Audit Report

OFFICE OF THE INSPECTOR GENERAL

PROCUREMENT OF MEDICAL MATERIEL AND EQUIPMENT

Report Number 91-085

May 30, 1991

Department of Defense

The following acronyms are used in this report.

CBD . . . . . .Commerce Business Daily
CDCS . . . . . .Customer and Depot Complaint System
DFARS. . . . . .Defense Federal Acquisition Regulation Supplement
DLA . . . . . Defense Logistics Agency
DVD-SPUR . . . . . Direct Vendor Delivery-Special Purchase System
FAR . . . . . Federal Acquisition Regulation
FMFIA . . . . . .Federal Managers' Financial Integrity Act
GSA . . . . . .General Services Administration
NSN . . . . . National Stock Number
PCO . . . . . .Procurement Contracting Officer
PET . . . . . Procurement by Electronic Transmission
SAMMS . . . . . .Standard Automated Materiel Management System
SPEDE . . . . . .Standard Automated Materiel Management System
Procurement by Electronic Data Exchange
VA . . . . . Department of Veterans Affairs

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

May 30, 1991

MEMORANDUM FOR DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Audit Report on the Procurement of Medical Materiel and Equipment (Report No. 91-085)

We are providing this final report for your information and use. Comments on a draft of this report were received from the Deputy Assistant Secretary of Defense, Health Affairs (Medical Readiness) and the Defense Logistics Agency and were considered in preparing the final report. We evaluated procurement practices and internal controls at the Defense Personnel Support Center, Directorate of Medical Materiel, for the acquisition of medical materiel and equipment.

Large purchase procedures for replenishment stock and direct delivery to overseas customers generally complied with procurement regulations and, for the contracts tested, materiel was procured at fair and reasonable prices. The mechanized bidders' list was being updated to reflect vendor requests but did not include controls to add or remove vendors based on individual procurement actions. Small purchase procedures, especially direct vendor delivery awards, needed improvements in the preaward compliance reviews and in the postaward reviews of price reasonableness. Increased use of Federal Supply Schedules for direct vendor delivery of small purchase procurements could save an estimated $1.4 million annually, totaling $8.4 million for the Future Years Defense Program. In addition, procedures and internal control processes for postaward review and evaluation of vendor performance and followup for nonconforming, delinquent, and missing materiel were not adequate. The causes of discrepancies were not properly identified and vendors were not requested to comply with the Fast Payment provisions that require vendors to replace materiel or reimburse the Government for reported discrepancies.

On February 27, 1991, a draft of this report was provided to the Director, Defense Logistics Agency and the Commander, Defense Personnel Support Center. Comments on the draft report, excluding Recommendation A.3., were received from the Defense Logistics Agency on May 10, 1991. The comments conformed to the requirements of DoD Directive 7650.3 and except for Recommendation A.3., there are no unresolved issues. The DoD Directive requires that all audit recommendations be resolved promptly. Therefore, we request that the Director, Defense Logistics Agency provide comment on Recommendation A.3. and the associated monetary benefits by July 29, 1991.

As required by DoD Directive 7650.3, the comments must indicate concurrence or nonconcurrence in the recommendation. If you concur, describe the corrective actions taken or planned, the completion dates for actions already taken, and the estimated dates for completion of planned actions. If you nonconcur, you must state your specific reasons. If appropriate, you may propose alternative methods for accomplishing desired improvements.

If you nonconcur with the estimated monetary benefits or any part thereof, you must state the amount you nonconcur with and the basis for your nonconcurrence. Recommendations and potential monetary benefits are subject to resolution in accordance with DoD Directive 7650.3 in the event of nonconcurrence or failure to comment.

The courtesies extended to the audit staff are appreciated. If you have any questions on this audit, please contact Mr. Charles Hoeger at (215) 737-3881 (DSN 444-3881). The planned distribution of this report is listed in Appendix G.

Edward R. Jones
Deputy Assistant Inspector General
for Auditing

cc:
Assistant Secretary of Defense (Health Affairs)
Assistant Secretary of Defense (Production and Logistics)
Commander, Defense Personnel Support Center

Office of the Inspector General, DoD

AUDIT REPORT NO. 91-085 May 30, 1991
(Project No. 0LD-0035)

PROCUREMENT OF MEDICAL MATERIEL AND EQUIPMENT

EXECUTIVE SUMMARY

Introduction. The Defense Personnel Support Center (the Center), Directorate of Medical Materiel, is responsible for the procurement of medical materiel and equipment for DoD hospitals and medical facilities worldwide. The Center managed 64,600 medical line items with a wholesale inventory valued at $577.2 million as of March 31, 1990. More than 43,900 line items were authorized for local procurement and normally were not stocked in the wholesale distribution system. For the 12 months ended March 31, 1990, the Directorate made 97,595 awards valued at $860.8 million.

Objectives. The objectives of the audit were to determine if procurements of medical materiel and equipment were made in accordance with DoD regulations and the Federal Acquisition Regulation, and to evaluate the adequacy of internal controls over the procurement process.

Audit results. The audit disclosed that procurement processes for large purchases for stock replenishment and for direct vendor delivery to overseas customers generally complied with procurement regulations and, for the contracts tested, materiel was procured at fair and reasonable costs. However, there were deficiencies in small purchase procedures and in processing reports of discrepancy.

o Small purchase procedures needed improvement in preaward compliance reviews and postaward price analysis reviews and could benefit through greater use of Federal Supply Schedules. Implemented and planned modifications to the automated procurement system could increase the use of Federal Supply Schedules and reduce procurement costs (Finding A).

o The review and disposition of customer reports of discrepancy were not effective, did not identify patterns of vendor abuse, and did not comply with Fast Payment provisions. As a result, some materiel was not delivered in accordance with contractual requirements and vendors continued to receive awards because patterns of vendor abuse were not identified (Finding B).

Internal Controls. Procedures and internal controls were not established or effective to ensure that preaward reviews and postaward price analyses of small purchases were in compliance with applicable procurement regulations (Finding A).

In addition, internal controls were not sufficient to ensure that the review and disposition of customer reports of discrepancy for materiel not conforming to contractual requirements were adequately performed (Finding B).

The Internal Controls section in Part I of this report contains the specific internal controls tested and provides the necessary improvements needed (page 2).

Potential Benefits of Audit. Increased use of Federal Supply Schedules for small purchase direct delivery procurements could save an estimated $1.4 million annually, totaling $8.4 million for the Future Years Defense Program. Nonquantifiable benefits include compliance with procurement regulations, increased competition with potential for cost savings, and improved management of reports of discrepancy and followup for nonconforming, delinquent, and missing materiel. (Appendix E).

Summary of Recommendations. We recommended that the Center establish additional procedures and controls for the establishment and maintenance of bidders' lists and reviews of small purchases, and increase the use of Federal Supply Schedules.

We also recommended that the Center establish additional guidance and enforce regulatory requirements to more effectively monitor vendor performance.

Management Comments. Comments from the Defense Logistics Agency, for all but Recommendation A.3. were received on May 10, 1991. The Agency concurred in the recommendations for corrective action and the management actions completed or ongoing are considered responsive. The Agency should provide final comments on Recommendation A.3. and associated monetary benefits by July 29, 1991.

The Deputy Assistant Secretary of Defense, Health Affairs (Medical Readiness) concurred in the recommendations for corrective action.

A discussion of the responses is included in Part II of the report. Copies of the responses are included in Part IV of the report.

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This report was prepared by the Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, DoD. Copies of the report can be obtained from the Information Officer, Audit Planning and Technical Support Directorate at (703) 614-6302 (DSN 224-6302).

PART I - INTRODUCTION

Background

The Assistant Secretary of Defense (Health Affairs) is the principal staff assistant and advisor to the Secretary of Defense for DoD health policies, programs, and activities. One of the functions of the Assistant Secretary is to provide direction, control and policy guidance to the Defense Medical Standardization Board, composed of the Surgeons General of the Army, Navy, and Air Force or their designated alternates. The functions of the board include reviewing specifications of medical materiel to determine conformity with essential characteristics; ensuring the entry, retention, or deletion of standardized medical items in the DoD medical supply system; and providing advice to the Defense Personnel Support Center (the Center), Directorate of Medical Materiel (the Directorate), to assist it in carrying out the technical functions assigned to it.

The Center is the DoD integrated materiel manager for medical items. As of March 31, 1990, the Center managed 64,600 medical line items with a wholesale inventory valued at $577.2 million. More than 43,900 of these line items are authorized for local procurement and are not normally stocked in the wholesale distribution system.

Objectives

The objectives of the audit were to determine if procurements of medical materiel and equipment were made in accordance with DoD regulations and the Federal Acquisition Regulation (FAR), and to evaluate the adequacy of internal controls over the procurement process.

Scope

The audit was limited to a review of the policies and procedures for the procurement of medical materiel and equipment at the Center. We did not review local procurement policies and procedures at hospitals and other medical facilities operated by the Military Departments. The Directorate's active contract file and the contract history file were used to determine the number and value of awards from April 1, 1989, through March 31, 1990. During this period there were 97,595 awards for 153,055 line items valued at $860.8 million.

We randomly selected 337 awards valued at $65.2 million -- 76 large purchases valued at $46.5 million, 219 small purchases valued at $0.7 million, and 42 Federal Supply Schedule purchases valued at $18.0 million -- from the four procurement branches in the Directorate's Contracting and Production Division (Appendix A). A large purchase is any purchase expected to exceed an aggregate amount of $25,000. The purchases included

awards for stock replenishment and for direct vendor delivery of nonstocked items to customers. We evaluated the adequacy of preaward reviews, method of solicitation, reasonableness of award price, procurement documentation, and postaward price analyses. We also evaluated internal controls used in the acquisition and review process.

This economy and efficiency audit was made from January through October 1990 in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD, and accordingly, included such tests of internal controls as were considered necessary. Activities visited or contacted during the audit are listed in Appendix F.

Internal Controls

To determine the adequacy of internal controls over the procurement process, we evaluated the procedures for preaward reviews for regulatory compliance and postaward price analyses and evaluated the adequacy of vulnerability assessments and internal management control reviews. We also reviewed the internal control processes for review and evaluation of vendors' performance and followup to vendors for nonconforming materiel, delinquent deliveries, and quantity discrepancies. As discussed in Findings A. and B. of this report, additional controls were needed in the preaward reviews for regulatory compliance, the monthly postaward price analysis of small purchases, and the review process for materiel discrepancies that were identified and reported on reports of discrepancy. The internal management control reviews did not properly test the effectiveness of controls for the seven administrative functional areas designated by the Defense Logistics Agency (DLA) for implementing the requirements of the Federal Managers' Financial Integrity Act (FMFIA).

The audit identified material internal control weaknesses as defined by Public Law 97-255, Office of Management and Budget Circular A-123, and DoD Directive 5010.38. Controls were not established or effective to ensure that the Directorate procedures and practices were in accordance with applicable procurement regulations. All recommendations in this report, if implemented, will correct the weaknesses. We have determined that the estimated monetary benefits that can be realized by implementing Recommendation A.3. are $1.4 million annually, totalling $8.4 million for the Future Years Defense Program. A copy of the final report will be provided to the senior official responsible for internal controls within your agency.

Prior Audits and Other Reviews

The Office of the Assistant Inspector General for Inspections Report No. 88-INS-03, "Final Inspection Report on the Defense Personnel Support Center," May 31, 1988, reported that deficiencies in the Procurement by Electronic Transmission (PET)

system were identified during a procurement management review performed by DLA, and during a review performed by a Defense Personnel Support Center ad hoc committee. The procurement management review found that PET did not properly record purchase actions, which resulted in duplicate orders, duplicate shipments, and no shipments. The cause of the condition was attributed to minimal management visibility and inadequate review and followup. The deficiencies essentially changed the PET award process from an automated to a manual operation. The report recommended that PET's features be evaluated for inclusion or exclusion in the new DLA Standard Automated Materiel Management System Procurement by Electronic Data Exchange (SPEDE). The report also recommended that DLA ensure that SPEDE comply with the FAR and appropriate computer security regulations. DLA concurred with the recommendations and automated the communications process to eliminate the duplication or omission of solicitation and award data. These changes were included in the implementation of SPEDE. Personnel from the Directorate manually reviewed vendor and system performance and these reviews resulted in the development of 20 proposed changes to the SPEDE procurement system for implementation in January 1991.

PART II - FINDINGS AND RECOMMENDATIONS

A. SOLICITATION, AWARD, REVIEW, AND INTERNAL CONTROL PROCEDURES

Large purchases (over $25,000) generally were properly documented, complied with procurement regulations, and for the awards tested, were bought at fair and reasonable prices. However, the mechanized bidders' lists, used for large and small stock replenishment purchases, were not properly maintained. Also, small purchase solicitation and award procedures governing the procurement of medical materiel and equipment for stock replenishment and direct vendor delivery to overseas customers were not always in compliance with procurement policy and regulations. These conditions existed because of the following reasons.

- o Adequate procedures for one Branch had not been established to prepare required Individual Contracting Action Reports.

- o Adequate controls had not been established to update mechanized bidders' lists to ensure access to additional vendors.

- o Noncompetitive price reasonableness determinations were not supported by documentation and prior awardees were not always solicited in small purchase awards.

- o Federal Supply Schedules and blanket purchase agreements were used only for a limited number of purchase awards.

In addition, internal controls did not adequately ensure that:

- o preaward reviews were made in compliance with applicable procurement regulations,

- o purchases in excess of $10,000 were always advertised in the Commerce Business Daily (CBD), and

- o postaward price analyses were conducted monthly to validate the reasonableness of price determinations.

As a result, management had no assurance that adequate competition was achieved and items were obtained at fair and reasonable prices. In addition, we estimated that savings of about $1.4 million annually, totaling $8.4 million for the Future Years Defense Program could be achieved if additional procurements for direct deliveries were made using Federal Supply Schedules.

DISCUSSION OF DETAILS

Background

The Directorate has four branches that procure materiel and equipment for the wholesale supply system (stock replenishment) and for nonstocked items for overseas hospitals and medical

facilities (direct vendor delivery items). The Drug and the Hospital and Surgical Branches procure stock replenishment items, the Equipment Branch procures stock replenishment and direct vendor delivery items, and the Customer Support and Automation Branch procures direct vendor delivery items.

The FAR establishes large purchase procedures for procurements that are expected to exceed $25,000, small purchase procedures for procurements that are not expected to exceed $25,000, and Federal Supply Schedule procedures that do not have specific dollar value thresholds. Federal Supply Schedules are indefinite delivery contracts established with vendors to provide supplies and services at stated prices for given periods. Additional guidance is provided in the Defense Federal Acquisition Regulation Supplement (DFARS), the Defense Logistics Acquisition Regulation, the Defense Personnel Support Center Contracting Policy Manual, and Procurement Contracting Officer (PCO) letters.

Individual Contracting Action Reports

The FAR requires that contracting officers submit Individual Contracting Action Reports, DD Form 350, for all procurements over $25,000. The Customer Support and Automation Branch began awarding large purchases during fiscal year 1990. These awards were for direct vendor delivery overseas of large quantities of stocked and nonstocked items. These direct vendor delivery awards were previously procured by the Drug and Hospital and Surgical Branches. The contract files were well documented and included all of the necessary reviews and approvals, and supported the award to the selected vendor. We noted, however, that the Individual Contracting Action Reports were not completed for any of the large purchases awarded by the Customer Support and Automation Branch. We attributed this oversight to the recent transfer of this function to the Customer Support and Automation Branch. We conveyed this condition to the buyer and the contracting officer and appropriate corrective action was taken. Therefore, this report does not contain a recommendation regarding the completion of the DD Form 350.

Mechanized Bidders' Lists

The FAR requires that procurement activities establish and maintain bidders' lists to ensure access to adequate sources of supply. However, vendors that fail to respond to two consecutive solicitations can unilaterally be removed from the mailing lists. PCO Letter No. 9, "Bidders Mailing List," dated January 31, 1989, provided procedures for the use and maintenance of the mailing lists, including the requirement to purge the list after every solicitation. Excessively long mailing lists may be divided into shorter lists for vendor solicitation rotation, but procurement activities should exercise considerable judgment in determining whether the size of the purchase justifies the rotation.

A mechanized bidders' list is maintained for all standardized medical items managed by the Directorate. The use of the bidders' lists is not appropriate for all bid solicitations. For example, in our sample of 337 awards there were nonstandardized medical items, items purchased for the first time, and items obtained from Federal Supply Schedules. Under these circumstances, bidders' lists would be unavailable or would not significantly increase the competitive process.

The buyers developed and maintained manual bidders' lists for assigned items because buyers did not receive the mechanized bidders' list as part of the procurement package for stock replenishment procurements under $25,000; buyers were not aware of the mechanized bidders' list maintained in the branches; and the mechanized bidders' list was considered unreliable, outdated, and incomplete for achieving maximum competition. Based on our review of 76 large purchases, the use of the buyers' manual bidders' lists resulted in the Directorate receiving bids from multiple vendors that were not on the mechanized bidders' lists and this resulted in competitive bidding practices. Although buyers took appropriate action in using the manually prepared bidders' lists to achieve bid competition, the buyers did not take appropriate action to ensure that the mechanized bidders' lists were updated to include new sources of supply or to remove sources of supply no longer interested in doing business with the Government.

For example, the mechanized bidders' list for National Stock Number (NSN) 6505-01264-1365, magnesia and alumina oral suspension, contained only one source of supply. The manual bidders' list maintained by the buyer included six potential sources of supply, none of which were included on the mechanized bidders' mailing list. In our sample procurement three bids were received and an award for $18,482 was made to the low bidder. A review of the procurement history showed that the low bidder was the successful awardee for the last five depot stock replenishment actions dating back to October 1988. Our review of the mechanized bidders' list, dated June 29, 1990, showed that neither the successful awardee nor the unsuccessful bidders were added to the list.

This example was not an isolated case of one buyer not taking the appropriate action to update the mechanized bidders' list. We found this condition in other awards processed by other buyers under both small and large purchase procedures. In one procurement branch, we reviewed 30 small purchase awards and 36 large purchase awards. We found that the successful awardees were not on the mechanized bidders' list for 16 of the 30 small purchase awards and for 23 of the 36 large purchase awards.

Management was aware of the problems with the mechanized bidders' list and initiated action in 1989 to validate existing data, and in June 1990, management reactivated the distribution of the mechanized bidders' list for small purchases. However, we did

not find any improvement in the maintenance of the mechanized bidders' list. Most requests for updating the mechanized bidders' lists came from vendors, not buyers. We attributed this condition to a lack of internal controls to monitor buyers compliance with procedures contained in PCO Letter No. 9.

Small Purchase Awards

Small purchase solicitation and award procedures governing the procurement of medical materiel and equipment for stock replenishment and direct vendor delivery to overseas customers were not always in compliance with procurement policy and regulations. The FAR, Part 13, "Small Purchase and Other Simplified Purchase Procedures," prescribes simplified purchasing procedures when the aggregate amount is not expected to exceed $25,000. The procedures are designed to reduce administrative costs, and improve opportunities for small businesses and small disadvantaged businesses to obtain a fair proportion of awards. Small purchase procedures include Federal Supply Schedules, blanket purchase agreements, and purchase orders. When an award is expected to exceed $2,500, the FAR requires that contracting officers solicit at least three sources in order to promote adequate competition. When possible, two of the vendors should be sources not previously solicited. Competition is achieved when price quotes are received from more than one vendor. When only one response is received, the procurement file should contain support for determining the reasonableness of the award price.

Limited solicitation and price reasonableness determinations. We selected 36 Federal Supply Schedule awards (76 line items) valued at $2.0 million and 219 small purchase awards (377 line items) valued at $0.7 million to determine whether these items were awarded in accordance with appropriate procurement regulations and procured at a fair and reasonable price. The sample of small purchase awards, by Branch, is shown in Appendix A.

The 36 Federal Supply Schedule awards were made at the scheduled price in effect at the time of the award. We considered these awards to be in accordance with regulations and awarded at fair and reasonable prices. Small purchase awards in excess of $2,500, however, were not always awarded competitively. In addition, the small purchase award files did not always contain sufficient documentation to support the award at the specified price. The Standard Automated Materiel Management System (SAMMS), the Direct Vendor Delivery - Special Purchase System (DVD-SPUR), and the SPEDE system did not determine whether the requested item was available from a Federal Supply Schedule. In addition, the small purchase solicitation process did not automatically solicit the previous successful low bidder and the evaluation process did not compare vendor price quotes to prior award price or to a standard (base) price. These conditions are discussed below.

Stock replenishment. Seventy of the 219 small purchase awards were for stock replenishment. Although 48 of the 70 purchases were in excess of $2,500 and met the competition requirements of the FAR and the DFARS, only 22 of the 48 purchase awards were awarded competitively. Further, the reasonableness of the price was not documented in the purchase order file. PCO Letter No. 78, "Price Reasonableness Determinations," November 18, 1989, requires that for price reasonableness determinations based on vendor catalogs and price lists, the purchase order file must include copies of relevant pages of the catalog and price lists. The purchase award files reviewed generally included the statement that the price offered was the price that was listed in the vendor's catalog or commercial price lists; however, there was no supporting documentation in the file.

For example, purchase order DLA120-90M-AA79 was awarded on October 31, 1989, for 100 bottles of chlorpromazine hydrochloride tablets, USP, 25mg, 1,000 tablets per bottle for $23,698. This was the first stock buy for this item. In addition, there were no prior direct vendor delivery buys recorded in the contract history file. Three vendors were solicited, but only one vendor quoted a price. The other two vendors responded but declined to quote a price on the item. The item was procured from the sole responsive bidder; however, there was no documentation in the purchase award file to support the award price, such as a copy of a commercial price list. The estimated price before purchase solicitation was $11,250.

Purchase awards under $2,500 are permitted to be awarded noncompetitively provided that there is some assurance that the price quoted is fair and reasonable. In our sample of 70 small purchases, there were 22 purchase awards under $2,500. Three of these were awarded competitively, but there was no documentation to support the reasonableness of price for 18 of the remaining 19 purchase awards except statements, such as the price was based on the vendor's catalog or price list. Copies of the catalog or price lists were not in the purchase award files. Procurement personnel informed us that action to verify price reasonableness was taken only when there was some reason to question the reasonableness of the price paid.

Direct vendor delivery. Of the 219 small purchase awards, 149 were purchase orders for direct vendor delivery. The Automation Section of the Customer Support and Automation Branch competitively awarded 53 purchase orders through SPEDE to the low bidder. The remaining 96 purchase orders were awarded noncompetitively; 32 through SPEDE to the sole bidder and 64 through the Customer Support Section. For the purchase orders awarded noncompetitively, the reasonableness of price was not documented in the purchase order files. There was no comparison to the previous low price and prior awardees were not always solicited.

The SPEDE system randomly selects three vendors, based on the vendor's registration with the Directorate identifying the Federal Supply Classes in which they had interest. Participating vendors are provided copies of the vendor's portion of the SPEDE computer program that enables them to electronically communicate with the Directorate, avoiding the need for hard copy mailings. The SPEDE system automatically generates requests for quotation, analyzes the vendor responses, makes the purchase award within defined parameters, receives and processes shipping and other information provided by the vendor, and provides necessary updates to the SAMMS and DVD-SPUR systems, DLA's standard computer systems. From April 1, 1989, through March 31, 1990, 46 vendors participated in the automated procurement process and were awarded 50,075 awards valued at over $17.7 million. Six vendors received 25,056 awards (50 percent) valued at over $9 million (51 percent). Procurement personnel were actively pursuing additional vendors for participation in SPEDE.

Automated Section procurements. Before soliciting three vendors, the SAMMS, DVD-SPUR, and SPEDE systems did not automatically determine whether the requested item was available from a Federal Supply Schedule. As discussed below, 20 of 85 procurements could have been procured from Federal Supply Schedules at overall lower prices. For example, NSN 6515-01197-8814, orthopedic bone blade, was procured through SPEDE for $52.50 each. This same item was procured 16 days earlier and 92 days later from two different vendors for only $25.11, the latter purchase against a Federal Supply Schedule.

In addition, the solicitation process did not automatically solicit the previous successful low bidder and the evaluation process did not compare vendor price quotes to prior award price or to a standard (base) price. Of the remaining 65 procurements not available on Federal Supply Schedule, the previous supplier was not solicited for 32 procurements, and lower prices for comparable quantities had been paid for 19 of these 32 procurements. In order for the previous successful low bidder to be solicited, the procurement history of the NSN had to be loaded onto the DVD-SPUR system. We found that the previous unit price field in the DVD-SPUR data base was usually blank indicating that the prior award history was not entered into the DVD-SPUR system. Procurement personnel told us that the initial award had to be independently posted to the DVD-SPUR system in order for the base price and the last successful vendor's code to be transferred to the SPEDE system for future solicitations and price comparison. They could not tell us why the DVD-SPUR system had not been updated. For example, one of our sample items, NSN 6520-01211-9595, dental restorative paste, was procured through SPEDE for $20.00 each. This item was previously procured at prices of $17.25 and $18.25 each, from a vendor who also supplied the item six other times during fiscal year 1989 at lower prices. This vendor was not solicited for our sample procurement.

Customer Support Section procurements. Direct vendor delivery purchase requests that were exempt from automated procurements (such as equipment items), unprocessable by the automated procurement system because of limited or missing descriptions, and processed through the automated system but not awarded because bids were not received or varied widely were forwarded to the Customer Support Section for solicitation and award. From April 1, 1989, through March 31, 1990, the Customer Support Section, including the Emergency Supply Operations Center, awarded 30,394 small purchases (59,934 line items) valued at over $40.9 million for non-stocked items for direct delivery to overseas medical activities.

Small Purchases	Number		Value
	Awards	Lines	($Millions)
Manual Purchase Orders	19,162	36,774	$17.2
Blanket Purchase Agreements	6,380	15,332	11.2
Federal Supply Schedules	4,852	7,828	12.5
Total Awards	30,394	59,934	$40.9

Of the 149 direct vendor delivery awards sampled, 80 small purchases with a total of 164 line items valued at $189,414 were procured by the Customer Support Section. Sixteen of the small purchases (16 line items), valued at $138,407, were awarded using Federal Supply Schedules. The remaining 64 small purchase awards (148 line items) valued at $51,007 were procured noncompetitively. Four of the awards, in excess of the $2,500 competitive limit, were awarded noncompetitively and the procurement folder stated that the basis for award was "single source under $2,500 competitive limit." The awards ranged from $3,460 to $10,894. Contrary to PCO Letter No. 78, copies of relevant pages of commercial catalogs or price lists were not in the purchase order folder to support reasonableness of the price paid. While several of these items were high priority and foreign military sales requisitions, none of the folders provided evidence that the procurements were expedited and justified because of these conditions. In addition, previous low price vendors were not always solicited. For 12 line items with awards valued at $9,867, the awards were made without soliciting bids from the previous successful low bidders that sold the items at lower prices than were paid on the current awards.

Federal Supply Schedules. Federal Supply Schedules were used for a limited number of large and small purchase awards. Materiel purchased for stock replenishment, usually exceeding the maximum order limits on the Federal Supply Schedules, can generally be purchased at prices lower than schedule prices because of the large quantity purchased. Consequently, we limited our review to the 149 small purchase awards purchased for direct vendor delivery (233 line items) for $88,549 that were awarded by the Customer Support and Automation Branch. Thirty-five of the 233 line items purchased at a cost of $13,915 were available from Federal Supply Schedules for $10,532 for a

net savings of $3,383 (24.3 percent). Based on the results of our review, we estimated that about $1.4 million annually, totaling $8.4 million for the Future Years Defense Program, could be put to better use if the Directorate made greater use of Federal Supply Schedules (Appendix B).

Federal Supply Schedules are established by the Department of Veterans Affairs (VA) and the General Services Administration (GSA) for medical items that are commonly requisitioned but are usually not stocked in the Federal Supply System because of low and infrequent demand. The VA is responsible for establishing schedules for drugs, pharmaceuticals, and other common hospital and surgical supplies. The GSA is responsible for establishing schedules for medical equipment and furniture items.

The use of Federal Supply Schedules is optional in the DoD. However, the Executive Director, Acquisition Management Planning and Support, Defense Personnel Support Center, issued Contracting Policy Memorandum Number 88-5, "Use of Optional Federal Supply Schedules," August 10, 1988, which stated that optional Federal Supply Schedules are the preferred sources of supplies and services, and they should be used before soliciting commercial sources. In response to inquiries from DoD field activities, the Deputy Assistant Secretary of Defense for Procurement also issued a memorandum, "GSA Federal Supply Schedules as Preferred Source of Supply," October 27, 1988, which reiterated the DoD policy that maximum use should be made of Federal Supply Schedules.

Personnel at the VA Marketing Center informed us during the audit that the VA was in the process of automating the vendor price lists and catalogs for items covered on Federal Supply Schedules established by the VA. This automation process is expected to be completed during fiscal year 1991 and will be updated when new awards were made, when items were added and deleted, and when prices change. This data base will reference all items by vendor and part number or catalog number, not necessarily an NSN.

Availability of direct vendor delivery materiel on Federal Supply Schedules. The Customer Support Section noncompetitively awarded 148 line items valued at $51,007. Eight of the 148 line items bought noncompetitively were available from another vendor on Federal Supply Schedules at lower prices. Another seven line items were purchased from vendors with Federal Supply Schedules, but the schedules were not cited. Similarly the Automation Section awarded 85 line items valued at $37,542 through SPEDE. Twenty of the 85 line items were available on Federal Supply Schedules at an overall lower price. Of the 20 items, 3 were priced higher on the Federal Supply Schedule, 1 was the same price, and 16 were available at a lower price. For example, NSN 6505-00812-2531, fluphenazine enanthate injection, USP, 25mg/ml, 5ml vial, was purchased through the automated procurement system for $60.50 per vial; this item was available on a Federal Supply Schedule awarded to Squibb for $44.26 per vial. For the remaining 65 items, 43 were supplied by

vendors that had a Federal Supply Schedule; however, the items were not included in the available price bulletins.

The Directorate did not maintain demand and procurement histories for the 111 nonstandard (non-NSN) items in our sample. However, we were able to review procurement histories for 161 sample items (150 nonstocked NSN's) purchased for direct vendor delivery, and found that 114 NSN's were purchased more than 5 times (56 NSN's at least 20 times) during fiscal years 1989 and 1990. Because of their repetitive demand, nonstocked items with high demands should be reported to the VA and the GSA for possible inclusion in future Federal Supply Schedules.

Proposed enhancements to SPEDE. Directorate personnel proposed 20 enhancements to the SPEDE system. These enhancements, scheduled for implementation in January 1991, included the solicitation of Federal Supply Schedule vendors for quotations for all items that they manufacture. When the item is on schedule, an award will be made automatically. Price quotes from large businesses for items that are not on schedule will be included in later solicitations and compared to small business price quotes allowing for a variable percentage in price. This is designed to enable small businesses to compete on a par with large businesses, yet allow the Government to obtain needed items at a fair and reasonable price. The program, as designed, will be effective for items that are identified to an NSN.

Blanket purchase agreements. Blanket purchase agreements were used for a limited number of small purchase awards. SPEDE and the Emergency Supply Operations Center, part of the Customer Support and Automation Branch, used blanket purchase agreements established under the automated procurement system; however, blanket purchase agreements were not used elsewhere in the Directorate for centralized purchases. Existing decentralized blanket purchase agreements could be used by the Directorate to expedite centralized purchases.

Blanket purchase agreements were designed to reduce the administrative costs associated with making awards to vendors that receive multiple small purchase awards. This is done by reducing the number of individual purchase documents and the associated cost of processing vendor invoices.

In addition to blanket purchase agreements established under the automated procurement system, the Directorate established over 200 decentralized blanket purchase agreements to assist hospitals and medical centers in obtaining materiel that was authorized for local procurement. At the time of our review, 50 medical facilities overseas and 128 medical facilities in the continental United States had decentralized blanket purchase agreements, 42 Army activities, 27 Navy activities, and 109 Air Force activities. Decentralized blanket purchase agreements were not used by Directorate personnel to expedite centralized purchases, although many of the awards made were to vendors that established

blanket purchase agreements with the Directorate. Directorate personnel could not provide a reason for not using the existing blanket purchase agreements for awards that were generally less than $500.

Lack of Internal Control Processes

There was a lack of internal controls to ensure that a random sample of small purchase preaward reviews were conducted, contracting actions were advertised in the CBD, and postaward price analyses were performed. Preaward contracting actions for large and small value procurements are made by buyers who are under the control and direction of contracting officers. Procurement files should contain sufficient documentation to support the award, including compliance with and deviation from procurement regulations and established local policies, a review and approval by appropriate contracting personnel, and a determination that the price is reasonable and in the best interest of the Government. The Defense Logistics Acquisition Regulation 4105.1 requires that the Directorate of Contracting conduct independent postaward price analysis reviews to ensure that price reasonableness is documented and justified.

Preaward reviews. For other than automated procurements, buyers are responsible for performing most preaward functions included in the solicitation and award process. Contracting officers are responsible for providing additional guidance and ensuring that procurements are made in accordance with appropriate procurement policies and procedures. Our review of 76 large procurements disclosed that procurement decisions, including compliance with procurement regulations and determinations of price reasonableness, were properly documented and appropriately approved by authorized contracting personnel. In addition, the 42 Federal Supply Schedule awards were considered appropriate and sufficiently documented for award. However, in all the 134 manual small purchase awards valued at $665,740 that we reviewed, there was no evidence of supervisory reviews of the buyers' performance or a review of the reasonableness of the prices paid. Supervisory personnel indicated that they did not have time to perform a detailed preaward review on all small purchases. We agree that the volume of small purchases precludes a detailed review on all awards, but a review of a random sample of awards is required for a supervisor to evaluate the performance of buyers so that corrective actions can be taken when identified.

The lack of preaward reviews of procurement files and the lack of documentation supporting price reasonableness determinations were identified in DLA's last two procurement management reviews. In response to the October 12, 1989, procurement management review report, the Directorate issued two PCO letters on November 13, 1989. The letters emphasized the need for supervisory reviews to ensure that procurement files are adequately documented and that price reasonableness determinations are fully supported before

issuing the award. However, our review results showed that further emphasis on the performance of supervisory reviews is required.

Advertising in the Commerce Business Daily. For contract actions expected to exceed $25,000, or $10,000 if there was not a reasonable expectation that at least two offers would be received from responsive and responsible offerors, contracting officers are required to advertise proposed contract actions in the CBD. The primary purpose of publicizing the proposed purchase in the CBD is to increase competition, broaden industry participation, and assist the development of socioeconomic programs. There are exceptions when proposed purchase actions do not need to be advertised in the CBD, such as when the Government would be seriously injured if the procurement activity was required to comply with the time required for full and open competition, or when a statute expressly requires purchase from a specified source.

For the 76 large purchase awards reviewed, 67 purchase awards were advertised and 9 were not. The procurement files for the nine purchase awards were adequately documented, cited an urgency of need, and provided justification of why full and open competition was not used. For the 219 small purchase awards in our sample only 26 were in excess of $10,000. The procurement files contained documentation to support the decision not to advertise 10 of the 26 awards. At least two offers were received on previous awards, or an urgency of need condition existed that justified the elimination of the need to advertise. The procurement files did not contain documentation to support the decision not to advertise the other 16 awards. Procurement personnel agreed that the 16 awards should have been advertised but they were unable to provide a reason for not doing so.

Postaward price analyses. Defense Logistics Acquisition Regulation 4105.1 requires that monthly postaward price analyses be performed by the Directorate of Contracting for 60 line items selected from all small awards made during the previous month. The purpose of this review is to determine the incidence of unreasonably priced awards and to determine what corrective action should be taken. The results of these reviews are required to be reported quarterly to DLA Headquarters.

In October 1989, a procurement management review team from DLA reported conditions that were identified during a previous review. They found that the Directorate of Contracting reviews did not satisfy the intent of the Defense Logistics Acquisition Regulation. The Directorate of Contracting's reviews were nothing more than cursory reviews of documentation. The reviews did not identify incidences of unreasonably priced small purchases or appropriate corrective measures. In addition, automated small purchase awards were not included in the review although they accounted for 41 percent of the small purchase line items awarded (excluding Federal Supply Schedules).

In response to the procurement management review, the Directorate reported that personnel shortages made it impossible for the small purchase postaward price analysis to be performed in the past, and that a realignment of procurement personnel, including their responsibilities, was necessary to ensure that the reviews, reports, and corrective actions associated with postaward price analysis were accomplished in accordance with existing policy. The realignment action was expected to be completed by May 30, 1990.

There was only one postaward price analysis conducted during fiscal year 1990 and the results of that analysis were included in a July 11, 1990, report to DLA. (Contracting personnel advised us that the postaward price analysis of small purchases was suspended in July 1990, without approval from DLA Headquarters, because personnel were not available to perform the review.) The scope of the Directorate of Contracting's report included 45 purchase orders selected from purchase actions awarded during the first 9 months of fiscal year 1990. The Directorate of Contracting's review did not include awards representative of all small purchases and did not comply with the requirements of the Defense Logistics Acquisition Regulation to include an evaluation of the reasonableness of price. The review consisted of an examination of file documentation and the type of discrepancies noted included "Block 11 of the DD Form 1155 should be checked," "DPSC Form 3816 missing complete addresses," and "Block 11 of DD Form 1155 missing quote date."

Internal control program. The Directorate of Contracting established an internal control program, including an internal management control review of administrative functions, to ensure that the procurement process was effectively and efficiently managed. The review of administrative functions was designed to determine whether the internal controls were adequate enough to prevent and detect the occurrence of potential risk.

The FMFIA requires managers to implement a comprehensive internal control system to provide reasonable assurance that programs and administrative activities are effectively carried out in accordance with the objectives of the FMFIA. To implement the FMFIA, DLA designated seven administrative functional areas in the Directorate's Contracting and Production Division for inclusion in the internal control reviews. These functional areas were solicitation, evaluation and award, postaward, funding, price negotiation or price reasonableness, safeguarding sealed bids and proposals, and administering the geographic distribution report. Questionnaires were developed to test the effectiveness of internal controls in these seven functional areas and a review was completed in July 1990. This review included only large purchase procedures in the Drug, Equipment, and Hospital and Surgical Branches. A total of 15 large purchases were selected for the test. The internal management control review found that the overall risk vulnerability for the

seven functional areas had been reduced since the June 1988 vulnerability assessment; however, these conclusions related to large purchase procedures only. The FMFIA does not define what types of procurements should be reviewed; however, small purchases account for about 86 percent of the awards, 79 percent of the line items, and 10 percent of the value of total procurement during the 12 months ended March 31, 1990.

Directorate of Contracting personnel decided not to include an assessment of small purchases under the automated procurement system because it deviated significantly from manual buying techniques and because the automated system was scheduled for further review. The subsequent review did not include an evaluation of automated or manually processed small purchases for the functional areas identified for coverage under the FMFIA. We concluded that although internal control weaknesses had been identified in previous procurement management reviews, the internal control reviews did not ensure that purchase orders were reviewed for compliance with appropriate procurement regulations, including documentation for price reasonableness determinations. Internal control reviews also did not detect that all procurement actions were advertised in the CBD when required, and that postaward price analyses were not performed in accordance with DLA regulations.

Conclusion

Large purchases were in compliance with procurement regulations except that in one Branch, the Individual Contracting Action Report was not prepared, and the mechanized bidders' lists were not properly maintained to reflect current sources of supply. Corrective action was taken to ensure that the Individual Contracting Action Report was completed. In addition, corrective action was being taken by Directorate personnel to maintain the mechanized bidders' lists using vendor input; however, procedures were still insufficient to ensure that vendors on the buyers' manual bidders' lists were included in the mechanized system.

The solicitation process did not include prior awardees in small purchases and did not always include a comparison to the previous price paid. Also, price reasonableness determinations were not documented in purchase order files. Use of Federal Supply Schedules for direct delivery purchases generally resulted in the procurement of materiel at fair and reasonable prices and should be used as the first source of supply. In addition, use of existing blanket purchase agreements would reduce administrative costs associated with making awards and the associated cost of processing vendor invoices.

Strengthening internal controls to include supervisory reviews of small purchases before purchase orders are awarded could lead to immediate identification and correction of noted deficiencies in the procurement process, such as the requirement to advertise solicitations in the CBD. Monthly postaward price analyses

should be completed to ensure that price reasonableness determinations for competitive and noncompetitive awards are properly documented and supported in the purchase order files.

RECOMMENDATIONS FOR CORRECTIVE ACTION

We recommend that the Commander, Defense Personnel Support Center:

1. Develop controls to ensure that procedures are properly implemented to establish and maintain mechanized bidders' lists to incorporate existing manual bidders' mailing lists maintained by the buyers, additional vendor requests to be added to the mailing list, and bid results from subsequent solicitations and awards.

2. Require that noncompetitive price reasonableness determinations are documented in purchase files, include prior awardees in solicitations, and use existing base prices in price reasonableness determinations for automated and manual purchase awards.

3. Increase the use of Federal Supply Schedules and blanket purchase agreements for direct vendor delivery items, incorporate the mechanized data base being developed by the Department of Veterans Affairs, and identify and report to the Department of Veterans Affairs and the General Services Administration items with recurring or repetitive small quantity demand for inclusion in future Federal Supply Schedules.

4. Develop adequate preaward small purchase review procedures to ensure, on a random basis, that small purchase awards are in compliance with all requirements of the Federal Acquisition Regulation, including required notices in the Commerce Business Daily, and price reasonableness is adequately determined and supported by preaward documentation.

5. Require that monthly postaward price analysis reviews are conducted and that all awards, including Automated and Customer Support Branch awards, are considered in the review process, and that identified deficiencies are summarized and tracked through resolution.

MANAGEMENT COMMENTS

On February 27, 1991, a draft of this report was provided to the Director, Defense Logistics Agency and the Commander, Defense Personnel Support Center. As of May 20, 1991, comments on Recommendation A.3. had not been received from the Defense Logistics Agency. DLA concurred in the other recommendations for

corrective action and in the internal control weaknesses identified in the report.

The Deputy Assistant Secretary of Defense, Health Affairs (Medical Readiness) concurred in the recommendations for corrective action.

Copies of the responses are included in Part IV of the report.

AUDIT RESPONSE

The management actions completed or ongoing are considered responsive. DoD Directive 7650.3 requires that all audit recommendations be resolved promptly. Therefore, we request that the Director, Defense Logistics Agency provide comments on Recommendation A.3. to the final report by July 29, 1991. The comments should indicate concurrence or nonconcurrence in the recommendation and the associated monetary benefits.

B. REPORTS OF DISCREPANCY FOR DIRECT VENDOR DELIVERY AWARDS

Reviews of reports of discrepancy for direct vendor delivery awards by personnel in the Directorate's Production Operations Branch were ineffective and inconsistently applied, did not identify potential patterns of vendor abuses, and were not consistent with the provisions of Fast Payment purchases. These conditions existed because established procedures were not followed to identify the root causes of reported discrepancies and to document and report discrepancies, including potential procurement abuse, for followup to vendors, customers, supply depots, and contracting personnel. In addition, there were no management reviews to ensure that reports of discrepancy were processed properly and that appropriate action was taken. As a result, reports of discrepancy for materiel that was nonconforming, materiel that was never received, and materiel that was received in a condition or quantity other than ordered were routinely accepted as valid without recourse to the shipping activities (vendors and supply depots) and vendors continued to receive awards because patterns of vendor abuse were not identified.

DISCUSSION OF DETAILS

Background

Medical materiel procured for direct delivery to hospitals and medical facilities are authorized for procurement under Fast Payment procedures. The FAR prescribes that payment for Fast Payment purchases can be made based on a vendor's certification that the materiel was shipped to the customer in the quantity and specifications of the procurement award. Vendors assume all responsibility to replace, repair, or correct supplies not received at the destination; damaged in transit; or not conforming to purchase requirements. Materiel can be shipped directly to a customer or to a storage depot for consolidation and shipment. The Fast Payment procedure provides 180 days for customers to request replacement of materiel that is not in conformance with the terms of the purchase.

The Military Departments and DLA issued a joint regulation, DLA Regulation 4140.55, "Reporting of Item and Packaging Discrepancies," that establishes the policies and procedures for submitting reports of discrepancy. Standard Form 364, "Report of Discrepancy," provides shipping and receiving activities a means for reporting discrepancies related to the condition of materiel, supply documentation, misdirected materiel, overages and duplicate shipments, packing and marking discrepancies, product quality deficiencies, shortages, and incorrect materiel. The information on the report of discrepancy is provided to the Directorate to determine the cause of the discrepancy, to effect corrective action, and to prevent recurrence.

Defense Personnel Support Center Regulation 4140.24, "Processing of Customer Generated SF364, Report of Discrepancy," supplements the DLA regulation and includes general and specific procedures for the receipt, review, and timely processing of reports of discrepancy, adjustments to accountable records and customer billing, and for initiating claims against vendors. The regulation also requires reviews by the Directorate's Management Support Office to detect trends and initiate corrective actions.

Customer and Depot Complaint System (CDCS)

The Center installed an automated data base (CDCS), a SAMMS system, to monitor all types of discrepancy reports received from customers and storage depots. This monitoring was to be done from the initial receipt of the discrepancy report through the resolution of the discrepancy. In addition to reports of discrepancy (SF364) there are five other forms that customers and depot personnel can use for reporting discrepancies. These forms include discrepancy in shipment reports, quality deficiency reports, reporting and processing medical materiel complaints and quality improvement reports, storage quality control reports, and government industry data exchange program alerts. The data base was started in April 1987 and totaled 98,845 discrepancy reports as of July 1990. For the 12 months ended March 31, 1990, the Center received 24,804 discrepancy reports. Appendix C provides a breakout of these discrepancy reports by the type of document submitted and by the type of discrepancy.

We reviewed the CDCS file for the 337 sample awards discussed in Finding A. For 49 of the awards we identified 84 discrepancy reports, 80 for stock replenishment awards, and 4 for direct vendor delivery awards. Of the 80 discrepancy reports for stock replenishment awards, 41 were attributed to packaging problems, 14 to product quality deficiencies, 7 to materiel shortages, and the remaining 18 to various other reasons. Materiel with packaging problems required remarking and bar coding. Storage depot personnel corrected these deficiencies and vendors were not asked to provide reimbursement for these deficiencies. Product quality deficiency reports were received from customers for materiel received from storage depots and were either resolved with the vendor or were still under investigation at the time of our audit. Storage depots submitted materiel shortage reports of discrepancy after receiving partial shipments that were incorrectly identified as final shipments.

The four discrepancy reports for direct vendor delivery awards were submitted for the following reasons.

o The customer stated that only two of three line items awarded on a single purchase order were received. The two items received cost $12 and $35, while the item not received cost $180. (Production personnel did not request replacement from the vendor despite the provisions of the Fast Payment purchase).

o Materiel was not received by the customer even though the Defense Depot, Mechanicsburg, to which the vendor had shipped the materiel for consolidation and shipment, acknowledged receipt of the materiel.

o The vendor offered a substitute item and the buyer accepted the item as an appropriate substitute even though the item did not meet the technical specification of the item requested.

o The vendor shipped the materiel twice and the materiel was returned even though the customer was not required to return vendor overshipments that were less than $250.

Reports of Discrepancy For Direct Vendor Delivery Under Fast Payment Procedures

Based on data in the CDCS, we reviewed reports of discrepancy, SF364, resulting from direct vendor delivery procurements that were awarded under Fast Payment procedures. We judgmentally selected 15 vendors that had a large number of reports of discrepancy submitted against their awards during the 12 months ended March 31, 1990. We further limited our review to the four types of discrepancies with the greatest possibility of vendor abuse: condition of materiel, overages, shortages, and wrong materiel. As shown below, these four types of discrepancies account for 85 percent of the total number of reports of discrepancy submitted against the 15 vendors selected.

Type of Discrepancy	Number of Reports	Percent
Condition of Materiel	230	13.0
Overages	146	8.3
Shortages	890	50.4
Wrong Item	234	13.3
Other Categories	266	15.0
Total	1,766	

For the 15 vendors, we selected 161 reports of discrepancy and, where possible, determined the root cause for each report of discrepancy based on available documentation in procurement, production, supply, and financial files. In addition, we reviewed records at the Defense Depot, Mechanicsburg, for materiel that was shipped to the depot for consolidation and forwarding to customers. We categorized the types of discrepancies into four problem areas: vendor related problems, procurement related problems, shipment related problems, and discrepancy reports for which we could not determine the root cause or that should not have been submitted. We also determined what, if any, actions were taken by production personnel to properly identify the reported discrepancy, make appropriate disposition, and report discrepancy trends to appropriate personnel to avoid recurrence of the problem. These areas are discussed below and are further categorized in Appendix D.

Vendor related problems. We identified 40 reports of discrepancy that resulted directly from vendor related actions. These included materiel shipped with insufficient shelf-life, incorrect materiel, materiel damaged in transit, and duplicate quantities or overshipments. The vendors were contacted only in 10 of the 40 cases. There was no documentation indicating why the vendors in the other 30 cases were not contacted. For 6 of the 10 cases where the vendors were contacted they agreed to replace the materiel when the deficient materiel was returned. In 3 of the 10 cases, the vendor stated that the materiel shipped was a substitute item or a different unit of issue because the materiel was manufactured in two different divisions of the same company with different part numbers or that the product requisitioned had been discontinued and was replaced by a different unit of issue. In the remaining case, the vendor stated that the materiel did not have an expiration date. There was no documentation available to determine whether the customers returned the materiel and whether the vendor shipped the replacement materiel.

Procurement related problems. In 23 cases, the reports of discrepancy resulted from errors in the procurement process. In 20 of the 23 cases, the discrepancy resulted from differences in the unit of issue. Many of the items procured in the Directorate are packaged in nondiscrete or multi-pack units, such as cases, packages, or bottles, that require specific quantity counts when ordering. In 10 of the 20 cases identified to the unit of issue, there was sufficient information in the solicitation process that the vendor could have used to identify the correct unit of issue and quantity of pack. In the remaining 10 cases, the description was vague and resulted in the buyer ordering a quantity that was not what the customer expected to receive. In 1 of these 10 cases, the vendor stated that the request for replacement was submitted after its 10-day return policy and was, therefore, not replaceable.

In two cases, buyers awarded a purchase order for the wrong item although there was sufficient information at the time of the award to know that the wrong item was being procured. In the last case, the materiel was ordered from a vendor who later stated that the item could not be identified. Production personnel did not notify supply, technical, and procurement personnel of the problems identified. Consequently, the differences in unit of issue and unit of pack were not researched to determine the reason for the errors, and no actions were taken to correct the incorrect data.

Shipment related problems. Fifty-nine of the discrepancies were attributed to the total or partial nonreceipt of materiel. In 27 cases no materiel was received and in the remaining 32 cases materiel was only partially received. Materiel was shipped either directly from the vendor to the customer, generally by parcel post, or from the vendor through a supply depot for consolidation and forwarding to the customer. In 5 of

the 59 cases, the vendor billed only for the quantity actually sent and received but the customer was billed by the Center for the full amount because the consolidation depot acknowledged receipt of the entire quantity. Because depot personnel did not physically open packages to count the contents before forwarding the materiel to customers, acknowledged quantities were based on either the total contract award quantity or on physical markings on the outside of the packages.

Instead of contacting all vendors for the 59 cases, production personnel contacted vendors in 35 of the 59 cases involving materiel shortages. Only one of the vendors promised to ship the missing quantities involving 5 of the cases. This vendor stated that the materiel was on backorder and would be shipped within the next few weeks. The vendor had invoiced and had been paid for the entire quantity ordered and not the actual quantity shipped. Invoicing for more than the quantity actually shipped is contrary to the provisions of the Fast Payment purchases and could have resulted in the removal of the vendor from receiving further awards. For the other 30 cases, the vendor provided shipment information that was passed on to the customer. The reports of discrepancy were closed; however, receipt status was not verified by the Center.

Other discrepancy reports. In 12 of the remaining 39 cases, customers submitted reports of discrepancy and then canceled the reports after the missing materiel was received or when the materiel was found to be the correct quantity. In some of these 12 cases, the customer miscounted the materiel or matched the materiel received to the wrong requisition. In 10 of the 39 cases, materiel was not received by the customers and the vendors did not submit invoices for payment. However, shipment data were posted to the file and the customers were billed by the Center for the materiel. Procurement, supply, and data systems personnel could not explain why the shipment data were posted and who had posted the data. In 14 of the 39 cases, procurement and comptroller personnel were unable to provide us sufficient documentation to make an informed evaluation. In the remaining three cases, customers were not billed for the materiel that was reported as not received. The reports of discrepancy should not have been submitted. Instead, the customers should have submitted standard followup requests to obtain delivery status.

Validity of CDCS Data

The data contained in the CDCS data base were not always accurate and either left out data elements or contained incorrect information. For the 15 vendors reviewed, we found 15 cases where the value of the report of discrepancy was recorded in the system at over $1 million each. In 2 of the 15 cases, documentation was not available to determine the correct value of the report of discrepancy; however, we determined that 13 of the 15 cases were actually valued at less than $5,000 each. The discrepancy reports for the four direct vendor delivery purchases, discussed

in our review of the sample awards, were incorrectly identified as discrepancies from storage depot receipts. In addition, the cause code provided by production personnel frequently did not represent the actual cause of the discrepancy. The cause code attributed to over 60 percent of the reports of discrepancy in the CDCS data base was "Other/Does Not Apply" that indicated to us that the cause of the reported discrepancy was not considered by management to be significant to the review and analysis of the reports of discrepancy. Based on our review of the CDCS data base, it appeared that appropriate supply, procurement, and comptroller personnel were not advised of these conditions and had not initiated corrective action. These inaccuracies, omissions, and misclassifications in the CDCS file are indicative of the inadequate review of the reports of discrepancy and the need for improved internal controls over their disposition, including emphasis on detecting trends and initiating positive corrective action as required by the Center regulation.

Management Support Office Reviews. Defense Personnel Support Center Regulation 4140.24 requires that semi-annual reviews of completed reports of discrepancy be conducted by the Directorate's Management Support Office with a special emphasis on detecting trends, evaluating management actions, and initiating positive corrective actions.

Management Support Office personnel told us that they had not performed any evaluations of the processing of reports of discrepancy and that there were no plans to review this area in the future. In addition, Production personnel told us that they had not developed any trend analyses of the reports of discrepancy recorded in the CDCS data base.

RECOMMENDATIONS FOR CORRECTIVE ACTION

We recommend that the Commander, Defense Personnel Support Center:

1. Require that vendors replace, repair, or correct supplies not received at the destination, damaged in transit, or not conforming to purchase requirements in accordance with the provisions of Fast Payment awards.

2. Establish controls, including Management Support Office reviews, to ensure that the analysis and disposition of reports of discrepancy include:

a. identifying the root cause of the reports of discrepancy,

b. advising appropriate personnel of the problems identified so that corrective action can be taken,

c. taking action to prevent vendors from receiving further awards when patterns of vendor abuse are identified, and

d. developing trend analyses of the results of the reviews by the Management Support Office to avoid their recurrence.

MANAGEMENT COMMENTS

The Director, Defense Logistics Agency and the Deputy Assistant Secretary of Defense, Health Affairs (Medical Readiness) concurred in the recommendations for corrective action. Copies of the responses are included in Part IV of the report.

AUDIT RESPONSE

The comments provided by the Defense Logistics Agency and the Deputy Assistant Secretary of Defense, Health Affairs (Medical Readiness) are considered responsive.

PART III - ADDITIONAL INFORMATION

APPENDIX A - Number and Value of Medical Materiel and Equipment Procurements - Total and Sample Reviewed

APPENDIX B - Statistical Sampling Plan and Projection

APPENDIX C - Customer and Depot Complaint System - Discrepancy Reports Processed

APPENDIX D - Classification of Discrepancy Reports Reviewed

APPENDIX E - Summary of Potential Monetary and Other Benefits Resulting From Audit

APPENDIX F - Activities Visited or Contacted

APPENDIX G - Report Distribution

APPENDIX A: NUMBER AND VALUE OF MEDICAL MATERIEL AND EQUIPMENT PROCUREMENTS - TOTAL AND SAMPLE REVIEWED

Total Procurements of Medical Materiel and Equipment
Defense Personnel Support Center, Directorate of Medical Materiel
April 1, 1989 through March 31, 1990

Branch	Total			Large 1/			Small 2/			FSS 3/		
	Awards	Lines	Value	Awards	Lines	Value	Awards	Lines	Value	Awards	Lines	Value
Drug	3,556	10,778	$445,265,150	1,820	5,791	$278,800,473	907	2,243	$9,229,489	829	2,744	$157,235,188
Equipment	9,500	17,941	$185,425,191	730	2,741	$160,358,456	4,875	10,325	$7,599,571	3,895	4,875	$17,467,164
Hospital/Surgical	4,062	14,315	$171,031,317	1,355	6,818	$121,415,751	2,457	6,607	$20,577,688	250	890	$29,037,878
Automation & Customer Support	80,477	110,021	$59,119,232	8	8	$411,410	75,617	102,185	$46,246,901	4,852	7,828	$12,460,921
Customer Support Section	30,402	59,942	$41,358,281	8	8	$411,410	25,542	52,106	$28,485,950	4,852	7,828	$12,460,921
Automation Section	50,075	50,079	$17,760,951				50,075	50,079	$17,760,951			
Total	97,595	153,055	$860,840,890	3,913	15,358	$560,986,090	83,856	121,360	$83,653,649	9,826	16,337	$216,201,151

Total Procurements Reviewed

Branch	Total			Large 1/			Small 2/			FSS 3/		
	Awards	Lines	Value	Awards	Lines	Value	Awards	Lines	Value	Awards	Lines	Value
Drug	64	196	$25,642,726	15	66	$17,015,861	36	78	$315,036	13	52	$8,311,829
Equipment	37	180	$22,354,850	22	161	$22,292,514	11	14	$26,457	4	5	$35,879
Hospital/Surgical	66	315	$16,755,616	34	123	$6,963,377	23	52	$273,240	9	140	$9,518,999
Automation & Customer Support	170	254	$465,163	5	5	$238,207	149	233	$88,549	16	16	$138,407
Customer Support Section	85	169	$427,621	5	5	$238,207	64	148	$51,007	16	16	$138,407
Automation Section	85	85	$37,542				85	85	$37,542			
Total	337	945	$65,218,355	76	355	$46,509,959	219	377	$703,282	42	213	$18,005,114

1/ Large Procurements Procedures - Acquisition of supplies, nonpersonal services, and construction from commercial sources; the aggregate amount expected to exceed $25,000.

2/ Small Procurements Procedures - Acquisition of supplies, nonpersonal services, and construction from commercial sources; the aggregate amount not expected to exceed $25,000.

3/ Federal Supply Schedules - Simplified process for obtaining commonly used supplies and services at prices associated with volume buying. Totals procurements reviewed include 6 awards over $25,000 valued at $16 million and 36 awards under $25,000 valued at $2 million.

APPENDIX B: STATISTICAL SAMPLING PLAN AND PROJECTION

Sampling Plan

The universe of awards from April 1, 1989, through March 31, 1990, was obtained from the Active Contract File and the Contract History File received from the Directorate of Medical Materiel, Defense Personnel Support Center. We stratified the universe of awards by procurement branch and type of award (contract, delivery order, purchase order, blanket purchase agreement, and Federal Supply Schedule) and statistically selected a random attribute sample with a 90-percent confidence level, ±5 percent, with an expected rate of occurrence not to exceed 20 percent. The sample was distributed among the four procurement branches as follows.

Branch	Large	Small	Total
Drug	30	45	75
Equipment	30	15	45
Hospital and Surgical	55	30	85
Customer Support and Automation	5	165	170
Total	120	255	375

Our sampling plan required a review of 120 large purchase awards -- contracts, delivery orders, and Federal Supply Schedule awards. Our review of 82 of the 120 awards (76 large purchases valued at $46.5 million, and 6 Federal Supply Schedules valued at $16.0 million) disclosed that, except for the maintenance of mechanized bidders' lists, the procurement process for large purchases generally complied with procurement regulations. Procurement decisions, including the reasonableness of price, were properly coordinated and approved and adequately documented in the procurement files. As a result, we discontinued further review of these type awards.

The large purchases included contracts, delivery orders, and Federal Supply Schedule awards over $25,000. Small purchases included manually awarded purchase orders, automated blanket purchase agreements, and Federal Supply Schedules under $25,000. We selected all contracts and delivery orders from the DD 350 data base (Individual Contracting Action Report Over $25,000) that were in excess of $1 million and randomly selected the balance of the sample from contract and purchase order logs maintained by the four procurement branches. (Appendix A includes our actual sample values).

Statistical Projection of Sample Results

We projected that $1.4 million of procurement funds annually, totalling $8.4 million for the Future Years Defense Program, could be put to better use in the Customer Support and Automation Branch if Federal Supply Schedules were used as the primary source of procurement. Our projection was made using procurement statistics for the 12 months ended March 31, 1990, and included

only the purchase orders and blanket purchase agreements issued by the Customer Support and Automation Branch as identified below. We applied the error rate (3.2 percent for the Customer Support Section, 4.7 percent for the Automation Section) encountered in our sample directly to the universe of items for this Branch. Detailed computations follow.

Total Awards - April 1, 1989 to March 31, 1990

Section	Awards	Lines	Dollar Value
Customer Support	19,162	36,774	$17,237,239
Automation	50,075	50,079	17,760,951
Total	69,237	86,853	$34,998,190

Total Sample Awards Reviewed

Section	Awards	Lines	Dollar Value
Customer Support	64	148	$51,007
Automation	85	85	37,542
Total	149	233	$88,549

Items Available on Federal Supply Schedules

Section	Awards	Lines	Purchase Price	FSS Price	Price Difference
Customer Support	8	15	$6,797	$5,188	$1,609
Automation	20	20	7,118	5,344	1,774
Total	28	35	$13,915	$10,532	$3,383

Projected Savings Using Federal Supply Schedules

Section	Awards	Lines	Dollar Value
Customer Support	2,395	3,727	$543,806
Automation	11,783	11,783	839,442
Total	14,178	15,510	$1,383,248

APPENDIX C: CUSTOMER AND DEPOT COMPLAINT SYSTEM - DISCREPANCY REPORTS PROCESSED

	Code & Type of Discrepancy	April 1987 - July 1990		April 1989 - March 1990	
		Number	Percent	Number	Percent
A	Stored Materiel	3,457	3.5	1,059	4.3
C	Condition of Materiel	19,635	19.9	4,035	16.3
D	Documentation	4,888	4.9	1,761	7.1
L	Wood Products	12	0.0	8	0.0
M	Misdirected Shipment	625	0.6	160	0.6
O	Overage	7,472	7.6	1,909	7.7
P	Packing Discrepancy	7,408	7.5	2,329	9.4
Q	Quality Deficiencies	14,946	15.1	2,029	8.2
S	Shortage	33,470	33.9	9,181	37.0
T	Technical Data	505	0.5	238	1.0
W	Wrong Item	5,866	5.9	1,897	7.6
X	Damaged	554	0.6	194	0.8
	Other Discrepancies	7	0.0	4	0.0
	Total	98,845		24,804	

	Code & Document Type	April 1987 - July 1990		April 1989 - March 1990	
		Number	Percent	Number	Percent
B	SF380 Type I	48	0.0	28	0.1
C	SF380 Type II	4,872	4.9	943	3.8
D	SF380 Type III	732	0.7	278	1.1
E	DD Form 1938 GIDEP Alert	356	0.4	129	0.5
F	DD Form 1938 GIDEP Safe Alert	1	0.0	0	0.0
0	SF368 Category I QDR	1	0.0	0	0.0
1	SF368 Category II QDR	194	0.2	68	0.3
2	Phone/Message	858	0.9	323	1.3
3	SF361 Discrepancy	3,024	3.1	1,189	4.8
4	Quality Audit	597	0.6	335	1.3
5	DD Form 1225	11,808	11.9	2,232	9.0
6	SF364 ROD (Direct Delivery)	11,039	11.2	4,505	18.2
7	SF364 ROD (Receipt from Stock)	42,294	42.8	9,964	40.2
8	SF364 ROD (Customer Return)	8,273	8.4	1,609	6.5
9	SF364 ROD (Depot Receipt)	14,748	14.9	3,201	12.9
	Total	98,845		24,804	

SF361 - Discrepancy in Shipment Report
SF364 - Report of Discrepancy
SF368 - Quality Deficiency Reports Category I or II
SF380 - Reporting and Processing Medical Materiel Complaints/Quality Improvement Report
DD Form 1225 - Storage Quality Control
DD Form 1938 - Government Industry Data Exchange Program Alert

APPENDIX D: CLASSIFICATION OF DISCREPANCY REPORTS REVIEWED

NUMBER OF CASES AND DESCRIPTION OF DISCREPANCY

Vendor Related Problems - 40 Cases

10 - The drug or pharmaceutical received did not have the required 75 percent of the shelf life remaining at the time of receipt. The materiel was retained by the customer without recourse to the vendor.

19 - The vendor shipped the wrong materiel and the customer retained the materiel without recourse to the vendor.

5 - The materiel was damaged in transit and the vendor was not requested to replace the damaged materiel.

6 - The vendor shipped the same materiel twice or shipped more than the quantity ordered. The materiel was retained by the customer.

Procurement Related Problems - 23 Cases

20 - The unit of issue requisitioned, ordered, and shipped did not agree and resulted in the submission of a report of discrepancy. The differences were not reported to supply and procurement personnel for corrective action. Vendors invoiced and were paid only for the quantity that was shipped.

3 - In one case, the Directorate ordered the materiel with the wrong electrical specifications. In another case, the materiel was received and identified as the incorrect materiel and the vendor could not provide the required materiel. In the last case, the vendor accepted the award for materiel then stated that the materiel could not be identified.

Shipment Related Problems - 59 Cases

Shipments through a consolidation point.

16 - **Total Nonreceipts.** Records indicated that materiel was received at a supply depot for consolidation and forwarding to the customer. We could not verify the accuracy of the quantity received at the depot; however, we found no evidence that a tracer was submitted by the customer.

22 - **Partial Nonreceipts.** Same as above except that only part of the total quantity ordered was received.

Direct shipments.

11 - **Total Nonreceipts.** The materiel was shipped directly from the vendor to the customer by parcel post. The vendor was not asked to provide valid proof of traceable shipment and did not replace the missing materiel.

10 - **Partial Nonreceipts.** Same as above except that only part of the total ordered was received. Materiel was shipped in multiple packages.

Other Discrepancy Reports - 39 Cases

12 - Customers submitted reports of discrepancy and later canceled the requests for the following reasons.

o Materiel was received in multiple shipments and the customer did not recognize the initial receipt as a partial shipment.

o Materiel was identified to the wrong requisition number and later corrected on the customers records.

o Shipping containers were incorrectly identified as the unit of issue instead of the individual multi-packages inside the containers.

10 - Vendors did not submit an invoice and were not paid; however, the customer was billed for the materiel. Activity personnel could not explain why shipment status was posted to the requisition history file. This action generated the billing to the customer.

14 - We could not perform an adequate review of these cases because all of the documentation was not available for our review.

3 - The customer was not billed for the materiel and submitted the report of discrepancy instead of requesting current supply status.

APPENDIX E: SUMMARY OF POTENTIAL MONETARY AND OTHER BENEFITS RESULTING FROM AUDIT

Recommendation References	Description of Benefits	Amount and/or Type of Benefit
A.1.	Increase the number of available bidders with the potential to increase competition and reduce costs of materiel purchases.	Nonquantifiable. Increased competition with potential for cost savings.
A.2.	Improve the ability to make informed procurement decisions regarding the reasonableness of price.	Nonquantifiable. Identify potential procurement problems and take appropriate corrective actions.
A.3.	Reduce the cost of materiel purchases and increase the efficiency of the automated procurement system by direct purchase from Federal Supply Schedules.	Funds put to better use. $1.4 million reduction annually in procurement costs totaling $8.4 million for the Future Years Defense Program, and other operating improvements and efficiencies.
A.4.	Improve visibility of buyers' performance and conformity to procurement regulations.	Nonquantifiable. Compliance with regulations and improved management of buyers' performance.
A.5.	Improve internal control over the procurement process including reasonableness of price determinations.	Nonquantifiable. Identify potential procurement problems and take appropriate corrective actions.
B.1.	Implement the Federal Acquisition Regulation and Defense Federal Acquisition Regulation Supplement requirements relating to	Nonquantifiable. Compliance with regulations and improved management of reports

APPENDIX E: SUMMARY OF POTENTIAL MONETARY AND OTHER BENEFITS RESULTING FROM AUDIT (cont'd)

Recommendation References	Description of Benefits	Amount and/or Type of Benefit
B.1. (cont'd.)	vendor responsibilities to replace missing or non-conforming materiel.	of discrepancy. Replacement of missing or non-conforming materiel.
B.2.	Identify patterns of potential vendor abuses and other problems related to the procurement process.	Nonquantifiable. Identify potential procurement problems and take appropriate corrective actions.

APPENDIX F: ACTIVITIES VISITED OR CONTACTED

Office of the Secretary of Defense

Office of the Assistant Secretary of Defense (Health Affairs), Washington, DC

Department of the Army

Department of the Army Surgeon General, Falls Church, VA
Headquarters, U.S. Army Health Services Command, Fort Sam Houston, TX
U.S. Army Medical Materiel Agency, Frederick, MD
U.S. Army Medical Department Activity, McDonald Army Hospital, Fort Eustis, VA

Department of the Navy

Department of the Navy, Bureau of Medicine and Surgery, Washington, DC
Navy Medical Materiel Support Command, Frederick, MD
National Naval Medical Center, Bethesda, MD

Department of the Air Force

Department of the Air Force Surgeon General, Bolling Air Force Base, Washington, DC
Headquarters, Air Force Office of Medical Support, Brooks Air Force Base, TX
Air Force Medical Logistics Office, Frederick, MD
Malcolm Grow USAF Medical Center, Andrews Air Force Base, MD

Defense Agencies

Defense Logistics Agency, Cameron Station, VA
Defense Personnel Support Center, Philadelphia, PA
Defense Depot Mechanicsburg, Mechanicsburg, PA
Defense Medical Standardization Board, Frederick, MD

Department of Veterans Affairs

Department of Veterans Affairs, Marketing Center, Hines, IL
Department of Veterans Affairs Medical Center, Philadelphia, PA

APPENDIX G: REPORT DISTRIBUTION

Office of the Secretary of Defense

Assistant Secretary of Defense (Health Affairs)
Assistant Secretary of Defense (Production and Logistics)
Assistant Secretary of Defense (Public Affairs)

Department of the Navy

Naval Audit Service

Department of the Air Force

Air Force Audit Agency

Defense Logistics Agency

Director, Defense Logistics Agency
Commander, Defense Personnel Support Center

Other Defense Agencies

Defense Contract Audit Agency
Defense Logistics Studies Information Exchange

Non-DoD Federal Organizations

Office of Management and Budget
U.S. General Accounting Office, NSIAD Technical Information Center

Congressional Committees:

Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
Senate Ranking Minority Member, Committee on Armed Services
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Ranking Minority Member, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Operations
House Subcommittee on Legislation and National Security, Committee on Government Operations

PART IV - MANAGEMENT COMMENTS

Deputy Assistant Secretary of Defense, Health Affairs (Medical Readiness)

Defense Logistics Agency

COMMENTS OF THE DEPUTY ASSISTANT SECRETARY OF DEFENSE, HEALTH AFFAIRS, (MEDICAL READINESS)

OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, D.C. 20301

HEALTH AFFAIRS
(MEDICAL READINESS)

19 MAR 1991

MEMORANDUM FOR DIRECTOR, LOGISTICS SUPPORT DIRECTORATE, DEPARTMENT OF DEFENSE INSPECTOR GENERAL

SUBJECT: Draft Audit Report on the Procurement of Medical Materiel and Equipment (Project No. OLD-0035)

We have reviewed the subject report and concur in your recommendations for corrective action.

Peter B. Collis, M.D.
Deputy Assistant Secretary of Defense

COMMENTS OF THE DEFENSE LOGISTICS AGENCY

DEFENSE LOGISTICS AGENCY
HEADQUARTERS
CAMERON STATION
ALEXANDRIA, VIRGINIA 22304-6100

IN REPLY REFER TO DLA-CI

6 May 91

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING, DEPARTMENT OF DEFENSE

SUBJECT: Audit Report on the Procurement of Medical Materiel and Equipment (Project No. 0LD-0035)

This is in response to your 27 Feb 90 memorandum requesting our comments pertaining to the audit of Procurement of Medical Materiel and Equipment (Project No. 0LD-0035). The attached positions have been approved by Ms. Helen T. McCoy, Deputy Comptroller, Defense Logistics Agency. Our response to Recommendation A.3. is not finalized yet and will be provided to you no later than 21 May 91.

8 Encl

Jacqueline G. Bryant
JACQUELINE G. BRYANT
Acting Chief, Internal Review Div.
Office of Comptroller

TYPE OF REPORT: AUDIT DATE OF POSITION: 3 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Procurement of Medical Materiel and Equipment (Project No. OLD-0035)

FINDING A: SOLICITATION, AWARD, REVIEW, AND INTERNAL CONTROL PROCEDURES. Large purchases (over $25,000) generally were properly documented, complied with procurement regulations, and for the awards tested, were bought at fair and reasonable prices. However, the mechanized bidders' lists, used for large and small stock replenishment purchases, were not properly maintained. Also, small purchase solicitation and award procedures governing the procurement of medical materiel and equipment for stock replenishment and direct vendor delivery to overseas customers were not always in compliance with procurement policy and regulations. These conditions existed because of the following reasons.

o Adequate procedures for one Branch had not been established to prepare required Individual Contracting Action Reports.

o Adequate controls had not been established to update mechanized bidders' lists to ensure access to additional vendors.

o Noncompetitive price reasonableness determinations were not supported by documentation and prior awardees were not always solicited in small purchase awards.

o Federal Supply Schedules and blanket purchase agreements were used only for a limited number of purchase awards.

In addition, internal controls did not adequately ensure that:

o Preaward reviews were made in compliance with applicable procurement regulations;

o Purchases in excess of $10,000 were always advertised in the Commerce Business Daily (CBD); and

o Postaward price analyses were conducted monthly to validate the reasonableness of price determinations.

As a result, management had no assurance that adequate competition was achieved and items were obtained at fair and reasonable prices. In addition, we estimated that savings of about $1.4 million could be achieved if additional procurements for direct deliveries were made using Federal Supply Schedules.

DLA COMMENTS: Concur. Refer to DLA comments on each recommendation.

MONETARY BENEFITS: None
DLA COMMENTS:
ESTIMATED REALIZATION DATE:
AMOUNT REALIZED:
DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

( ) Nonconcur. (Rationale must be documented and maintained with your copy of the response.)
(X) Concur; however, weakness is not considered material. (Rationale must be documented and maintained with your copy of the response.)
( ) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Diana Maykowskyj, x47936, 23 Apr 91
PSE REVIEW/APPROVAL: BILLY B. WILLIAMS, Acting Deputy Executive Director, Office of Contracting, x46401, 24 Apr 91

DLA APPROVAL: Helen T. McCoy, Deputy Comptroller

TYPE OF REPORT: AUDIT DATE OF POSITION: 3 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Procurement of Medical Materiel and Equipment (Project No. 0LD-0035)

RECOMMENDATION A.1.: We recommend that the Commander, Defense Personnel Support Center, develop controls to ensure that procedures are properly implemented to establish and maintain mechanized bidders' lists to incorporate existing manual bidders' mailing lists maintained by the buyers, additional vendor requests to be added to the mailing list, and bid results from subsequent solicitations and awards.

DLA COMMENTS: Concur. The following corrective action has been taken: (a) PCO Letter No. 115 issued 22 June 1990 (copy attached) provided that buyers would provide a bidders list with all stock PRs under $25,000. The letter also established that buyers would update their bidders list by sending additions and deletions to a focal point in the Operations Analysis Branch. (b) Reminders were issued at the February PCO meeting. This policy will be reinforced at the monthly PCO meetings.

DISPOSITION:
( ) Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None.
DLA COMMENTS:
ESTIMATED REALIZATION DATE:
AMOUNT REALIZED:
DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:
( ) Nonconcur. (Rationale must be documented and maintained with your copy of the response.)
(X) Concur; however, weakness is not considered material. (Rationale must be documented and maintained with your copy of the response.)
( ) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Diana Maykowskyj, x47936, 23 Apr 91
PSE REVIEW/APPROVAL: BILLY B. WILLIAMS, Acting Deputy Executive Director, Office of Contracting, x46401, 24 Apr 91

DLA APPROVAL: Helen T. McCoy, Deputy Comptroller

ATTACHMENT

INTER-OFFICE MEMORANDUM

IN REPLY REFER TO DPSC-RP (T. Cardella, Ext 5765)

JUN 22 1990

SUBJECT: Use of Bidders List and Labels for Stock PRs under $25,000, PCO letter No. 115

TO: All PCOs

1. PCOs are reminded that bidder lists should be rotated on small purchases. In order to assist you, the OAB will now provide you with a bidders list and labels for all stock PRs under $25,000.

2. You should ensure that these bidders lists are updated on a timely basis. Additions and deletions should be sent to Ruby Simpkins (OAB).

G. P. GALLUP
Acting Chief
Contracting & Production Division
Directorate of Medical Materiel

ATTACHMENT

DLA FORM JUL 62 111 PREVIOUS EDITION MAY BE USED UNTIL EXHAUSTED

TYPE OF REPORT: AUDIT DATE OF POSITION: 3 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Procurement of Medical Materiel and Equipment (Project No. 0LD-0035)

RECOMMENDATION A.2.: We recommend that the Commander, Defense Personnel Support Center, require that noncompetitive price reasonableness determinations are documented in purchase files, include prior awardees in solicitations, and use existing base prices in price reasonableness determinations for automated and manual purchase awards.

DLA COMMENTS: Concur. The following corrective action has been taken: (a) DPSC-P has resumed periodic reviews of small purchases to ensure documentation of price reasonableness and related matters regarding adherence to the Federal Acquisition Regulation (FAR). (b) Reinforcement of the need for compliance will be addressed at the next PCO monthly meeting. (c) SAMMS Procurement by Electronic Data Exchange (SPEDE) enhancement ensures that the previous awardee will be solicited.

DISPOSITION:
( ) Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None.
DLA COMMENTS:
ESTIMATED REALIZATION DATE:
AMOUNT REALIZED:
DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:
( ) Nonconcur. (Rationale must be documented and maintained with your copy of the response.)
(X) Concur; however, weakness is not considered material. (Rationale must be documented and maintained with your copy of the response.)
( ) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Diana Maykowskyj, x47936, 23 Apr 91
PSE REVIEW/APPROVAL: BILLY B. WILLIAMS, Acting Deputy Executive Director, Office of Contracting, x46401, 24 Apr 91

DLA APPROVAL: Helen T. McCoy, Deputy Comptroller

TYPE OF REPORT: AUDIT DATE OF POSITION: 3 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Procurement of Medical Materiel and Equipment (Project No. OLD-0035)

RECOMMENDATION A.4.: We recommend that the Commander, Defense Personnel Support Center, develop adequate preaward small purchase review procedures to ensure, on a random basis, that small purchase awards are in compliance with all requirements of the Federal Acquisition Regulation, including required notices in the Commerce Business Daily, and price reasonableness is adequately determined and supported by preaward documentation.

DLA COMMENTS: Concur. The following corrective action is planned or has been taken: (a) Periodic Small Purchase reviews were resumed by DPSC in March 1991. (b) DPSC will incorporate audit/review findings in PCO letter as appropriate. (c) DPSC will reinforce corrective policy as an agenda item in their monthly PCO meetings, a memorandum will be issued reinforcing the requirement to synosize requirements in excess of $10,000 in the Commerce Business Daily. (d) DPSC will include Small Purchases as part of their annual Internal Control Study in Aug 91 to ensure files are adequately reviewed by Contracting Officers. (e) DPSC will revise their small purchase file to incorporate a checklist of required actions for use by the buyers to further ensure compliance.

DISPOSITION:
(X) Action is ongoing; Final Estimated Completion Date: 30 Aug 91
( ) Action is considered complete.

MONETARY BENEFITS: None.
DLA COMMENTS:
ESTIMATED REALIZATION DATE:
AMOUNT REALIZED:
DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:
( ) Nonconcur. (Rationale must be documented and maintained with your copy of the response.)
(X) Concur; however, weakness is not considered material. (Rationale must be documented and maintained with your copy of the response.)
( ) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Diana Maykowskyj, x47936, 23 Apr 91
PSE REVIEW/APPROVAL: BILLY B. WILLIAMS, Acting Deputy Executive Director, Office of Contracting, x46401, 24 Apr 91

DLA APPROVAL: Helen T. McCoy, Deputy Comptroller

TYPE OF REPORT: AUDIT DATE OF POSITION: 3 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Procurement of Medical Materiel and Equipment (Project No. OLD-0035)

RECOMMENDATION A.5.: We recommend that the Commander, Defense Personnel Support Center, require that monthly postaward price analysis reviews are conducted and that all awards, including Automated and Customer Support Branch awards, are considered in the review process, and that identified deficiencies are summarized and tracked through resolution.

DLA COMMENTS: Concur. DPSC resumed the small purchase reviews as of March 1991. These reviews include awards by the Customer Support/Automation Branch.

DISPOSITION:
( ) Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None.
DLA COMMENTS:
ESTIMATED REALIZATION DATE:
AMOUNT REALIZED:
DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:
( ) Nonconcur. (Rationale must be documented and maintained with your copy of the response.)
(X) Concur; however, weakness is not considered material. (Rationale must be documented and maintained with your copy of the response.)
( ) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Diana Maykowskyj, x47936, 23 Apr 91
PSE REVIEW/APPROVAL: BILLY B. WILLIAMS, Acting Deputy Executive Director, Office of Contracting, x46401, 24 Apr 91

DLA APPROVAL: Helen T. McCoy, Deputy Comptroller

TYPE OF REPORT: AUDIT DATE OF POSITION: 3 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Procurement of Medical Materiel and Equipment (Project No. OLD-0035)

FINDING NUMBER B: REVIEW AND DISPOSITION OF REPORTS OF DISCREPANCY. Reviews of reports of discrepancy by personnel in the Directorate's Production Operations Branch were ineffective and inconsistently applied, did not identify potential patterns of vendor abuses, and were not consistent with the provisions of Fast Payment purchases. These conditions existed because established procedures were not followed to identify root causes of reported discrepancies and to document and report discrepancies, including potential procurement abuse, for followup to vendors, customers, supply depots, and contracting personnel. In addition, there were no management reviews to ensure that reports of discrepancy were processed properly and that appropriate action was taken. As a result, reports of discrepancy for materiel that was nonconforming, materiel that was never received, and materiel that was received in a condition or quantity other that ordered were routinely accepted as valid without recourse to the shipping activities (vendors and supply depots) and vendors continued to receive awards because patterns of vendor abuse were not identified.

DLA COMMENTS: Concur. Refer to DLA comments in Recommendations B-1 and B-2.

MONETARY BENEFITS: None.
DLA COMMENTS:
ESTIMATED REALIZATION DATE:
AMOUNT REALIZED:
DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:
( ) Nonconcur. (Rationale must be documented and maintained with your copy of the response.)
(X) Concur; however, weakness is not considered material. (Rationale must be documented and maintained with your copy of the response.)
( ) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Diana Maykowskyj, x47936, 23 Apr 91
PSE REVIEW/APPROVAL: BILLY B. WILLIAMS, Acting Deputy Executive Director, Office of Contracting, x46401, 24 Apr 91

DLA APPROVAL: Helen T. McCoy, Deputy Comptroller

TYPE OF REPORT: AUDIT DATE OF POSITION: 3 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Procurement of Medical Materiel and Equipment (Project No. OLD-0035)

RECOMMENDATION B.1.: We recommend that the Commander, Defense Personnel Support Center, require that the vendors replace, repair or correct supplies not received at the destination, damaged in transit, or not conforming to purchase requirements in accordance with the provisions of Fast Payment awards.

DLA COMMENTS: Concur. The following corrective action is planned or has been taken: DPSC conducted a training session for ROD clerks and their immediate supervisors on 19 Mar 91 and 20 Mar 91, which covered the DoD IG findings. Copies of the FAR clauses 52.213-1 were distributed and instructions given on Fast Payment procedures. Henceforth, DPSC will require vendors to replace, repair, or correct supplies not received at the destination, damaged in transit, or not conforming to purchase requirements in accordance with the provisions of Fast Payment Awards.

DISPOSITION:
( ) Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None
DLA COMMENTS:
ESTIMATED REALIZATION DATE:
AMOUNT REALIZED:
DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:
( ) Nonconcur. (Rationale must be documented and maintained with your copy of the response.)
(X) Concur; however, weakness is not considered material. (Rationale must be documented and maintained with your copy of the response.)
( ) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Diana Maykowskyj, x47936, 23 Apr 91
PSE REVIEW/APPROVAL: BILLY B. WILLIAMS, Acting Deputy Executive Director, Office of Contracting, x46401, 24 Apr 91

DLA APPROVAL: Helen T. McCoy, Deputy Comptroller

TYPE OF REPORT: AUDIT DATE OF POSITION: 3 May 91

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Procurement of Medical Matériel and Equipment (Project No. OLD-0035)

RECOMMENDATION B.2.: We recommend that the Commander, Defense Personnel Support Center, establish controls, including Management Support Office reviews, to ensure that the analysis and disposition of reports of discrepancy include:

a. identifying the root cause of the reports of discrepancy,

b. advising appropriate personnel of the problems identified so that corrective action can be taken,

c. taking action to prevent vendors from receiving further awards when patterns of vendor abuse are identified, and

d. developing trend analyses of the results of the reviews by the Management Support Office to avoid their recurrence.

DLA COMMENTS: Concur. The following corrective actions are planned or have been taken: (a) Copies of the list of codes were distributed to the ROD clerks with instructions to minimize the use of the OT Code (other/does not apply) and to use the remaining 29 codes believed more representative of the actual causes of ROD problems.
(b) Representatives from DPSC-M are working with the DPSC office of Telecommunications and Information Systems to establish a program that will analyze the CDCS data base and generate reports comparing offending contractors. These reports will be reviewed by management to identify problem areas and to determine the appropriate action to be taken. (c) The Management Support Office has commenced a study of RODS data from October 90 thru March 91. Data being used for this study is a direct download from CDCS. It is anticipated that this analysis will be completed by 15 June 1991. This effort will represent the first semiannual report required by DPSCR 4140.24.

DISPOSITION:
(X) Action is ongoing; Final Estimated Completion Date: 30 Sep 91
( ) Action is considered complete.

MONETARY BENEFITS: None
DLA COMMENTS:
ESTIMATED REALIZATION DATE:
AMOUNT REALIZED:
DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:
( ) Nonconcur. (Rationale must be documented and maintained with your copy of the response.)
(X) Concur; however, weakness is not considered material. (Rationale must be documented and maintained with your copy of the response.)
( ) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Diana Maykowskyj, x47936, 23 Apr 91
PSE REVIEW/APPROVAL: BILLY B. WILLIAMS, Acting Deputy Executive Director, Office of Contracting, x46401, 24 Apr 91

DLA APPROVAL: Helen T. McCoy, Deputy Comptroller

LIST OF AUDIT TEAM MEMBERS

Shelton R. Young, Director, Logistics Support
Gordon P. Nielsen, Deputy Director
Charles F. Hoeger, Program Director
William A. King, Project Manager
Bernard J. Siegel, Team Leader
Robert E. Schonewolf, Auditor
Joseph P. Girardi, Auditor