

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

MANAGEMENT DATA USED TO MANAGE THE
DEFENSE LOGISTICS AGENCY SUPPLY
MANAGEMENT DIVISION OF THE DEFENSE
BUSINESS OPERATIONS FUND

Report No. 94-128

June 14, 1994

Department of Defense

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Acronyms

| | |
|-------|---|
| DLA | Defense Logistics Agency |
| MIS | Management Information System |
| SAMMS | Standard Automated Material Management System |



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

June 14, 1994

**MEMORANDUM FOR COMPTROLLER AND CHIEF FINANCIAL OFFICER OF
THE DEPARTMENT OF DEFENSE
DIRECTOR, DEFENSE LOGISTICS AGENCY**

SUBJECT: Audit Report on Management Data Used to Manage the Defense Logistics Agency Supply Management Division of the Defense Business Operations Fund (Report No. 94-128)

We are providing this report for your review and comments. This audit is one of a series of audits conducted in response to the Chief Financial Officers Act of 1990. This report discusses management data used to manage the Defense Logistics Agency Supply Management Division of the Defense Business Operations Fund. Management comments on a draft of this report were considered in preparing the final report.

We revised Recommendation 4. based on management comments. DoD Directive 7650.3 requires that all recommendations be resolved promptly. We request that the Director, Defense Logistics Agency, provide comments on the revised recommendation by August 15, 1994. This report identifies no monetary benefits.

The courtesies extended to the audit staff are appreciated. If you have questions on this audit, please contact Mr. Charles F. Hoeger, Audit Program Director, or Mr. Terrance Wing, Audit Project Manager, at (215) 737-3881 (DSN 444-3881). The distribution of this report is in Appendix C. The audit team members are listed on the inside back cover of this report.

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Office of the Inspector General, DoD

Report No. 94-128
(Project No. 3LD-2004)

June 14, 1994

MANAGEMENT DATA USED TO MANAGE THE DEFENSE LOGISTICS AGENCY SUPPLY MANAGEMENT DIVISION OF THE DEFENSE BUSINESS OPERATIONS FUND

EXECUTIVE SUMMARY

Introduction. The Defense Logistics Agency Supply Management Division (the Division) of the Defense Business Operations Fund provides supplies and logistics services to DoD Components and other Government agencies. The Division manages approximately 3.5 million consumable type supply items; and its FY 1993 financial statements reported assets of \$14.1 billion, liabilities of \$1.2 billion, revenues of \$11.8 billion, and expenses of \$15.4 billion.

This audit is one of a series of audits being conducted in response to the Chief Financial Officers Act of 1990, which requires an annual audit of the financial statements of funds, such as the Division's. The related Chief Financial Officers Act audit work also includes evaluating financial and nonfinancial management data used to manage the funds. This management data audit was performed in conjunction with audits of the Division's inventory account (Project No. 3LD-2022), property, plant, and equipment account (Project No. 3LD-2023), and fund balance with the Treasury account (Project No. 4LE-2001) that were reported in the Division's FY 1993 financial statements. The audits are part of a building block approach to provide audit coverage of the Division. Inventory and property, plant, and equipment represent 81 percent (\$15.7 billion) of the Division's reported assets.

Objectives. The objectives of the audit were to determine whether critical management data are available and accurate and whether the Division's managers receive the data they need to operate, evaluate, and make financial and nonfinancial decisions.

Audit Results. The Division had a management information system that, except for management data related to unit cost, provided its managers reliable data that the managers used to operate, evaluate, and make financial and nonfinancial decisions (Part II). Unit cost reports provided to the Division's managers and the Comptroller of the DoD were inaccurate and untimely. Division and DoD personnel recognized that the unit cost data were inaccurate and used other sources for this information. However, the reports and the automated system used to generate the reports were not corrected (Part III).

Internal Controls. Internal controls and the implementation of the DoD Internal Management Control Program were not effective to ensure that unit cost management data reported to Division managers and the Comptroller of the DoD were accurate. Part I contains information on the controls assessed and Part III contains details on the material weaknesses.

Potential Benefits. This report does not claim any quantifiable monetary benefits. However, nonmonetary benefits include improving the accuracy of unit cost data used to make financial and nonfinancial decisions.

Summary of Recommendations. We recommend that the Director, Defense Logistics Agency, establish internal controls to verify that unit cost management reports are accurate and timely. We also recommend that procedures be developed to assign responsibilities and describe the process for accumulating, evaluating, and reporting unit cost data.

Management Comments. The Director, Defense Logistics Agency, concurred with all recommendations, except the recommendation that procedures be established to coordinate and reconcile the development of cost data used in the surcharge rate charged to customers and the unit cost process. The Director nonconcurred and stated that there is no direct linkage between unit cost reports and the development of surcharge or cost recovery rates used in the pricing process. The Comptroller of the DoD generally concurred with the recommendations and we considered his comments in preparing the final report. Details on management comments and the audit responses are in Part III of the report, and the full text of all management comments is in Part V.

Audit Response. In response to comments from the Director, Defense Logistics Agency, we revised the recommendation to have procedures established to require that the Defense Logistics Agency's accounting and budget divisions coordinate the development of unit cost goals. We request that the Director respond to the revised recommendation in this final report by August 15, 1994.

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This report was prepared by the Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, Department of Defense.

Part I - Introduction

Background

The Defense Logistics Agency (DLA) was established in 1961 as the Defense Supply Agency to reduce inventory management costs by consolidating the management of selected items of supply into a single agency. DLA's mission was subsequently expanded to provide specified logistics services to DoD Components. DLA provides worldwide support for needed supplies and repair parts to DoD Components and other Government agencies.

In FY 1992, DoD established the Defense Business Operations Fund. DLA's Supply Management Division (the Division) is a business area within the Defense Business Operations Fund. DLA's other business areas within the Defense Business Operations Fund are Distribution Depots, Reutilization and Marketing, Industrial Plant Equipment, and the Clothing Factory. The Division employs approximately 15,000 personnel to operate 6 inventory control points that manage about 3.5 million items of supply. Supply management includes materiel requirements determination, customer requisition processing, supply effectiveness, supply financial management, and inventory stock control.

The Division receives more than 25 million requisitions annually (approximately 75 percent of the total DoD orders for materiel) and receives authority to obligate funds based on the dollar value of sales to its customers. The Division's FY 1993 financial statements reported assets of \$14.1 billion, liabilities of \$1.2 billion, revenues of \$11.8 billion, and expenses of \$15.4 billion.

In March 1993, recognizing the need for DLA to reduce the overall cost of logistics support while still maintaining readiness, DLA restructured its headquarters. The restructuring was designed to facilitate prompt decision making to enable DLA to meet new challenges rapidly and effectively, and to continuously be responsive to customer requirements. Included in the restructuring was the establishment of a Corporate Performance Office that was tasked to develop an Executive Information System. The purpose of the Executive Information System is to bring visibility and focus to management data that define what is important to DLA customers. The system, expected to be completed in October 1994, will be an additional tool for DLA managers to oversee the entity's performance by tracking more than 70 management data indicators of quality, efficiency, and preparedness.

Objectives

The objectives of the audit were to determine whether critical management data were available and accurate and whether the Division's managers receive the data they need to operate, evaluate, and make financial and nonfinancial decisions.

Scope and Methodology

This audit is one of a series of audits being conducted in response to the Chief Financial Officers Act of 1990, which requires an annual audit of the financial statements of revolving funds, such as the Division. The related Chief Financial Officers Act audit work also includes evaluating financial and nonfinancial management data used to manage the funds. This management data audit was performed in conjunction with audits of the Division's inventory account (Project No. 3LD-2022), property, plant, and equipment account (Project No. 3LD-2023), and fund balance with the Treasury account (Project No. 4LE-2001) reported in the Division's FY 1993 financial statements. Inventories and plant, property, and equipment represent 81 percent (\$15.7 billion) of the Division's reported assets. The audits are part of a building block approach to provide audit coverage of the Division.

We examined the mission, goals, and objectives of the Division and determined whether they were defined in terms that allowed management to measure the extent to which the mission, goals, and objectives were accomplished. We also determined whether key management data were available for the Division managers to make major types of operational decisions. We did not evaluate how well the Division was run or how effectively individual elements of management data, once reported, were used.

Based on discussions with Division personnel and our analysis of the Division's operations, we selected 17 management indicators from the Division's management information system (MIS) that were considered key to evaluating the Division's mission accomplishment. For the 17 indicators, we determined whether the Division managers used the management data. We also tested selected transactions and determined whether internal controls were in place to provide management with reliable and accurate data to make financial and nonfinancial decisions. We also assessed the extent to which the financial statements or the financial accounting systems that support the statements were used in developing the selected indicators. We did not evaluate management data specifically identified to weapons system support items managed by the Division. The DLA weapons system support program is being evaluated under Project No. 3LD-0057. The accuracy of DLA administrative lead time is also being evaluated separately. See Prior Audits and Other Reviews for details of that project.

The audit was performed from March 1993 to March 1994 for three DLA managed commodities (Clothing and Textiles, Industrial, and Medical) and at DLA Headquarters. This financial related audit was made in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. Accordingly, the audit included such tests of internal controls as were considered necessary. As part of our review, we evaluated the reliability of computer-processed data used in managing the Division. We did not use statistical sampling procedures to conduct this audit. Except for errors in automated unit cost reporting, such as

Introduction

incomplete or inaccurate information, we considered the data to be reasonably reliable and accurate. Appendix C lists the organizations visited or contacted during the audit.

Internal Controls

Internal Controls Assessed. We evaluated internal controls applicable to ensuring that critical management data used to manage the Division were accurate and reliable. Specifically, we reviewed the Division's procedures and processes used to accumulate, report, and evaluate management data.

Internal Control Weaknesses. The audit disclosed material internal control weaknesses as defined by DoD Directive 5010.38, "Internal Management Control Program," April 14, 1987. Internal controls were not adequate to ensure that data in unit cost reports provided to the DLA management and the Comptroller of the DoD were accurate and provided on a timely basis. Unit cost reporting was not an assessable unit in DLA's implementation of the DoD Internal Management Control Program. The Division and the Comptroller of the DoD recognized that the unit cost reports were inaccurate; therefore they used information from other sources to accumulate and evaluate unit cost data. However, problems with the report and the system used to generate the report were not corrected.

Recommendations 1., 2., 3., and 4. in this report, if implemented, will correct the internal control weaknesses. No quantifiable monetary benefits were associated with those recommendations. A copy of the final report will be provided to the senior officials responsible for internal controls within the Office of the Secretary of Defense and DLA.

Prior Audits and Other Reviews

No prior audits or other reviews were conducted specifically to evaluate management data used to manage the Division. However, in the course of some audits and reviews, the accuracy of management data was reviewed in accomplishing the overall objectives of the audit or review.

An ongoing Inspector General, DoD, audit, Audit of DoD Administrative Lead Time (Project No. 3CD-0043), is assessing the accuracy of administrative lead times used in computing materiel requirements by the Military Departments and DLA. The audit is evaluating whether all appropriate data are included in the computations of administrative lead time.

Inspector General, DoD, Report No. 92-129, "Defense Stock Fund Financial Statements (Materiel Managed Under the Standard Automated Material Management System) for FY 1991," was issued on August 26, 1992. The report stated that, except for the uncertainties associated with \$355 million of inventory categorized as other than stock on hand, the \$7.7 billion of inventory managed under the Standard Automated Material Management System (SAMMS) reported in DLA's FY 1991 financial statements was reasonably accurate. The report recommended that DLA establish procedures and controls to ensure that inventory other than stock on hand was reasonably stated in the financial statements. Management concurred and stated that actions would be taken to correct the problems identified in the audit report. The dollar value of inventory is a Division key management indicator.

General Accounting Office officials testified before the Subcommittee on Readiness, Committee on Armed Services, House of Representatives, "Opportunities to Strengthen Management of the Defense Business Operations Fund", on May 13, 1993. The General Accounting Office officials stated that unit cost reports were not used by DoD managers because the accuracy of the reports was questionable. Unit cost is a Division key management indicator.

Other Matters of Interest

The Government Performance and Results Act of 1993 provides for the establishment of strategic and performance planning in the Federal Government. The Government Performance and Results Act requires all Federal agencies to develop strategic plans by FY 1997, to prepare annual plans with performance goals, and to report annually on actual performance versus goals. Strategic planning is a statement of an Agency's mission, goals, and objectives for the major functions and operations of the Agency. The strategic plan is designed to improve Federal program effectiveness and public accountability by focusing on results, service quality, and customer satisfaction. Performance planning establishes performance goals by defining the level of performance to be achieved; expresses those goals in an objective, quantifiable, and measurable form; and establishes performance indicators to be used in measuring or assessing the relevant outputs, service levels, and outcomes of each program activity. DLA was selected to be in the pilot program, scheduled to start in FY 1994, to test the implementation of the Government Performance and Results Act.

Part II - Adequacy of Management Data

Management Data

Except for management data related to unit cost, the Division had a management information system that provided its managers reliable data needed to operate, evaluate, and make financial and nonfinancial decisions. Issues related to unit cost management data are discussed in Part III of this report.

Mission of the Defense Logistics Agency

DLA's supply management mission is to provide effective and timely logistics support, at the lowest feasible cost, to DoD Components and other Government agencies in the event of mobilization, war, or other national emergency and in peacetime for those items of supply that it manages. A goal of DLA is to become the supplier of choice for its customers. The Division's responsibilities include materiel requirement determination, supply effectiveness, supply financial management, and inventory stock control.

Data Used to Assess the Division's Performance

To determine whether and to what degree the Division accomplishes its mission, the Division has an extensive automated MIS to satisfy recurring and specific needs of each management level throughout the Division. The MIS allows the Division to assess mission accomplishment against quantifiable goals, provides the ability to portray mission results to reflect improvement or regression, and permits the Division to compare mission results among its inventory control points and with other supply management business areas in the Defense Business Operations Fund. The MIS also provides data and input for reports to oversight organizations such as the Office of the Secretary of Defense, the Office of Management and Budget, and Congress.

DLA Regulation 7730.1, "DLA Management Information System," November 28, 1980, states that the objectives of the MIS are to:

- o establish efficient and economical processes for the identification, compilation, transmission, and presentation of management data to ensure that accurate and reliable information, in usable form, is available at the appropriate point of use in the organization on a timely basis;

- o provide each level of management with a factual basis to establish quantifiable goals, program objectives, and standards of performance; and

- o assess the status and operating effectiveness of ongoing mission programs relative to established goals and objectives, and identify actual or potential problem areas requiring special management attention.

Data elements in the MIS are uniquely defined and expressed in quantitative units, percentages, dollars, lines, etc. The source of the data elements varies according to the indicator being accumulated. The majority of the Division's data elements come from the supply, financial, and procurement subsystems of SAMMS. The SAMMS financial subsystem produces the materiel management trial balance used in preparing the Division's financial statements required by the Chief Financial Officers Act. The types of data in the MIS can be categorized as either inputs, outputs, or outcomes/results.

- o Inputs. The resources, time, and staff utilized for a program (for example, total funding, end strength, work hours).

- o Outputs. The work done or quantities produced (for example, line items shipped, dollar value of sales, number of procurement actions).

- o Outcomes/Results. The direct results achieved by the outputs being produced. Those measures assess the effect of outputs against given objective standards (for example, supply availability).

In addition to the MIS, the Division has a Customer Assistance Program that assesses customer satisfaction with the Division's performance. The program is implemented by a worldwide network of specialists whose mission is to provide customer assistance on a continuing basis. The specialists also are required to alert the proper Division element(s) of significant problems that could affect supply support or customer satisfaction.

Audit Approach

Based on discussions with Division personnel and our analysis of the Division's operations, we selected 17 management data elements (see Appendix A) from the Division's MIS that were considered key to evaluating the Division's mission accomplishment. For the 17 data elements, we determined whether the Division managers used the management data and whether controls were in place to provide reliable and accurate data to make financial and nonfinancial decisions. We also assessed the extent to which the financial statements or the financial accounting systems that support the statements were used in developing selected indicators.

Audit Results

Except for management data related to unit cost, the Division MIS provided its managers the reliable data needed to operate, evaluate, and make financial and nonfinancial decisions. Issues related to unit cost management data are discussed in Part III of this report.

Reliability of Management Data. Generally, the MIS data evaluated was electronically accumulated based on transactions processed through the SAMMS. To determine whether the MIS data were reliable, we identified and evaluated the internal controls in the SAMMS and in the MIS reporting process used to ensure that the data were accurate; and we performed tests of selected transactions for the data elements reviewed.

Internal Controls. Our evaluation of internal controls showed that the controls provided reasonable assurance that the MIS data were accurate.

SAMMS Controls.

- o Input transactions are validated and edited to ensure that duplicate transactions are not processed and that transactions are properly coded for processing.

- o Exception reports are generated to show transactions rejected from SAMMS input that must be reviewed, corrected, and reentered into the system.

- o SAMMS is an integrated system that automatically processes transactions to all affected subsystems. For example, a requisition for materiel automatically flows from the supply subsystem, where the issue is recorded to reduce inventory stock on hand, to the financial subsystem where the sale is recorded and the dollar value of the financial inventory general ledger account is reduced. This integration reduces the chances for processing errors, such as inventory being issued and the sale not being recorded.

MIS Reporting Controls. Management data reports generally provide trend analyses to show current versus prior periods. That type of reporting portrays significant variations between reporting periods and provides management the information needed to evaluate the data to determine whether data are correct or whether there are problems with the data.

Audit Tests. For the 17 indicators evaluated, we either judgmentally selected transactions to test to determine whether the transactions were properly recorded in the MIS or, where specific transactions were not available for analysis, we reviewed the process used to accumulate the MIS data. Our tests and analysis showed that the MIS data provided a reliable basis for management to manage the Division.

Use of MIS Data. We interviewed Division managers to determine whether they receive the data they need to manage the Division. The managers stated that the MIS data they received were sufficient to manage the Division and additional data were not needed. According to the managers, the data are primarily used to assess operations relative to established goals, to identify and isolate potential problems areas, and to ensure that authorized funding limits are not exceeded.

Part III - Finding and Recommendations

Unit Cost Management Data

Unit cost reports provided to the Division managers and the Comptroller of the DoD were inaccurate and untimely, and unit cost data were not consistent with data used to develop the Division's surcharge rates. The conditions occurred because the logic used to generate the reports was flawed, no controls existed to ensure that data in the unit cost report were accurate or that the report was prepared in a timely manner, and no procedures existed describing the reporting process and the assignment of responsibility to accumulate, verify, and report unit cost data. Additionally, data used to develop the Division's surcharge rates were not consistent with unit cost data used to manage the Division. As a result, the September 30, 1993, unit cost report overstated the Division's FY 1993 costs by a net amount of \$3.6 billion. The Division and DoD personnel recognized that the unit cost data were inaccurate and untimely and used other sources for that information. However, the unit cost reports and the automated system used to generate the reports were not corrected.

Background

To meet the needs of DoD within available resources, the Principal Deputy Comptroller of the DoD directed that a DoD-wide cost per output system be developed for selected functions of Defense Business Operations Fund entities to enhance the visibility of costs and contribute to better resource management.

The unit cost concept is that all costs incurred within a function should be related to an output of the function. The primary advantage of unit cost is that it provides management with visibility of cost drivers (those actions that contribute to the production and cost of an output) and allows management to track cost per output and to monitor productivity. Unit cost also encourages management to look at all costs so that managers can take actions to get the job done better and cheaper. The goal of unit cost is to capture data to provide the most accurate cost of each output or product. The success of the unit cost concept depends on how well it is supported, and the level of cost-consciousness reached and sustained by everyone in the process.

The primary output of the Division is the dollar value of materiel sales to customers. Unit cost is calculated by dividing the Division's total costs related to sales by the value of its sales. The Division's annual operating budget received from the Comptroller of the DoD provides a unit cost goal for the Division. The Division's FY 1994 unit cost goal is \$0.86 per dollar value of sales. To assist in managing its resources, the Division uses the DoD annual operating budget to establish budgets and unit cost goals for each of the commodities it manages. The Division and subsequently the Division's inventory control points receive funding authority based on the established unit cost goals and the level of sales achieved during the year of execution.

On October 15, 1990, the Principal Deputy Comptroller of the DoD issued guidance to implement the unit cost concept. The guidance recognized the absence of a uniform accounting system throughout the Department to capture unit cost data. The guidance was intended to establish a practical level of consistency and uniformity until a standard system was in place.

Data reported in the Division's unit cost report is accumulated in the Defense Finance and Accounting Service Defense Business Management System, based on information from various reporting entities (inventory control points, DLA headquarters, etc.). The data gathered in the Defense Business Management System is downloaded into the DLA Management Analysis Statistical System (part of the DLA overall MIS) where a computer program extracts data required to produce unit cost reports for each inventory control point and the Division.

Unit Cost Reports

Unit cost reports provided to the Division managers and to the Comptroller of the DoD were inaccurate and untimely, and unit cost data were not consistent with data used to develop the Division's surcharge rates. The conditions occurred because the logic used to generate the reports was flawed, no controls existed to ensure that data in the unit cost report were accurate or that the report was prepared in a timely manner, and no procedures existed describing the reporting process and the assignment of responsibility to accumulate, verify, and report unit cost data. Additionally, data used to develop the Division's surcharge rates were not consistent with unit cost data used to manage the Division.

Accuracy of Unit Cost Reports. Unit costs reports provided to the Division managers and the Comptroller of the DoD were inaccurate. We identified \$3.7 billion of overstated costs and \$132.5 million of understated costs in the Division's September 30, 1993, unit cost report. We also identified differences between the cost data in the unit cost report and the cost data in the Division's accounting records that were used to prepare the Division's financial statements. We attributed the inaccurate data to flawed computer logic used to generate the unit cost reports and a lack of controls to ensure the data were accurate.

Computer Logic. The computer logic to accumulate costs and compute costs was flawed.

- o The unit cost report for September 30, 1993, was overstated by \$3.7 billion because the computer spreadsheet formula used to calculate and summarize unit cost data had incorrectly counted some categories of costs twice.

- o For one cost item, warstoppers, the computer logic used to accumulate the cost was incorrect, and as a result, it understated unit cost data by \$64.4 million.

Unit Cost Management Data

- o Categories of costs in the unit cost report are based on cost data collected in the Defense Business Management System cost account codes. We found 45 cost account codes that had negative balances of \$18.9 million, which primarily represented adjustments of prior years' costs. Those transactions understated the current year's costs in the unit cost report.

- o September 1993 costs for one inventory control point were not included in the report, resulting in the costs being understated by \$49.2 million.

Adequacy of Controls. Controls were inadequate to ensure that unit cost data in the unit cost reports agreed with the data in the Division's accounting records. Unit cost data for depreciation, first destination transportation expense, and credits for materiel returns did not agree with the Division's accounting records. The unit cost report showed depreciation of \$7 million, first destination transportation of \$46 million, and credits and allowances of \$208.3 million; yet the DLA accounting system trial balance, which is used to prepare the financial statements, showed costs of \$5.3 million, \$35.9 million, and \$196.7 million, respectively, a difference of \$23.4 million.

Timeliness of the Unit Cost Report. Unit cost reports provided to the Division managers and the Comptroller of the DoD were untimely. We attributed the untimeliness to system changes, late reporting of cost information by the inventory control points, and a lack of controls to ensure that the unit cost reports were provided to managers in a timely manner. The Comptroller of the DoD sometimes received the monthly unit cost reports 15 to 20 days after the due date.

Written Procedures. No written procedures were established to describe the process used by the Division's headquarters and inventory control point personnel to accumulate, verify, evaluate, and report unit cost data. Procedures are needed to establish:

- o the process used to identify and allocate costs that are applicable to more than one of the Division's business areas (for example, DLA headquarters overhead) among all its business areas;

- o the process used to identify and allocate costs that are applicable to more than one of the Division's inventory control points (for example, DLA Administrative Support Center);

- o the responsibilities of the various functional entities, such as, DLA headquarters and the DLA inventory control points, in the unit cost process; and

- o the distribution of the unit cost report and timeframes for its distribution.

Consistency of Data. Unit cost data were not consistent with data used to develop the Division's surcharge rates. The inconsistency occurred because data used to develop the Division's surcharge rates were not the same unit cost data used to manage the Division. Each fiscal year the Division develops recommended standard prices for materiel sold to its customers. The purpose of

standard pricing is to recover all of the costs of operations and to maintain constant pricing during the future fiscal year to facilitate customer budgeting. The standard prices include materiel cost and a surcharge rate for wholesale and retail stock losses, transportation expenses, inventory control point and storage depot operations costs, and inflation. Except for the timing of the calculation, cost data used in determining the DLA unit cost goal and the surcharge rates should be obtained from the same sources and be approximately the same. Surcharge rates must be approved by the Comptroller of the DoD.

We compared the FY 1994 surcharge rates with comparable costs included in the FY 1994 unit cost goal developed by the DLA and approved by the Comptroller of the DoD to determine whether they were comparable. The total costs used in each process were basically the same. The total costs used to compute the surcharge rates were \$1.430 billion and costs used to develop the unit cost goal were \$1.413 billion. However, when we compared the costs associated with individual inventory control points, the costs between the two processes varied significantly. For example, there were estimated depot operations costs of \$73.1 million in the computation of the subsistence commodity surcharge while depot operations costs for the subsistence commodity used to calculate the Division's unit cost goal were \$4.3 million, a \$68.8 million difference. If the depot costs of \$4.3 million used to calculate the unit cost goal were accurate, the standard prices charged to customers for subsistence materiel would be overstated.

The difference in the costs used in each process occurred because of several reasons.

- o The surcharge cost data was gathered in March and April 1993. Unit cost goal information was gathered in the July and August 1993 time frame.

- o The sources of the information used to develop the surcharge data were based on estimates and accounting data received from the inventory control points. The unit cost goals were developed primarily on responses to budget call data provided by the inventory control points.

- o There were no procedures requiring coordination and reconciliation between the accounting division that prepared the standard pricing data and the budget division that developed the unit cost goal.

Recommendations, Management Comments, and Audit Response

We recommend that the Director, Defense Logistics Agency:

- 1. Review and revise the computer logic used to generate the unit cost report to validate that all costs are captured and accurately reported on the unit cost report.**

Unit Cost Management Data

Comptroller of the DoD Comments. The Comptroller partially concurred with the recommendation and stated that a standard periodic review process, including a comprehensive analysis of the cost collection process used to generate the unit cost reports, is being developed for use in all business areas. See Part V of the report for the complete text of the Comptroller's comments.

DLA Comments. DLA concurred with the recommendation and stated that the problem with the computer logic had been corrected and that action had been taken to ensure that the unit cost reports accurately reflect actual financial performance and that the reports are reconciled with the trial balance. DLA also stated that it continually updates cost account code mapping to ensure that the most accurate costs are recorded. See Part V of the report for the complete text of the DLA's comments.

2. Establish controls to verify that cost data are accurately reported in the unit cost report and that the unit cost report is provided to management in a timely manner. The controls should include periodic evaluations of the computer logic used to generate the unit cost report and reconciliations of the Defense Logistics Agency Headquarter's unit cost report to unit cost data available at the inventory control points and data in the Defense Logistics Agency's financial system used to produce financial statements required by the Chief Financial Officers Act.

Comptroller of the DoD Comments. The Comptroller concurred and stated that monthly reconciliations of unit cost reports will continue to be required. The Comptroller also stated that the Supply Management Unit Cost Working Group will evaluate the costs associated with the outputs of the business area.

DLA Comments. DLA concurred with the recommendation and stated that controls have been established to ensure that the unit cost reports are both accurate and timely. Daily status reports have been reinstated to monitor and correct problems in receiving data extracts from the Defense Finance and Accounting Service and information processing centers; and DLA will continue to coordinate efforts to resolve future problems as they occur. The scheduled completion date is November 30, 1994.

3. Establish standard operating procedures to describe the development, reconciliation, and maintenance of the unit cost report. The procedures should include the allocation procedures used to distribute common costs among the Defense Logistics Agency business areas and within the Supply Management Division, responsibilities of the various functional entities involved in the unit cost process, to include assignment of overall responsibility for the unit cost report; and distribution of the unit cost report and time frames for distribution.

Comptroller of the DoD Comments. The Comptroller concurred and stated that the DoD Comptroller, Financial Review and Analysis Directorate, will continue to work with the respective business areas' financial organizations to refine and improve the usefulness of unit cost reports as decisionmaking tools.

DLA Comments. DLA concurred and stated that the recommended procedures are in practice, but are not fully documented in a single source. Standard written operating procedures will be developed for the unit cost reporting process, and input and approval will be obtained from the Comptroller of the DoD. Scheduled completion date is November 30, 1994.

4. Establish procedures to require that the Defense Logistics Agency's accounting and budget divisions coordinate the development of unit cost goals. The procedures should provide that costs used to develop unit cost goals be reconciled with costs used to develop surcharge rates in order to verify that costs common to both are derived from the same sources of information (for example, the Defense Business Management System) and to ensure that consistent data were used to develop both and that significant variances, other than timing, are investigated.

Comptroller of the DoD Comments. The Comptroller partially concurred with the recommendation in the draft report to establish procedures to coordinate and reconcile the development of cost data used in the surcharge rate charged to customers and the unit cost process. The Comptroller stated that prices are established through the budget process and remain fixed during the year of execution. Unit cost budgets must reflect what is actually happening and managers must adjust to those unforeseen changes during the year of execution, or request changes to their unit cost budgets.

DLA Comments. DLA nonconcurred with the recommendation in the draft report. DLA stated that there is no direct linkage between unit cost reports and the development of surcharge or cost recovery rates used in the pricing process. Surcharge rates for a specific fiscal year are developed 13 to 15 months before the start of that fiscal year using source data from selected general ledger accounts, produced through the Defense Business Management System. Following all adjustments made by the Comptroller of the DoD, DLA finalizes the surcharge rates in May before the fiscal year begins in October. Unit cost reports contain the same information from the Defense Business Management System; and managers use those unit cost reports to formulate budgets and to determine whether current year execution is proceeding according to plan. However, the unit cost reports will not and cannot assist in developing cost recovery rates for future years, particularly when cost recovery rates must recover costs that are not incurred in the supply business area. The unit cost report is an inappropriate tool to consider for use in the surcharge development.

Audit Response. Based on DLA's comments, we revised our final report recommendation. We recognize that a timing difference exists between the development of the surcharge rates and the unit cost reporting process. Further, we agree that the surcharge rates recover some costs that are not included in the supply business area. The finding and recommendation addressed the development of the supply management unit cost goals, not actual costs collected to compare to the goals, and cost data used to compute the surcharge rates. Costs common to both unit cost goals and surcharge rates (for example, depot operations costs) should be derived from the same sources of information to ensure that consistent data are used to develop both and that significant variances, other than timing, are investigated. No procedures existed that

Unit Cost Management Data

required the budget division to coordinate the development of unit cost goals with the accounting division that is responsible for developing surcharge rates. We request that the Director, DLÁ, provide comments to the revised recommendation in response to the final report.

Part IV - Additional Information

Appendix A. Management Data Elements Evaluated

Administrative lead time. The time interval between identification of a need to buy and the issuance of a contract or delivery order.

Average time to process a quality deficiency report. The average time from receipt of a quality deficiency report until the processing of the report is completed.

Average time to process a report of discrepancy. The average time from receipt of a report of discrepancy until the report of discrepancy is resolved.

Average time from date requisition received to materiel shipped. The average time from receipt of a requisition until the date the materiel is shipped.

Customer complaints. Number of reports of discrepancy and quality deficiency reports to be processed.

Customer wait time (requisition date to date materiel received). Average time between the requisition date and the date materiel is received by the requisitioner.

Direct vendor delivery. The percentage of total gross sales shipped directly from vendors to requisitioners.

Inventory adjustments. Gross inventory adjustment rate as a result of materiel release denials and physical inventories accomplished by storage depots.

Inventory value. The acquisition cost of inventory on hand, serviceable and unserviceable, at a given time.

Materiel obligations (backorders) outstanding. Measurement of unsatisfied customer requests for materiel due to the lack of stock on hand or discrepant materiel.

Materiel returns. Value of excess inventory returned from customers' retail stock to wholesale inventory.

Production lead time. The time interval between the contract award date and the receipt date of the first significant delivery against the contract.

Sales. Cumulative total of all reimbursable issues at the standard unit price of the materiel issued.

Stock fund obligations. Cumulative obligations incurred during the current fiscal year for the purchase of materiel, transportation, inventory repair, or other expense payable by the Division.

Appendix A. Management Data Elements Evaluated

Supply availability. The percentage of requisitions that are immediately available for issue from stocked materiel.

Unit cost/cost per output. Comparison of all costs of an activity to the output of the activity.

Unit cost execution. Comparison of costs incurred by an activity to an activity's unit cost funding (actual versus budgeted).

Appendix B. Organizations Visited or Contacted

Office of the Secretary of Defense

Office of the Comptroller of the Department of Defense, Arlington, VA

Defense Agencies

Headquarters, Defense Logistics Agency, Alexandria, VA

Defense Construction Supply Center, Columbus, OH

Defense Electronics Supply Center, Dayton, OH

Defense Fuel Supply Center, Alexandria, VA

Defense General Supply Center, Richmond, VA

Defense Industrial Supply Center, Philadelphia, PA

Defense Personnel Support Center, Philadelphia, PA

Headquarters, Defense Finance and Accounting Service, Arlington, VA

Defense Finance and Accounting Service Center, Columbus, OH

Appendix C. Report Distribution

Office of the Secretary of Defense

Comptroller and Chief Financial Officer of the Department of Defense

Defense Logistics Agency

Director, Defense Logistics Agency
Commander, Defense Industrial Supply Center
Commander, Defense Personnel Support Center

Non-Defense Federal Organizations

Office of Management and Budget
U.S. General Accounting Office
National Security and International Affairs Division, Technical Information Center
National Security and International Affairs Division, Defense and National
Aeronautics and Space Administration Management Issues
National Security and International Affairs Division, Military Operations and
Capabilities Issues

Chairman and Ranking Minority Member of Each of the Following Congressional
Committees and Subcommittees:

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

Part V - Management Comments

Comptroller of the DoD Comments



OFFICE OF THE COMPTROLLER OF THE DEPARTMENT OF DEFENSE

WASHINGTON DC 20301-1100

MAY 18 1994


(Financial Systems)

MEMORANDUM FOR DIRECTOR, LOGISTICS SUPPORT, DOD INSPECTOR GENERAL

SUBJECT: Audit Report on Management Data Used to Manage the
Defense Logistics Agency Management Division of the
Defense Business Operations Fund (Project No. 3LD-2004)

This is in response to your memorandum dated April 5, 1994 requesting that we review and comment on your audit report (Project No. 3LD-2004). We partially concur with the report and have attached our comments. Please note that the Department recently completed a review of the Defense Business Operations Fund (DBOF). As a result of that review, a DBOF Improvement Plan was developed and approved by the Deputy Secretary of Defense. Actions identified in the Improvement Plan address many of the unit cost reporting problems identified in your audit. I have attached a copy of the DBOF Improvement Plan for your information.*

My point-of-contact on this matter is Ms. Phyllis Campbell. She may be reached on (703) 697-8281.


Richard F. Keevey
Deputy Comptroller
(Financial Systems)

Attachments

*Not included
because of
its length.

DRAFT AUDIT REPORT - DATED APRIL 5, 1994
Project No. 3LD-2004

MANAGEMENT DATA USED TO MANAGE THE DEFENSE
LOGISTICS AGENCY SUPPLY MANAGEMENT DIVISION OF THE
DEFENSE BUSINESS OPERATION FUND

* * * *

FINDINGS

- **Finding A: Flawed Computer Logic.** The computer logic to accumulate costs and compute costs was flawed.

DOD Comptroller Response: Partially concur. The overstatement of costs found by the DoDIG was primarily caused by systems problems. The unit cost reports are developed from data extracted from the Defense Business Management System (DBMS). Improper installation of systems changes during March 1993 affected the accuracy and timeliness of the unit cost reports throughout FY 1993. The systems changes were extensive and affected many processing routines within DBMS, one of which accumulated costs. Prior to these changes, the program logic to accumulate and compute costs was executing properly. The errors that resulted from these changes were resolved during March 1994 and the FY 1993 year end reports were adjusted to reflect the correct data.

- **Finding B: Inadequate Controls.** Controls were inadequate to ensure that unit cost data in the unit cost reports agreed with the data in the Division's accounting records. Unit cost data for depreciation, first destination transportation expense, and credits for materiel returns did not agree with the Division's accounting records.

DOD Comptroller Response: Partially concur. The DoD Comptroller requests a monthly reconciliation of the unit cost reports with the business area accounting reports. Significant adjustments to the unit cost reports should be reported to, and, if necessary, approval of mapping changes requested from the DoD Comptroller. During FY 1993, the reconciliation process was hampered by the inaccurate data on the unit cost reports. Under normal circumstances, the unit cost reports and the general ledger should agree. Further, mapping of cost codes to outputs is a significant factor in the determination of accurate costs. Just as inaccurate data effects the reconciliation process, inaccurate mapping of costs to outputs also complicates the process.

- Finding C: Timeliness of the Unit Cost Reports. Unit cost reports provided to the Division managers and the Comptroller of the DoD were untimely. We attributed the untimeliness to system changes, late reporting of cost information by the inventory control points, and a lack of controls to ensure that the unit cost reports were provided to managers in a timely manner. The Comptroller of the DoD sometimes received the month unit cost reports 15 to 20 days after the due date.

DOD Comptroller Response: Concur.

- Finding D: Written Procedures. No written procedures were established to describe the process used by the Division's headquarters and inventory control point personnel to accumulate, verify, evaluate, and report unit cost data.

DOD Comptroller Response: Concur.

- Finding E: Inconsistent Data. Unit cost data were not consistent with data used to develop the Division's surcharge rates. The inconsistency occurred because data used to develop the Division's surcharge rates were not the same unit cost data. Each fiscal year the Division develops recommended standard prices for materiel sold to its customers. The purpose of standard pricing is to recover all of the cost of operations and to maintain constant pricing during the future fiscal year to facilitate customer budgeting. Except for the timing of the calculation, cost data used in determining the DLA unit cost goal and the surcharge rate should be approximately the same.

DOD Comptroller Response: Partially concur. It is not clear that the comparison the audit makes between unit cost data used in developing the budget and in execution during the year is valid. There is a timing difference for revolving funds between unit cost goals used in a fiscal year and the budgeted cost recovery rates. One is based on data current a year before the fiscal year begins and is then fixed, and the other is developed using data current immediately before the year begins. FY 1994 costs were and will be re-estimated and reviewed at several points before, during, and after FY 1994. Therefore, while the data should arise from the same sources, they should never be precisely the same.

* * * * *

RECOMMENDATIONS

- Recommendation 1: Review and revise the computer logic used to generate the unit cost report to ensure that all costs are captured and accurately reported on the unit cost report.

DoD Comptroller Response: Partially concur. The DoD Comptroller's key objective is to develop meaningful unit cost data for use by all levels of management. A standard, periodic review process, including a comprehensive analysis of the cost collection process used to generate the unit cost reports, is currently being developed for use in all business areas.

- Recommendation 2: Establish controls to ensure that cost data are accurately reported in the unit cost report and that the unit cost report is provided to managers in a timely manner. The controls should include periodic evaluations of the computer logic used to generate the unit cost report and reconciliations of the Defense Logistics Agency Headquarter's unit cost report to unit cost available at the inventory control points and data in the Defense Logistics Agency's financial system used to produce financial statements required by the Chief Financial Officers Act.

DoD Comptroller Response: Concur. The DoD Comptroller will continue to require monthly reconciliation of unit cost reports from the business area. In addition, an immediate objective of the DoD Comptroller is a thorough evaluation of the cost associated with the outputs of the business area. This evaluation will be completed by the Supply Management Unit Cost Working Group as a part of the DoD Comptroller's initiative to reenergize unit cost. This working group is comprised of representatives from each of the Components, the Defense Logistics Agency, and the Defense Finance and Accounting Service. The key areas of concentration during the evaluation are identification and documentation of workload and cost data submission requirements and establishing control files.

- Recommendation 3: Establish standard operating procedures to describe the development, reconciliation, and maintenance of the unit cost report. The procedures should include the allocation procedures used to distribute common costs among the Defense Logistics Agency business areas and within the Supply Management Division, responsibilities of the various

functional entities involved in the unit cost process, to include assignment of overall responsibility for the unit cost report; and distribution of the unit cost report and time frames for distribution.

DoD Comptroller Response: Concur. The DoD Comptroller, Financial Review and Analysis Directorate, has overall responsibility for the development of unit cost reports. This office will continue to work with the respective business area's financial organizations to refine and improve the usefulness of these reports as decisionmaking tools. This includes the development of overall guidance on the report process, which will be applicable for use by all unit cost business areas. Also, the Financial Review and Analysis Directorate is working closely with DLA during the development of their procedures to assure that they adequately reflect current DoD Comptroller policies.

- Recommendation 4: Establish procedures to coordinate and reconcile the development of cost data used in the surcharge rate charged to customers and the unit cost process.

DoD Comptroller Response: Partially concur. Prices are established through the budget process and remain fixed during the year of execution. This stabilized rate policy serves to protect customers from unforeseen inflationary increases and other cost uncertainties and better assures customers that they will not have to reduce programs to pay for potentially higher than anticipated prices. Unit cost budgets, on the other hand, must reflect what is actually happening and managers must adjust to those unforeseen changes during the year of execution, or request changes to their unit cost budgets. In addition, because prices are set to recover cost over the long run, prices will contain adjustments to reflect prior year gains or losses which will not be reflected in unit cost budgets.

Defense Logistics Agency Comments



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



IN REPLY
REFER TO

DDAI

01 JUN 1994

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR INSPECTIONS,
DEPARTMENT OF DEFENSE

SUBJECT *OIG Audit Report on Management Data Used to Manage the Defense
Logistics Agency Supply Management Division of the Defense Business
Operations Fund (Project No. 3LD-2004)*

This is in response to your 5 April 1994 request

1 Encl

Jacqueline G. Bryant
for JACQUELINE G BRYANT
Chief, Internal Review Office

CC:
FO

Defense Logistics Agency Comments

TYPE OF REPORT: AUDIT

DATE OF POSITION:

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO: Draft Report on the Management Data Used to Manage the Defense Logistics Agency Supply Management Division of the Defense Business Operations Fund (Project No. 3LD-2004)

FINDING: Unit Cost Management Data. Unit cost reports provided to the Division managers and the Comptroller of the DoD were inaccurate and untimely and unit cost data were not consistent with data used to develop the Division's surcharge rates. The conditions occurred because the logic used to generate the reports was flawed, no controls existed to ensure that data in the unit cost report were accurate or that the report was prepared in a timely manner, and no procedures existed describing the reporting process and the assignment of responsibility to accumulate, verify, and report unit cost data. Additionally, data used to develop the Division's surcharge rates were not consistent with unit cost data used to manage the Division. As a result, the September 30, 1993, unit cost report overstated the Division's FY 1993 costs by a net amount of \$3.6 billion. Division and DoD personnel recognized that the unit cost data were inaccurate and untimely and used other sources for that information. However, the unit cost reports and the automated system used to generate the reports were not corrected.

DLA COMMENTS: Partially concur. The Supply Business Management Area Unit Cost Reports for September 1993 were inaccurate and untimely due to systems errors. However, since unit cost reports are utilized as one of several indicators in measuring performance, the \$3.6 billion error noted in the audit report had absolutely no material impact on DLA's execution of its FY 93 budget, particularly since the reporting error occurred in the final month of the fiscal year. By the time the error was reported, management could not have taken any corrective action with regard to FY 93 execution.

The Defense Finance and Accounting Service Financial Systems Activity (DFAS-FSA) is responsible for the development and maintenance of the Defense Business Management System (DBMS) and the extract process that provides cost data. DBMS is processed (for DPSC and DISC) by the Information Processing Center in Philadelphia (IPC-P). The September 1993 overstatement occurred because IPC-P either modified or improperly installed standard programs sent to them by DFAS-FSA HQ. DLA received corrected files for September 1993 data in March 1994. Subsequently, the September 1993 report was corrected on 24 March 1994.

Another reason for the overstatement was that the Defense Personnel Support Center's (DPSC) three commodities (C&T, Medical, and Subsistence) were consolidated in the DPSC-Noncommodity report. The supply center unit cost report summary then added all four DPSC pieces (C&T, Medical, Subsistence, and Noncommodity) with the other business

area commodities to derive the total cost. This error double counted DPSC's costs. As noted above, this error had no material impact on FY 93 budgetary execution. Management has taken corrective action to ensure that the reports accurately reflect actual financial performance and that the reports are reconciled with the trial balance.

The Business Management Directorate in the DoD Comptroller's Office and the Chief Financial Officer of DLA (DLA-FO) have oversight responsibility for the report. Within FO:

- the Management Information Systems Group (FOM) is responsible for accumulating and generating the report;
- the Program/Budget Group (FOB) is responsible for mapping the cost account code structure and analyzing the actual cost data; and
- the Financial Systems and Control Group (FOX) is responsible for the financial system integrity.

Collectively, we are developing written standard operating procedures for the unit cost report process and will obtain input and approval from the DoD Comptroller. On 14 Feb 1994, we directed DLA's Supply Centers to ensure the timely and accurate reporting of unit cost data. Further, we have instituted daily status reports to monitor and correct any problems in receiving the data extracts from DFAS and the Information Processing Centers. As a result, data transmission timeliness and accuracy have improved significantly. We will continue to coordinate efforts with DFAS and the IPCs to resolve future problems as they arise. We have initiated additional controls which will ensure consistency between financial reports and the unit cost reports. Prior to FY 94, OSD directed unit cost reports in expenses. Consequently, the database that produced the report was in expenses while the trial balance was in obligations, thus making reconciliation impossible. OSD directed that the Supply Management Business Area Unit Cost Report be produced in obligations starting in FY 94. We now have the database to extract this data and are able to cross check monthly to identify inconsistencies. Lastly, we have updated the cost account code mapping to ensure that the most accurate costs are recorded.

We do not agree with the statement that data used to develop the surcharge rates for the Supply Management Division were inconsistent with unit cost data used to manage the division. Surcharge or cost recovery rates are developed during budgetary formulation as a projection of the costs which should be recovered in DLA's prices to its customers. These surcharge rates employ selected source data from the general ledger accounts, produced through DBMS, since not all costs recorded in the general ledger must be recovered through pricing. Utilizing this data, the surcharge rates for a specific fiscal year are developed from 13-15 months prior to the start of that fiscal year and incorporated into DLA's budget submission. Following all adjustments made by OSD, the surcharge rates are finalized in May before the fiscal year begins in October. Unit cost reports utilize the same source data

Defense Logistics Agency Comments

from DBMS, but are employed by managers in execution vice budget formulation. The unit cost report assists managers in determining whether current year execution is proceeding according to plan, but will not and cannot assist in developing cost recovery rates for future years, particularly when cost recovery rates must recover costs which are not incurred in DLA's Supply Business Area. Such examples would include the cost of financing Joint Logistics Systems Center costs, overocean transportation costs for movement of service-managed material, and recovery of prior year losses from Supply Business activities. The unit cost report is an inappropriate tool to consider for use in surcharge development.

~~DISPOSITION:~~

- ~~(X) Action is ongoing. Estimated Completion Date: 30 Nov 94~~
- ~~() Action is considered complete.~~

INTERNAL MANAGEMENT CONTROL WEAKNESSES:

- () Nonconcur.
- (X) Concur; however, weakness is not considered material.
- () Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

MONETARY BENEFITS:

DLA COMMENTS:

ESTIMATED REALIZATION DATE: 31 July 1994

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

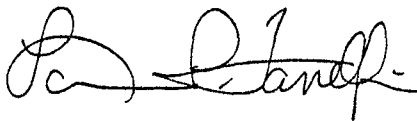
ACTION OFFICER: Patrick Kashmer, DLA-FOBR, 47876, 29 Apr 94

REVIEW/APPROVAL: *J.S.* Rountree, CAPT, SC, USN, Acting Chief Financial Officer

COORDINATION: DLA-FOX, DLA-FOM
Koneta Dixon, FOB, x46228
L. COLLIER, DDAI, 5 24 94 *Bygmt, DDAI, 25 May 94*

DLA APPROVAL:

31 MAY 1994



LAWRENCE P. FARRELL, JR.
Major General, USAF
Principal Deputy Director

TYPE OF REPORT: AUDIT

DATE OF POSITION:

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO: Draft Report on the Management Data Used to Manage
the Defense Logistics Agency Supply Management
Division of the Defense Business Operations Fund
(Project No. 3LD-2004)

RECOMMENDATION 1: We recommend that the Director, Defense Logistics Agency, review and revise the computer logic used to generate the unit cost report to ensure that all costs are captured and accurately reported on the unit cost report.

DLA COMMENTS: Concur. We have reviewed and corrected the problem with the computer logic in the September 1993 report. The DFAS-FSA is responsible for the development and maintenance of the DBMS and the extract process that provides cost data. DBMS is processed by IPC-P in Philadelphia for DPSC and DISC. The September 1993 overstatement occurred in part because IPC-P modified or improperly installed standard programs sent to them by DFAS-FSA. HQ DLA received corrected files for September 1993 data in March 1994, which fully corrected the September 1993 report.

Another reason for the overstatement was that the Defense Personnel Support Center (DPSC) three commodities (C&T, Medical, and Subsistence) were consolidated in the DPSC-Noncommodity report. The supply center unit cost summary report then added all four DPSC pieces (C&T, Medical, Subsistence, and Noncommodity) with the other business area commodities to derive the total cost. This error double counted DPSC's costs. As noted above, this error had no material impact on FY 93 budgetary execution, management has taken corrective action to ensure that the reports accurately reflect actual financial performance and that the reports are reconciled with the trial balance. This problem is now corrected.

Lastly, we continually update the cost account code mapping to ensure that the most accurate costs are being recorded.

DISPOSITION:

- Action is ongoing. Estimated Completion Date:
- Action is considered complete.

INTERNAL MANAGEMENT CONTROL WEAKNESSES:

- Nonconcur.
- Concur; however, weakness is not considered material.
- Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

MONETARY BENEFITS:

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

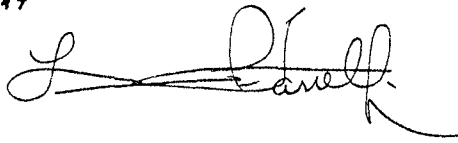
DATE BENEFITS REALIZED:

Defense Logistics Agency Comments

ACTION OFFICER: Patrick Kashmer, DLA-FOBR, 47876
REVIEW/APPROVAL: J.S. Rountree, CAPT, SC, USN, Acting Chief Financial
Officer

COORDINATION: DLA-FOX, DLA-FOM
Koneta Dixon, FLA-FOB, 46228
L. Coulter, DODI 5 24-94
General, DODI, 25 May 94

DLA APPROVAL:



31 MAY 1994

LAWRENCE E. FARRELL, JR.
Major General, USAF
Deputy Director

TYPE OF REPORT: AUDIT

DATE OF POSITION:

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO: Draft Report on the Management Data Used to Manage the Defense Logistics Agency Supply Management Division of the Defense Business Operations Fund (Project No. 3LD-2004)

RECOMMENDATION 2: We recommend that the Director, Defense Logistics Agency, establish controls to ensure that cost data are accurately reported in the unit cost report and that the unit cost report is provided to management in a timely manner. The controls should include periodic evaluations of the computer logic used to generate the unit cost report and reconciliations of the Defense Logistics Agency Headquarters' unit cost report to unit cost data available at the inventory control points and data in the Defense Logistics Agency's financial system used to produce financial statements required by the Chief Financial Officers Act.

DLA COMMENTS: Concur. We have established controls to ensure that the reports are both accurate and timely. On 14 Feb 1994, we directed DLA's Supply Centers to ensure the timely and accurate reporting of unit cost data.

We have reinstated daily status reports to monitor and correct problems in receiving the data extracts from DFAS and the Information Processing Centers. As a result, the data transmission timeliness and accuracy has improved significantly. We will continue to coordinate efforts with DFAS and the IPCs to resolve future problems as they arise. Additional controls will assure consistency between financial reports and the unit cost report. Now that both systems report obligation data, we are developing monthly cross checks to identify inconsistencies.

DISPOSITION:

- Action is ongoing. Estimated Completion Date: 30 Nov 94
- Action is considered complete.

INTERNAL MANAGEMENT CONTROL WEAKNESSES:

- Nonconcur.
- Concur; however, weakness is not considered material.
- Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

MONETARY BENEFITS:

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: Patrick Kashmer, DLA-FOBR, 47876

REVIEW/APPROVAL: J.S. Rountree, CAPT, SC, USN, Acting Chief Financial Officer

COORDINATION: DLA-FOX, DLA-FOM
Koneta Dixon, DLA-FOB, 46228

DLA APPROVAL: MAY 1994

Support, ODAI, 25 May 94
[Signature]

LAWRENCE P. FARRELL, JR.
Major General USAF
Deputy Director

Defense Logistics Agency Comments

TYPE OF REPORT: AUDIT

DATE OF POSITION:

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO: Draft Report on the Management Data Used to Manage the Defense Logistics Agency Supply Management Division of the Defense Business Operations Fund (Project No. 3LD-2004)

RECOMMENDATION 3: We recommend that the Director, Defense Logistics Agency, establish standard operating procedures to describe the development, reconciliation, and maintenance of the unit cost report. The procedures should include the allocation procedures used to distribute common costs among the Defense Logistics Agency business areas and within the Supply Management Division, responsibilities of the various functional entities involved in the unit cost process, to include assignment of overall responsibility for the unit cost report; and distribution of the unit cost report and time frames for distribution.

DLA COMMENTS: Concur. These procedures are in practice today, but are not fully documented in a single source. We are developing standard written operating procedures for the unit cost report process, and we will obtain input and approval from the DoD Comptroller.

DISPOSITION:

- Action is ongoing. Estimated Completion Date: 30 Nov 94
- Action is considered complete.

INTERNAL MANAGEMENT CONTROL WEAKNESSES:

- Nonconcur.
- Concur; however, weakness is not considered material.
- Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

MONETARY BENEFITS:

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

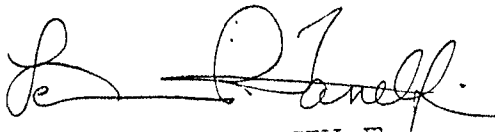
DATE BENEFITS REALIZED:

ACTION OFFICER: Patrick Kashmer, DLA-FOBR, 47876

REVIEW/APPROVAL: J.S. Rountree, CAPT, SC, USN, Acting Chief Financial Officer

COORDINATION: DLA-FOX, DLA-FOM
Koneta Dixon, DLA-FOB, 46228
Accounting DDME 5-24-94

DLA APPROVAL:



LAWRENCE P. FARRELL, JR.
Major General, USAF
Deputy Director

1 MAY 1994

TYPE OF REPORT: AUDIT

DATE OF POSITION:

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO: Draft Report on the Management Data Used to Manage
the Defense Logistics Agency Supply Management
Division of the Defense Business Operations Fund
(Project No. 3LD-2004)

RECOMMENDATION 4: We recommend that the Director, Defense Logistics Agency, establish procedures to coordinate and reconcile the development of cost data used in the surcharge rate charged to customers and the unit cost process.

DLA COMMENTS: Nonconcur. There is no direct linkage between unit cost reports and the development of surcharge or cost recovery rates used in the pricing process. Surcharge or cost recovery rates are developed during budgetary formulation as a projection of the costs which should be recovered in DLA's prices to its customers. These surcharge rates employ selected source data from the general ledger accounts, produced through DBMS, since not all costs recorded in the general ledger must be recovered through pricing. Utilizing this data, the surcharge rates for a specific fiscal year are developed from 13-15 months prior to the start of that fiscal year and incorporated into DLA's budget submission. Following all adjustments made by OSD, the surcharge rates are finalized in May before the fiscal year begins in October. Unit cost reports utilize the same source data from DBMS, but are employed by managers in execution vice budget formulation. The unit cost report assists managers in determining whether current year execution is proceeding according to plan, but will not and cannot assist in developing cost recovery rates for future years, particularly when cost recovery rates must recover costs which are not incurred in DLA's Supply Business Area. Such examples would include the cost of financing Joint Logistics Systems Center costs, overocean transportation costs for movement of service-managed material, and recovery of prior year losses from Supply Business activities. The unit cost report is an inappropriate tool to consider for use in surcharge development.

DISPOSITION:

- Action is ongoing. Estimated Completion Date:
- Action is considered complete.

INTERNAL MANAGEMENT CONTROL WEAKNESSES:

- Nonconcur.
- Concur; however, weakness is not considered material.
- Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

MONETARY BENEFITS:

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

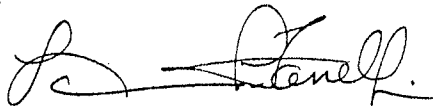
AMOUNT REALIZED:

DATE BENEFITS REALIZED:

Defense Logistics Agency Comments

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J. S. Rountree, DDAT, 25 May 94

DLA APPROVAL:



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