get their job done in the safest way possible. And second the taxpayer, who is paying the bill for the defense of the nation. Efficient and effective reutilization is a key component in serving both groups, and I've outlined how we plan to improve our reutilization and disposal practices by implementing the GAO's recommendations, and by continuing the initiatives we already underway to improve our end to end supply chain.

The DoD logistics enterprise is a $129 billion business. Our investment in inventory exceeds $70 billion. We will continue to look for opportunities to optimize our resources and improve operational availability. We will focus on implementing initiatives to achieve greatest return in improving cost-effective support to the warfighter, and continue to evaluate our processes to ensure that our men and women in harm's way have what they need when they need it to fight and win wars.

In closing Mr. Chairman, thank you for the opportunity to testify before the Committee about our Excess Property Systems. I would be happy to answer any questions you and the Members of the Committee may have.

Mr. SHAYS. Thank you, Mr. Estevez.

General Mongeon.

STATEMENT OF MAJOR GENERAL DANIEL MONGEON

General MONGEON. Good afternoon, Mr. Chairman, and distinguished members of the subcommittee. I am Major General Dan Mongeon, Director of Logistics Operations at the Defense Logistics Agency.

I appreciate the opportunity to discuss the findings of the March 2005 GAO report and inform of you the actions we have taken and will take to improve our excess reutilization program.

As the Director of Logistics Operations, I have staff responsibility for the procurement, management, storage and distribution of some 5 million line items of our military customers.

The primary mission of DLA is to provide the best possible logistics support to America's warfighters. In accomplishing this worldwide mission, DLA uses four major supply centers, five DLA service centers, a distribution system with 26 depots, and a reutilization and disposal service with 92 defense reutilization and marketing offices [DRMOs]. DLA operates in 48 States and 28 countries.

With me today is Colonel Pat O'Donnell, Commander of the Defense Reutilization and Marketing Service [DRMS].

Today we are here to discuss the economy and efficiencies of DOD's excess property reutilization program.

DRMS has operational responsibility for the reutilization program and accomplishes this mission at 92 locations throughout the United States and in 15 foreign countries.

Mr. Chairman, we concur with the recommendations of the GAO report. We recognize the issues identified in the GAO report and fully understand the importance of ensuring DOD has a viable reutilization program.

The recommendations agree with a series of actions we had already initiated to increase management oversight and improve inventory management and property accountability of excess material. These actions include increased senior leadership involvement to monitor adherence with policy, guidelines and performance standards and quarterly progress briefings to the DLA director.

We have also established a compliance assessment program geared toward policy oversight and monitoring the performance of DLA's reutilization and marketing program. We concur with the GAO conclusion that it is critical that services and DRMS ensure the proper assignment of condition codes.

To address this issue, the Assistant Deputy Undersecretary of Defense for Supply Chain Integration directed the military services and DLA to review their procedures, provide accurate excess property return and documentation, and establish appropriate accountability mechanisms for the disposal of excess and surplus properties.

To assist in this effort, I have directed the DRMS commander to work closely with the military services to improve training and awareness of the impact of inaccurate data. DRMS is developing property accounting courses for employees and supervisors as well as reviewing and upgrading its Web-based training tools for the services.

GAO correctly recognizes deficiencies in our current automated systems and their impact on the concurrent purchase and disposal issue. Long-term solutions lie in emerging automated systems. Since 2004, DRMS has been working closely with DLA's business systems modernization design team to enhance support of the two-fold mission of facilitating and reutilization of property in good condition and disposing of property DOD cannot use.

A modernized disposal system will provide DLA with the ability to better manage both the near-term and long-term disposal needs of DOD.

We agree with GAO's concerns regarding human capital shortages. DRMS has increased the use of contract employees, sent experienced personnel TDY to the most severely affected DRMOs and relocated some of our more experienced specialists. Also, the completion of the public-private A–76 competition will create an organizational structure that will consist of fewer DRMOs, ensure more efficient utilization of facilities and improve work load and management.

Mr. Chairman, DLA's top priority is to support the American warfighter. We are confident increased leadership, oversight, changes in policy and procedures, modern business systems, and investment in human capital and resources will allow us to better use our resources and ensure America's fighting forces remain the best equipped in the world.

I thank you, sir, and I would be happy to answer any questions.

[The prepared statement of General Mongeon follows:]

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NATIONAL SECURITY, EMERGING THREATS AND INTERNATIONAL RELATIONS SUBCOMMITTEE

Statement of
Major General Daniel G. Mongeon
Director, Logistics Operations
Defense Logistics Agency
Hearing before the National Security, Emerging Threats and International Relations Subcommittee
Of the
House Government Reform Committee
June 7, 2005

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Statement of

Major General Daniel G. Mongeon

Director, Logistics Operations

Defense Logistics Agency

Hearing Before the National Security, Emerging Threats and International Relations Subcommittee

of the

House Government Reform Committee

June 7, 2005

Good afternoon, Mr. Chairman, Mr. Kucinich, and distinguished members of the Subcommittee. I am Major General Daniel Mongeon, Director of Logistics Operations (J3) at the Defense Logistics Agency (DLA). I appreciate the opportunity to discuss the findings of the draft March 2005 Government Accountability Office (GAO) Report and inform you of the actions that we have taken and will take to improve our excess reutilization program. As the Director of Logistics Operations, I am responsible for the procurement, management, storage, and distribution of some 5 million line items for our military customers, various federal agencies, and allied forces. In accomplishing this worldwide mission, DLA uses four major supply centers, five DLA service centers, a distribution system with 26 depots, and a reutilization and disposal service with 92 Defense Reutilization and Marketing Offices (DRMOs) in 48 states and 28

countries. With me today, is Colonel Patrick O'Donnell, USA, Commander, Defense Reutilization and Marketing Service (DRMS).

The primary mission of the 22,000 men and women of DLA is to provide the best possible logistics support to America's Warfighters. Supporting the military services is DLA's number one priority, and our demonstrated ability to provide virtually every consumable item imaginable – food, fuel, medical supplies, clothing, weapons systems repair parts, and construction material to our forces in Afghanistan and Iraq is a testament to our talented and dedicated workforce. The challenges posed by the Global War on Terror are being met with innovative business practices and collaborative partnerships with OSD, the combatant commanders, the services, and industry. We are improving our end-to-end distribution and disposal processes, modernizing our infrastructure and technology, and streamlining our business practices to integrate the supply chains. The common threads of our efforts are people, processes and technology.

Today, however, I realize the Committee's focus is on the economy and efficiency of the Department of Defense (DOD) excess property reutilization program; in particular, the concurrent procurement and disposal of items that are serviceable but excess. The Defense Reutilization and Marketing Service (DRMS) is the executor of the reutilization program. DRMS is a one of a kind support command, responsible for providing hazardous material/waste disposal, demilitarization, reutilization or disposal of excess or damaged/destroyed equipment for each Combatant Command and Military Service. DRMS

accomplishes this mission at 92 locations in 15 foreign countries, multiple Theaters and throughout the United States to ensure effective and efficient support to the Warfighter.

The Government Accountability Office's March 2005 report to Congress identified issues with excess property inventory data; oversight, accountability, and physical control of excess property; outdated, non-integrated inventory systems; and training. Mr. Chairman, we recognize the issues identified in the GAO report and fully understand the importance of ensuring the Department of Defense has a viable reutilization program. DLA is committed to achieving a proactive and aggressive plan to combat management challenges in our reutilization program.

We concur with the recommendations of the GAO Report. The recommendations agree with a series of actions we had already initiated to increase management oversight and improve inventory management/property accountability of excess materiel. These actions include increased senior leadership involvement to monitor adherence with policy, guidelines and performance standards, and quarterly progress briefings to the DLA Director. We are developing performance metrics directly associated with this Audit to add to the Director's monthly management and corporate reviews of the Agency's performance. We have also established a Compliance Assessment Program geared towards policy oversight and monitoring the performance of DLA's reutilization and marketing program.

Additionally, DRMS will implement an aggressive inventory initiative program designed to: 1) identify the root causes of property accountability errors, 2) train employees 3) provide comprehensive formal training on policy, processes and systems and clean up the physical warehouse location balances 4) hold all employees accountable for their functional areas, 5) and correct the accountable transaction records.

In further response to the GAO findings, DRMS is implementing policy changes, is currently reviewing training, and has introduced new inspection protocols. On May 5, 2005, DRMS issued new guidance on counting excess property inventory that revises inspection protocols, ensuring actual quantities are accurately verified at receipt. DRMS will strictly monitor its excess property inventory accuracy via its Self-Assessment and Compliance Assistance Visits, with HQ DLA oversight through the DLA Director's corporate reviews.

Resolving the concurrent purchase/disposal dilemma requires a synchronized response by all of the players involved – OSD, the Services and DLA. We must begin by resolving the issue with the assignment of condition codes. We concur with the GAO report's conclusion that it is critical that the Services and DRMS ensure the proper assignment of condition codes. Failure to assign correct condition codes minimizes the efficiency and effectiveness of the Department's reutilization program. To address this issue, OSD directed the Military Services and DLA to review their procedures and provide accurate excess property turn-in documentation and establish appropriate accountability mechanisms for the disposal of excess/surplus property. To assist in this effort, I

directed the DRMS Commander to work closely with the Military Services to improve training and awareness of the impact of inaccurate data. DRMS is now partnering with the Defense Training Center (DTC) to develop in-depth property accounting courses for employees and supervisors that will provide long term solutions to this problem. In addition, DRMS is reviewing and updating its Web-based training tools for the Services, as well as its internal training for subordinate DRMO personnel – both employees and supervisors. Also, DRMS issued guidance to the DRMOs reminding them of their responsibility to challenge or change condition codes as outlined in DOD 4160.21-M Disposal Manual.

GAO correctly recognizes deficiencies in our current automated systems and their impact on the concurrent purchase and disposal issue. Today our supply inventory and excess property inventory management systems do not interface. Consequently, Item Managers are required to manually query the DRMS Automated Information System (DAISY) for information on the availability of serviceable excess property before initiating a purchasing action. This step is time-consuming, given the fact that DLA must rapidly process over 54,000 requisitions a day in order to meet the immediate needs of the Warfighters. Our long-term solutions lie in emerging systems; Both HQ DLA and DRMS have taken action to improve visibility of excess assets. DRMS expanded the use of existing Pre-receipt Want Lists, Automated Want Lists, and expedited processing property visibility on the DRMS website DLA is currently developing metrics to

further monitor the Inventory Control Point's utilization of DRMS' serviceable excess.

Since 2004, DRMS leadership has been working closely with DLA's Business Systems Modernization (BSM) Design Team to enhance support of the two-fold mission of facilitating the reutilization of property in good condition and disposing of property DOD cannot use.

DLA's BSM Release 2.2 functionality enables maximum use of DRMS' A1 condition excess. By proactively seeking to identify and recoup assets, DLA will maximize the utilization of assets at DRMS. Release 2.2 is planned to be operational in early Calendar Year 2006.

As DLA continues to modernize business processes and implement information technology solutions, the DRMS disposal processes will be incorporated into the BSM enterprise strategy. This disposal service initiative is known as the Reutilization Modernization Program (RMP). RMP will increase asset visibility and integrate the redistribution of excess property into the supply chain for maximum effectiveness. The overall RMP development/implementation timeframe is Fiscal Year 2006 – 2009.

BSM's Recoupment process will give DLA users the functionality to view serviceable excess property matches in an integrated and automated manner. Implementation of RMP will further align the recoupment processes within BSM. The goal of RMP is to fully incorporate DRMS' excess property data into BSM and use a single, Enterprise-wide integrated software backbone. This will give DLA users instantaneous visibility of all available DLA inventory, including DRMS

managed serviceable excess property. A modernized disposal system will provide DLA with the ability to better manage both the near-term and long-term disposal needs of DOD.

In response to GAO's concerns about adequately safeguarding excess property inventory from loss, theft, and damage, DRMS leadership has directed an increase in oversight of site security and improvement in reporting and tracking systems that will help distinguish bookkeeping errors from actual property losses. DRMS is working to upgrade physical security at DRMO sites where security risks exist. DRMS is also inspecting all government owned, contractor operated facilities and will evaluate the findings and invest in the appropriate upgrades for safeguarding property.

We agree with GAO's concerns regarding human capital shortages. A contributing factor was a leadership decision to conduct a public-private competition (A-76) for select distribution functions at the 68 DRMO's in the United States. This competition began in 2001 and is projected for completion this summer. During this period it was not prudent to hire permanent government employees during the competition. To mitigate personnel shortages, DRMS increased use of contract employees, sent experienced personnel TDY to the most severely affected DRMOs, and relocated some of our more seasoned specialists. The completion and award of the A-76 competition will result in an organizational and physical structure that will consist of fewer DRMOs, provide appropriate staffing levels, improve command, control and communication, ensure more efficient utilization of facilities, and improve workload management.

Mr. Chairman, DLA's top priority is to support the American Warfighter. To that end, we recognize that by resolving the issues identified by the GAO, the men and women on the frontlines of the Global War on Terrorism will be better served. We are committed to meeting the challenges laid out in this report. We are confident increased leadership oversight, changes in policy and procedure, modernized business systems, investment in human capital and resources, will allow us to better use our resources and ensure America's fighting forces remain the best equipped in the World.

Mr. SHAYS. Thank you, very much, General.

Colonel O'Donnell, sir, you're going to need to move the mic closer to you.

STATEMENT OF COLONEL PATRICK E. O'DONNELL

Colonel O'DONNELL. All right, sir, Mr. Chairman, and distinguished members of the subcommittee, I am Colonel Patrick O'Donnell, Commander of the Defense Reutilization and Marketing Service and the Defense Logistics Agency.

I appreciate this opportunity to address your concerns regarding the reutilization of DOD excess property in our efforts to improve inventory accountability in the efficient use of DOD assets.

DRMS is responsible for the execution of DOD policy on the reutilization, transfer, donation, sale and environmentally compliant disposition DOD excess property.

DRMS supports U.S. forces worldwide with personnel co-located with the military in Iraq, Kuwait and Afghanistan. We are committed to being good stewards of the property under our control and to ensuring compliance with DOD policies, guidelines and standards.

We have implemented many initiatives that are at the forefront of reverse logistics. This includes processing demilitarization-required property at dedicated facilities to ensure proper disposition, using innovative processes for disposing of excess electronic equipment, and partnering with a private sector firm to sell property on a shared proceeds basis.

In the past year, DRMS has implemented specific improvements to enhance reuse of excess assets within the Department, including providing DOD customers with additional online information and pre-receipt item visibility so that needed property can be redistributed quickly.

We are working to ensure our systems and process improvements will become compatible and interactive with military services.

The DOD reutilization system is trusted and regularly used by military service customers. And DRMS's reutilization and property disposal program performance measures demonstrate the quality of services provided.

In fiscal year 2004, DRMS return over 160,000 line items with an acquisition value in excess of $1 billion to DOD activities. Additionally, in April 2005, DLA Office of Operations Research and Resource Analysis study supports DRMS's own analysis that its overall inventory shrinkage rate in fiscal year 2004 due to losses is well below 1 percent.

DRMS recognizes its relocation of inventory accountability program can be improved. We are committed to correcting substandard performance and ensuring accountability while strengthening management controls to minimize such issues in the future. DRMS's actions to improve these programs include issuing a contract for commercial assistance in assessing and improving inventory data accuracy and developing additional internal audit capabilities, surveying significant generating activities to understand why property condition may be improperly classified, why local stock numbers are being used, and identifying barriers to using DRMS as a source of supply, meeting with DLA supply centers to

discuss constraints they face in using DRMS as a source of supply and to develop program metrics and goals.

DRMS is working with headquarters DLA to outline additional management controls and metrics to ensure proper inventory accountability and to synchronize the application of policy, oversight, education, training and program execution. We are also working to update our inventory accounting procedures, monitor inventory adjustments and losses, and reduce aging excess property and inventory and backlogs. DRMS spent $49 million in facilities upgrades in fiscal years 2000 through 2004 and plans to spend an additional $25 million in fiscal years 2005 through 2009.

Mr. Chairman and distinguished subcommittee members, we recognize the issues noted in the GAO report and are taking appropriate measures to ensure they are corrected.

DRMS stands ready to execute all policy and procedure changes that optimize the disposition of excess property. Thank you, Mr. Chairman, and I'm prepared to answer any of your questions.

[The prepared statement of Colonel O'Donnell follows:]

Statement of
Colonel Patrick O'Donnell
Commander, Defense Reutilization and Marketing Service
Defense Logistics Agency
Hearing before the National Security, Emerging Threats, and
International Relations Subcommittee of the House Government Reform Committee
June 7, 2005

Mr. Chairman and distinguished Members of the Subcommittee, I am Colonel Patrick O'Donnell, Commander of the Defense Reutilization and Marketing Service of the Defense Logistics Agency. I appreciate this opportunity to address your concerns regarding the reutilization of DoD excess property and our efforts to improve inventory accountability and the efficient use of DoD assets.

DRMS is responsible for the execution of DoD policy on the reutilization, transfer, donation, sale, and environmentally compliant disposition of DoD excess property. DRMS supports U.S. forces worldwide, with personnel co-located with the military in Iraq, Kuwait, and Afghanistan. We are committed to being good stewards of the property under our control and to ensuring compliance with DoD policies, guidelines and standards.

We have implemented many initiatives that are at the forefront of reverse logistics. This includes processing demilitarization-required property at dedicated facilities to ensure proper disposition, using innovative processes for disposing of excess electronic equipment, and partnering with a private sector firm to sell property on a shared proceeds basis.

In the past year, DRMS has implemented specific improvements to enhance reuse of excess assets within the Department, including providing DoD customers additional on-line item information and pre-receipt item visibility so needed property can be redistributed quickly. We are working to ensure our systems and process improvements will become compatible and interactive with the Military Services.

The DoD reutilization system is trusted and regularly used by its Military Service customers, and DRMS' reutilization and property disposal program performance measures demonstrate the quality of service provided. In Fiscal Year 2004, DRMS returned over 160,000 line items with an acquisition value of approximately $1.1 billion to DoD activities. Additionally, an April 2005, DLA Office of Operations Research and Resource Analysis study supports DRMS' analysis that its overall inventory shrinkage rate in Fiscal Year 2004 due to losses is well below 1%.

DRMS recognizes its reutilization and inventory accountability program can be improved. We are committed to correcting substandard performance and ensuring accountability, while strengthening management controls to minimize such issues in the future. DRMS' actions to improve these programs include:

- Issuing a contract for commercial assistance in assessing and improving inventory data accuracy and developing additional internal audit capabilities.
- Surveying significant generating activities to understand why property condition may be improperly classified, why local stock numbers are being used, and identifying barriers to using DRMS as a source of supply.

- Meeting with DLA Supply Centers to discuss constraints they face in using DRMS as a source of supply and to develop program metrics and goals.

DRMS is working with Headquarters DLA to outline additional management controls and metrics to ensure proper inventory accountability and to synchronize the application of policy, oversight, education, training and program execution. We are also working to update our inventory accounting procedures, monitor inventory adjustments and losses, and reduce aging excess property inventory and backlogs. DRMS spent $49 million in facility upgrades in Fiscal Years 2000-2004 and plans to spend an additional $25 million in Fiscal Years 2005-2009.

Mr. Chairman and distinguished subcommittee Members, we recognize the issues noted in the GAO report and are taking appropriate measures to ensure they are corrected. DRMS stands ready to execute all policy and procedure changes that optimize the disposition of DoD excess property.

Thank you, Mr. Chairman

Mr. SHAYS. Thank you all very, very much.

What is, in each of your judgments, the biggest challenge that you face?

Mr. ESTEVEZ. Interestingly enough, Mr. Chairman, I believe that the two issues raised by Mr. Kutz are the same two issues I'm going to talk about. One is training, and the second is the integration of our systems.

We have folks from military units turning in material most of the time that they no longer need so they want to get rid of it, turning it into folks at DRMS who are now expecting to make a judgment on the value of that material if it is improperly coded.

So it is important for us to ensure that the folks that are turning in that material are trained properly to understand the entire lifecycle of that material and the importance of that material across the Department. And it is important that our DRMS folks are trained to also make a judgment about that material and challenge as appropriate.

And in the commercial sector, turning in something to a retail outlet or a retail store, they send it back to someone to make those judgments.

Second, we have to have the systems integration so that, when our wholesale system goes out and looks and says, what do we need to buy in order to fulfill a military requirement that has come in from the field, that it is automatic that something that was turned in through our reutilization process is on the books. And we are working to do that. And in fact, in January 2006, DLA's new Enterprise Resource Planning System will be integrated with the DRMS system so that those items that are turned into DRMS will automatically, that are in class A condition, that are in good condition, will be moved back into the inventory.

General MONGEON. Sir, I would really echo those two comments. I think the training of both the services and also the DRMS personnel is absolutely key. And we have to be very vigilant in that area and continue to improve that training and make tools available to the services and to our employees so that they can improve the process.

In terms of the systems integration, again, I totally concur with that comment. And we do have a fix on the horizon. There is really a long-term and a short-term approach. The short-term approach is in fact linking of the current management system, inventory management system, with the business system modernization and, as was mentioned by Mr. Estevez, that comes on line in January 2006. So those two would be the two key areas.

The third one I would just comment on is the data validation. And we are working very diligently on that, in terms of improving our inventory accuracy and working a comprehensive program in terms of personnel training, inventory accuracy and accountability of our employees.

Mr. SHAYS. Thank you, General.

Colonel.

Colonel O'DONNELL. Sir, again, I think my comments would parallel those of Mr. Estevez and General Mongeon.

Certainly, data reliability is of critical importance to us in the disposal business. We make all of our business decisions about

what to do with property based on the information that we receive about the items that are turned in to us.

Certainly that relates to the aspect of training that has already been mentioned. And again, the importance of having the systems integration that supports not only the buying of the property, the use of property, and ultimately the disposition of property, will take us a long way to sort of resolving all these problem.

Mr. SHAYS. I would like to ask each of you, what you think the biggest success has been and your biggest failure. Not you personally, necessarily, but for the system.

Mr. ESTEVEZ. I'm going to address this across-the-broad system, not just the reutilization system. I think we are doing a pretty good job. We can do better. But we're doing a pretty good job in getting the warfighter what he needs.

We have decreased the time from moving high-priority shipments to our forces deployed in Operation Iraqi Freedom from about 30 days in shortly after the main operation ended to down to about 15 days today.

In order to do that, we may end up having bought more than we need, but that is important. Because it is more important to have a soldier, sailor, airman, marine being able to sustain himself and to have those weapons platforms operating and to have a plane flying, than it is to have it down.

Mr. SHAYS. I'm going to confirm that. And you can relate it to lots of different circumstances. You may invite guests to an event, and you can say, well, I'm going to have 30 people show up, but you buy for 40 because you don't want to have an undersupply. So I think it is a point that needs to be made. Sometimes we are going to have better excess supply than undersupply. That is OK.

Mr. ESTEVEZ. So we are doing fairly well today moving stuff to support our Armed Forces in the field.

On the reutilization side, I'll point out that we did reutilize about $400 million worth direct reutilization within the Department of Defense over the 3-year period and up to about $1 billion if you include some of those special program areas which are congressionally mandated and have the same rights as requisitioning material as Department of Defense agencies or units themselves. So we did over the period of time reutilize a good chunk of the material that came in.

Now, obviously, we do need to do better on some of the other areas. We should not be buying $400 million at the same time. And those areas that I addressed previously, I believe will go a long way toward fixing those.

Mr. SHAYS. So is your biggest failure the buying of $400 million that you shouldn't have been buying?

Mr. ESTEVEZ. I believe that buying concurrent with things that we are using in the inventory is our biggest failure.

Mr. SHAYS. And tell me why you think that is going to be reduced?

Mr. ESTEVEZ. That goes back two reasons, one goes back to, we need to train better so that they identify, but really, if you make those system interfaces that we discussed so that the buyer, who is processing numerous orders, doesn't have to think, it is an automatic link between his system that he is looking in to see what in-

ventory we have in the wholesale system and what is in our reutilization system is automatically linked, so that he doesn't think it is bought and it is on the books.

Mr. SHAYS. And that interface, though, that is nothing I see happening all that quickly. What part is being interfaced you say January.

Mr. ESTEVEZ. January 2006, will be an interface between DLA's system that they are fielding, their enterprise planning system called Business Modernization System, and the system that Colonel O'Donnell operates called Daisy.

Mr. SHAYS. It will begin, or it will be up and running fully implemented?

General MONGEON. It will be fully implemented. The design has already been worked out, has been completely designed, and now, as we go to the 2.2 roll-out of our business system modernization process, it will be implemented. And you will have that automatic link.

Mr. SHAYS. So, General, tell me the thing that you're most proud of or you consider the biggest success and what you think the biggest failure has been?

General MONGEON. I think the biggest success has been DLA's continued business process improvements. You heard some of those numbers as it related to our highest level of supply available in terms of supporting our warfighters, our lowest level of back orders, direct impact on readiness of our forces as well as reducing the cost, the overall cost, of operating the Defense Logistics Agency. And you've seen that on those charts.

In addition to that, our overall ability to work aggressively in terms of taking on inventory accountability. As recently as 2002, our adjustment rate was 19 percent.

Today, in second quarter of fiscal year 2005, that has been reduced down to less than 5 percent, 4.6 percent. So taking on very seriously recommendations made on inventory accountability and working that very hard.

Mr. SHAYS. Tell me again the percent of what? I'm sorry.

General MONGEON. These are adjustment to inventory. In 2002, for our distribution depots, our adjustments to inventory was running at 19 percent. Today, after some very aggressive inventory accountability measures, training, holding personnel accountable, that has been reduced down to, in this second quarter of fiscal year 2005, to less than 5 percent, specifically 4.6 percent.

In terms of improvements, where we could have improved better or faster, I think it is in business systems modernization. I think it is the linkage between, as you heard, or the integration of the systems, so that we get a higher correlation between what is being purchased and what is being turned in in condition code A.

We have moved very fast. But it would have been great if we could have moved even faster to accommodate that linkage.

Mr. SHAYS. So, OK, I don't want to minimize the failures. In other words, your recognition of the failures, and I don't want us to be like, I asked someone what their biggest failure was or their biggest liability when I was hiring them, and they said they were too friendly. I want to have a better sense of what you think your biggest disappointment, or maybe it is redundant, so give me your

second biggest disappointment. I want to have a sense that you have a sense of the failures.

General MONGEON. Well, I think in terms of what I just stated, sir, is in relationship to, as was stated by Mr. Estevez, was in relationship to the $400 million that were concurrent purchases. And I was relating that to our business systems modernization. If we were able to move faster on that, we potentially could have avoided the vast majority of that concurrent purchase.

Mr. SHAYS. But you think, do you think that actually gets resolved in just 6 months?

General MONGEON. In terms of linking the visibility of condition code A items that are turned in to the individuals, the inventory item managers that are purchasing that items, we will be able to link the two together. So he or she will be aware that those items are available, can look to see if they in fact are in condition code A and then make those issues from those items as opposed to turning them in as excess.

Mr. SHAYS. You are making, Mr. Estevez, Deputy Undersecretary, you were making a statement you turned a negative into a positive, and that may be very fair, but you basically said we wouldn't have known about the $400 million if we hadn't done what? I thought I was inferring from you that you were saying that even the fact that we—maybe someone else made that point—that we would have not have been able to have had any statistics on the $400 million had we not had something else in place. Am I, was that something I just invented from something you said?

Mr. ESTEVEZ. I'm struggling. Because I don't remember saying exactly that. But I did point out that was, in my view, our biggest failure. And as General Mongeon just alluded to, I view making that systems integration, it is one of the keys, it is probably the key to making that fix, but I do have to point out that the training has to be in place because you have to code it properly to enter it into the system. So it has to be turned in at condition code A, identified as condition code A and logged in to the reutilization system as condition code A for it to move up into the higher system as available for reuse.

Mr. SHAYS. Do we put bar codes on our products so that you just scan them in?

Mr. ESTEVEZ. Depending on the, you know if it comes in, its performing original package, it is going to have some kind of marking on it.

Mr. SHAYS. So you don't have to manually do it?

Mr. ESTEVEZ. If it is a weapons platform, if it is a part for a weapons system, it is going to have a part mark on it. Some today have none, that you have to code it in. We are moving so that you have to scan everything in. And we are also moving toward the use of radio frequency identification across our supply chain so that it becomes an automatic entry into our inventory systems.

Mr. SHAYS. Colonel, the thing you're the most happy about and the thing that troubles you the most.

Colonel O'DONNELL. Sir, I guess the thing that I'm most pleased with——

Mr. SHAYS. Move the mic just a little closer to you, sir.

Colonel O'DONNELL. I think the thing that I am most pleased with overall is the value that DRMS and Defense Reutilization Marketing Service brings to the Department in terms of its ability to execute a fairly wide range of complex tasks. As I indicated in my opening remarks, we're responsible for not only selling property and reutilizing it, making sure that it is used as effectively as possible, prior to it having to be demilitarized, and our role in the environmental compliance as it relates to DOD's hazardous waste and hazardous materials excess, but those are tough challenges.

And the men and women who make up DRMS do a yeoman's job in making those kinds of things happen day in and day out.

I think the area we struggle with the most, quite honestly, is our ability to keep our employees as well trained as we absolutely need to in light of changing regulation at the Federal level, within the Department, to give them the best rules and tools that we can in order to enable them to perform their daily tasks at a level that is consistent with what is expected of us.

Mr. SHAYS. So you say training is your biggest disappointment?

Colonel O'DONNELL. Yes, sir. Yes, sir.

Mr. SHAYS. Fair enough. Before I go to our professional staff, we breezed through these charts. And, they're very familiar to you but I don't know what is on the access and so, so just, if you would, and Mr. Secretary, start with the DLA cost recovery rates are declining.

Mr. ESTEVEZ. Simply. DLA works in a working capital fund. So they're funded through sales to the military services.

Mr. SHAYS. Right.

Mr. ESTEVEZ. Through the recovery costs of those sales.

So back in the 1992 timeframe, that cost recovery was up to about $33.

Mr. SHAYS. And the years are on your chart?

Mr. ESTEVEZ. Yes. As you can see, the cost recovery rates have been declining.

Mr. SHAYS. Define cost recovery rates to me. What is it?

Mr. ESTEVEZ. That is the cost above the actual purchase price of an item that DLA sells it to the military services; DLA's working capital funded.

Mr. SHAYS. Give me an example.

Mr. ESTEVEZ. If DLA buys a part for a helicopter at $10, they will sell it at now $11.50 rather than $20 some years ago. That is how DLA operations are funded, through an additional tack-on on top of the cost of the price to the service.

Mr. SHAYS. OK. I'm so sorry, but I'm not understanding the cost. I must be thinking of it in reverse.

Mr. ESTEVEZ. DLA buys from a vendor, from Boeing, Lockheed, whoever, at $10, and they'll sell it to the service at $12, to the Army at $12. The Army gets appropriated funds from the Congress to buy those items at that rate.

Mr. SHAYS. At $12.

Mr. ESTEVEZ. At $12. If DLA reduces the costs that it can charge in overhead——

Mr. SHAYS. So these are overhead costs?

Mr. ESTEVEZ. Yes, sir. These are overhead costs. So DLA is becoming more efficient, and then the service has more dollars to buy.

Mr. SHAYS. I didn't realize—these are basically overhead costs?

Mr. ESTEVEZ. Yes, sir.

Mr. SHAYS. And you're getting your overhead costs down?

Mr. ESTEVEZ. Yes, sir.

Mr. SHAYS. And we can assume these are fairly reliable statistics?

Mr. ESTEVEZ. Absolutely.

The second chart shows Air Force mission-capable rates, the correlation between mission-capable rates of weapons systems—and that is a generic across the Air Force, so it is not for a particular aircraft—and the reduction in back orders. So if I don't have an item on back order—in other words, you're waiting for the item because it is not in the inventory, and it is not available from the industrial base—I have weapons systems that are sitting idle. If I decrease the back orders and get that material out to the force, I am decreasing the amount of mission-capable rates of the weapons platforms. So I'm getting better utilization of the material that the Department has bought for use to defend the American people.

Mr. SHAYS. And the third one?

Mr. ESTEVEZ. And the third one shows industry averages, by year, of what the industry would call shrinkage, how much the industry loses. And that is not just in retail operations. That is across, you know, warehousing and, for specific industries, and of course, we are a mix of industries, but industry average is, as you can see, about 1.7 percent across the board, and in our DRMS, we are down to about 1 percent, and that relates on the $466 million. Now that is not to say that we want to live with having a 1 percent unaccountable rate. We of course want to have a zero unaccountable rate.

Mr. SHAYS. Yeah.

Let me just tell you how we will proceed, and I think this will be a good way.

General, you basically have said we can look in 6 months to some integration of systems, and it would seem to me and you said it will be online running, so I assume you'll start to process it in before. So if we had a hearing a year from now, will you all be in that same capacity a year from now or will we be dealing with different people?

General MONGEON. I will not be. No, sir.

Mr. ESTEVEZ. It is my plan to be, sir.

Mr. SHAYS. Fair enough. That's good.

Colonel.

Colonel O'DONNELL. No, sir. I will not then either.

Mr. SHAYS. That triggers the question, what is the amount of time that someone serves in a capacity like you're in General.

General MONGEON. Normally 2 years.

Mr. SHAYS. Colonel.

Colonel O'DONNELL. Two years sir.

Mr. SHAYS. Just, that is probably unfortunate, frankly, you know, but at any rate, your predecessors are going to either say, well, the General is right or he is wrong. Because we are going to

get you back here, or your replacements, in a year, and that hopefully we will have a good story to tell. Hopefully, we will have a good story to tell.

General, when would you be leaving? What is your——

General MONGEON. Sir, I'll be leaving around October of this year.

Mr. SHAYS. Well, we may have you be a duplicate witness here, so don't hide from us. We're going to have the professional staff ask a few questions. And what I would like GAO to do, and I appreciate your staying, I would like you to just, you know, at the end, just say the things that, just comment on what you've heard in this testimony.

Yes. OK.

Mr. CHASE. Either to the general or to Mr. Secretary Estevez. One of the previous witnesses, Mr. Rhodes, suggested an improvement might be linkage between the excess property system and the acquisition systems, so there was no—in a sense—put in a lockout system. Did you have any thoughts about his recommendation.

General MONGEON. Let me start out. Essentially that system modernization, that linkage between the inventory system that the DRMS is currently using, Daisy, linked to DSM, what that does is it identifies to the item manager that those items would be in condition code A, and that he should automatically put those in stock.

Now, there are criteria for that in terms of his—where his position is. But if he is going to buy it within the next 6 years, then it's going to automatically put it in stock.

Mr. CHASE. OK. Going back to the systems, then, you have indicated that January 2006 you expect completion. Now, in your response to GAO, in the recommendations regarding inventory management improvements, you mention something about full operational capability for the DRMS RMP will be realized in fiscal year 2009. Could you explain what that is, and tell us whether that can be implemented any sooner than fiscal year 2009?

General MONGEON. That is the long-term plan in terms of modification of the reutilization system; so that is coming on board after Business System Modernization. So that's the major integrated program for the Defense Logistics Agency, BSM. The long-term solution comes on with an implementation date of 2009, so it's a more comprehensive, more sophisticated capability. Pat might want to add something in addition to that.

So we have a near-term fix, which was mentioned by GAO as being very important, and we have a long-term fix, and the combination of those two give us where we think we need to be.

Mr. CHASE. What happens if the Business System Modernization program is delayed? They're still trying to count the number of systems they have on hand.

General MONGEON. We are in the process of rolling out our Business Systems Modernization as we speak. We have met every milestone, so that is going very successfully. We are integrating about 200 customers every month, 200,000 items. We are learning in that process, and right now that is a very successful program rollout. So we have a considerable amount of time under our belt right now, and we anticipate that success will continue throughout the final rollout of the Business System Modernization.

Mr. ESTEVEZ. Just to clarify there. DLA has one instance of a system that's being modernized, they're rolling out a resource planning solution. That is not the overall business management systems of the Department of Defense. That's their instance of it, and obviously that doesn't take into account all the finance systems in the Department or the logistics systems.

DLA's rollout, for what is a commercial product, is the largest rollout of that product, as is the Army-specific rollout. And these are products that are out in the commercial sector and regularly used.

Mr. CHASE. I'm curious. I don't understand how brand-new material, unused, new, "A" condition material can be scrapped or junked. Could you explain that? I'm not sure I understand how something new is scrapped or is junked.

Mr. ESTEVEZ. There's a number of reasons why.

We have the two issues; we have stuff that we're buying concurrently, and then we have other stuff that's in A condition that may be—I won't call it junk—that we either donate out to other agencies, or is used somewhere else in the Federal Government, or it could end up being sold. It has to do with what's the admission of the Department, what is the status of that item. It can be a new item that we potentially could have bought and now have a technological upgrade so we no longer need that. We no longer use the old body armor; we use the new body armor because it has better protective capabilities for our forces.

Mr. SHAYS. So what you're saying is if you have old body armor that's new, it's not that it's——

Mr. ESTEVEZ. That's correct. And there is—that applies across the board.

An upgrade in something, we want our forces to have the best that's available. And in certain instances, if it's a modernization of a weapons platform, then the old stuff is no longer needed even though it's still in new condition, because we just did a mod on the platform.

Mr. CHASE. Well, I understand the body armor example, but what about the tent example?

General MONGEON. I would say in terms of the tent example, it's one of those areas where it was the condition code; the condition code was marked condition code H. That is part of what we have all said is in fact a training issue, and we have to work very closely with the services and with our personnel to ensure that those items are coded correctly. That is an item that we are still buying, not in large quantities, but the fact of the matter is they in fact were condition-coded items turned in, and that we should be able to pick those up. And they should have been in condition code A, marked in condition code A, so that then would have had the visibility potentially as an example on a want list.

We have some automated processes, you can go to the Web; organizations have a want list. So let's say somebody needed those tents for reutilization. If it had been turned in in condition code A and it had been on their want list, it would have automatically linked up and they would have been able to get it.

So going back to what Mr. Estevez said, going back to what Colonel O'Donnell said, training and adherence to making sure that the proper condition code is marked on these items is very important.

Mr. CHASE. When did you implement the want list program?

Colonel O'DONNELL. Sir, the want lists have been in effect for over a year now. And it's a tool; again, a way of trying to enhance our overall reutilization program by giving our customers, across the spectrum of military organizations, the ability to tell DRMS the kinds of property they need and the types of quantities that they're looking for. They can come on our Web site, give us that product, which then is screened against our inventories for a prescribed period of time, hopefully with the expectation of fulfilling the requirements.

Mr. CHASE. OK. GAO raised the question of restricted items that they were able to obtain. Why isn't DLA able to restrict unnecessary purchases?

Colonel O'DONNELL. Let me go ahead and answer that one, sir.

NonDOD entities within the Federal Government can, in fact, acquire restricted property through a reutilization, or the RT program, reutilization and transformation and donation program, depending on where they fit in terms of eligibility.

The decision to release property which has some sort of restrictive characteristic rests with GSA, who has proponency for property utilization throughout the Federal Government, which would account for why GAO could use their DODAC to come in and requisition that property.

Mr. SHAYS. Could you just explain it? GSA, outside of DOD, doesn't have ownership of this; they have to give approval to another government agency to buy something from you?

Colonel O'DONNELL. They have to give, sir, approval for a nonDOD organization to withdraw property from DRMS that has a restrictive characteristic. Having said that, they are also obliged to tell that organization that they have to sign a statement that says you recognize that this item, for example, has a DRMO requirement and that you will abide by the tenets of that DRMO requirement when you, in turn, get ready to dispose of that property.

But GSA is the proponent, if you will, for property reutilization throughout the Federal Government, and they are delegated that responsibility for DOD down to the Defense Logistics Agency.

Mr. SHAYS. Is it your testimony that GAO would not have been able to buy that restricted property—excuse me, correction. I will say it just this way: Is it your statement that the only way GAO was to buy this restrictive property is because they were GAO, and that they would not have been able to buy it if they had tried to buy it privately?

Colonel O'DONNELL. That's correct, sir. Those items up on the podium there were requisitioned through DRMS, using a DODAC that had been assigned a Department of Defense activity address code that had been assigned to GAO, enabling them to acquire property from us.

Mr. CHASE. Colonel, could we move on to the point that the GAO made regarding the storage of material that was destroyed or weather damaged? They specifically said in their report, property was improperly stored outside for several months at the Huntsville

liquidation sales location and I guess was damaged due to the hurricane. Have you gotten a handle on how you could prevent that in the future?

Colonel O'DONNELL. Sir, the situation that was described in the GAO report with respect to our facility down in Huntsville has, in fact, been corrected. It was a—the result, rather, of a series of events that sort of cascaded upon themselves.

First and foremost was that the team that we had down at our sales partners office at Huntsville was unable to keep up with the volume of property that was coming to them in terms of their ability to sell it and to turn it over at a sufficiently rapid rate that would ensure that all the property they were receiving could, in fact, be stored inside. They made some decisions that particular management team at that particular site needed to be replaced, and they have, in fact, done that. We, DRMS, have put some additional manpower down at Huntsville to help monitor what is going on, not only within our sales partners operations, but how that all relates back to the flow of property from DLA depots.

As to the fact that we had property stored outside which ultimately was weather damaged, again, that was a function of there being more property in the pipeline than our sales partner could deal with based on the skills, I guess, and the ability of the team that they had on board at the time. Again, we've rectified that. We've worked with our sales partner, they have made some significant improvements in terms of the caliber of folks that they had down there. And the problem that existed at the time of the audit no longer exists.

Mr. CHASE. So I understand that was a private contractor that was responsible for that location?

Colonel O'DONNELL. For the sales operation co-located at our DRMO at Huntsville, AL, yes, sir, that is correct.

Mr. CHASE. Were we—or have we considered trying to recover some of the acquisition value for that material from the contractor? I mean was it—you know, was it something that he could have prevented that maybe we should try to recover?

Colonel O'DONNELL. In this instance, no, sir, I don't think that's the case at all. I mean, the fact is there was more property coming his way than he had the capability at the time to deal with. But by the same token, we had a responsibility to say there is more property in the pipeline, let's divert that to another location. Which ultimately we wound up doing to help solve that particular situation.

Mr. CHASE. Another point raised in the report was the issue of missing items, 72 chemical and biology protective suits, protective gloves, weather parka. Given the losses that GAO identified, what is DLA's criminal investigative agency doing to access the DRMO's security and vulnerability?

Colonel O'DONNELL. Sir, the DLA Criminal Investigative Agency routinely conducts criminal vulnerability assessments of our DRMOs. And I can't speak in this particular instance, but those inspections take place on a routine basis; they put a team of investigators down there, and they look at our operation from the standpoint of what process improvements do we need to make, what do we need to do in terms of improving physical security, the way we

handle property, the way we account for property. And we find those to be very, very useful tools.

General MONGEON. If I might just expand on that point. The JS list very specifically—and I think comments were made by GAO in terms of when they went on to look since the last time of the hearing when what was discussed, they found all those items being available. There have been very aggressive actions taken, and there is an organization called the Joint Service MBC Equipment Assessment Team. All of that equipment and MBC-related items now flow to those four sites. And in the past, a very avowed criticism that those items were in batch lots and they were coming in; and thus you did not have the direct accounting of those, because they might have said I turned in 50 suits, and there might be more pants than jackets, etc.; that process was ongoing during that investigation. We no longer accept batch lots. All of the items that are now turned in, JS lists, are reviewed at those sites. They make the determination if they are serviceable for reutilization.

In the last year, they have determined about $1.3 million worth is for reutilization; if it is not for reutilization in terms of being able to be used, then it is marked clearly for training. And if it is unserviceable, then it is turned in to be destroyed. I think that is one of the examples of where DRMS has taken and the services have taken the recommendations of the committee very seriously.

Mr. CHASE. That just raised another point. Have any more of the 250,000 BDOs turned up, the defective BDOs?

General MONGEON. Not to my knowledge. Not to my knowledge.

Mr. SHAYS. We're going to close up here. But let me be clear. From each of you, is there anything that GAO said—you've said what you've agreed with in the recommendations; is there anything in the testimony they gave today that you would take issue with or would choose to qualify? I mean, we qualified one—and I would like GAO to respond—that the restrictive items that they got, they were able to get not as private citizens but as a government agency. Still, they shouldn't have gotten it. What use did it have to them?

But is there anything else that you would have disagreed with what they said? And then I'll make the assumption that you agreed with what they said. I mean, you were here listening to some pretty hard stuff. Or any members, what I said, or anyone else said?

Mr. ESTEVEZ. With regard to what is called waste, the stuff that we no longer need that goes out to—and again, I'm not talking about things that we do concurrent buys on. If we no longer need it in the Department and we excess it and it is reutilized either by some of the congressional mandated agencies that have the same rights to the materials that the Department of Defense has, or if it goes out to first responders or States or some other people that review that, that's valid use of that; and, in fact, it's helpful to the American taxpayer in many instances, or State taxpayer as the case may be.

The other stuff that we no longer need that goes for sale through our government contractor, we believe we are getting the best price available. That goes for open auction. And we have two choices at that point. You can either not sell it and hold it, and there is a cost related for doing that; or you can get it off our books and off our

management control because we no longer need it, and get the best return on the dollar that we can get at that point.

So I'm not sure what—we keep hearing the pennies on the dollar point, but we are getting the best value that we can get through that open auction at that point, without holding that material for an undisclosed amount of time.

So I just want to characterize what is being called "waste," as we view if we no longer need it, we're getting the best return that we can possibly get on that.

Mr. SHAYS. OK. Colonel, anything that you would—Colonel, anything that you would want to take issue with or that you want to qualify that you heard from the previous panel or any Member of Congress?

Colonel O'DONNELL. Yes, sir. I think that Mr. Estevez has said the point that I would have made exceptionally well.

Mr. SHAYS. If I could have GAO just join, and this is not a debate—I'm sorry, General.

General MONGEON. I did have one comment, sir.

Mr. SHAYS. I'm sorry, I didn't mean to overlook you.

General MONGEON. The comment I would make is—and I use the gasoline burner unit as an example. While the gasoline burner unit is in condition code A, there is a modernization program going, and it happens to be called the modern burner unit. So as units are deploying, they are being fielded, the new item. And so while we have in fact sold a very small amount of these burners and buy a very small amount, we are in a transition program.

And I think what you find in a number of these programs, a number of these areas, that you're in a transition program. So the units that we're deploying, the forces that we're deploying, we're deploying with the modern burner unit, the replacement for that. That gasoline burner is still a condition code A item, but in fact it is not the most modern item.

With an example that was mentioned for the NSA computers, and just to embellish the point that Mr. Estevez made, in fact the LESO that was able to get those computers, they in fact are 1 of the 12 congressionally mandated programs that in fact have access to it on an equal footing with the Department of Defense.

Mr. SHAYS. Right, OK.

Mr. Kutz, just tell me, from the testimony you heard here—and this is not—this is a dialog, not a debate. But help me kind of sort things out; what would you find—is there anything that was said that basically you would want to give us your perspective that would differ? Or, for the most part, do you concur with the comments that were made?

Mr. KUTZ. For the most part. I would say a couple of things. The issue of shrinkage. I mean, I understand the perspective of the 1 percent, and we didn't look at it from that perspective necessarily, but it is important to note that we are still talking about things like body armor, aircraft helicopter parts, chem-bio suits and circuit cards. I'm not sure that is a relevant apples-to-apples comparison completely to say that this excess property system in the military losing things is the same as the retail entity losing things. So I think that's a broader perspective I would have on that issue.

With respect to the items that we've requisitioned—and maybe we weren't clear in our testimony that we had requisitioned those because we didn't pay anything for those except a little bit of shipping. It was really the medical instrument chest and the parts supply and the circuit cards, we requisitioned those at GAO, whereas everything else we bought on the Internet with our undercover credit card.

Mr. SHAYS. What were the two that you did at GAO?

Mr. KUTZ. Well, there were three; there were the parts supply, the circuit cards—exhibit 3 and 2 over there—and then the medical instrument chest.

Mr. SHAYS. Is there any restricted item that you got not through GAO but as a result of just private citizen—your card?

Mr. KUTZ. No, I do not believe so.

Mr. SHAYS. I mean, I just think that's important to point out. These still are restricted items, but it's not like I could have gone on and gotten them.

I was thinking that, you know, in your work, if you assign people to look at something, in a way you almost hope they find it so you feel like you are accomplishing something and doing your job. But I would think your biggest satisfaction would be when you come back here a year from now—I didn't ask you; will you be in your position a year from now?

Mr. KUTZ. If you would like us to do certain studies. If you want us to test their system in January or whatever the case may be, we will work with you on that.

Mr. SHAYS. I want to come back a year from now. And I would think your biggest satisfaction would be to—and maybe not to the extent that you did—but test the system out again, and to find that you didn't—you weren't as successful in breaking through the system or finding things that were being sold that were also being purchased. I mean, if that system works, General, as you hope, I would think that frankly that would say to GAO, gosh, we accomplished something. That would be my view.

Mr. KUTZ. Absolutely. We would agree with that.

Mr. SHAYS. And General, if whoever takes your place comes back here—and Mr. Estevez, you will be here—and if we have the same story, I will feel like we failed. I will feel like all of us failed. So I hope we see some good success here.

Is there anything, gentlemen, that we should have asked that we didn't ask that you want part of the record?

Mr. Kutz, anything that you want to conclude with?

Well, again, thank you for your service, and we will hope that we see some significant progress. Thank you. This hearing is adjourned.

[Whereupon, at 4:43 p.m., the subcommittee was adjourned.]

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