



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

~~13728~~
112304

LOGISTICS AND COMMUNICATIONS
DIVISION

MAY 15, 1980

B-162152

The Honorable Harold Brown
The Secretary of Defense



112304

Dear Mr. Secretary:

Subject: [The Army Can Save Millions Annually By
Properly Considering Serviceable Returns in
Its Requirements Computations] (LCD-80-64)

We have completed our review of the way the Army removes invalid demands, representing customers' unsuccessful attempts to cancel orders, from its demand data base. We found the Army's requirements for future procurement or rework of demand-supported items are inflated by tens of millions of dollars annually because four of the five major wholesale inventory control points have placed substantial limitations on the extent to which serviceable returns can be applied to past demands.

Demands which reflect customers' orders placed on the wholesale supply system are recorded and maintained for 24 months in the Army's data base. The Army uses this data to compute inventory levels and requirements for future procurements or repair programs.

We previously reported to you (LCD-77-201, Feb. 17, 1977) that the Army could realize substantial savings by eliminating demands representing orders which customers have attempted to cancel but were unsuccessful.

Your response to that report stated that the Army does have a system for removing demands representing unsuccessful cancellation attempts. The Army's system removes the demand when the customer returns serviceable materiel.

(943052)

010366

REQUIREMENTS INFLATED BY FAILURE
OF INVENTORY CONTROL POINTS TO
FOLLOW ARMY POLICY

Army policy and the wholesale supply system procedures were designed to reduce demands in the data base by the amount of serviceable materiel customers returned. However, the automated system at each inventory control point can be set to limit or prevent serviceable returns from initiating demand reductions in the system's data base. The U.S. Army Materiel Development and Readiness Command (DARCOM) has given the inventory control points blanket authority to use these limitations without prior notice or approval. The following chart illustrates the degree which the inventory control points will allow serviceable returns to reduce demands.

<u>Materiel Readiness</u> <u>Commands</u>	Maximum percent total demands can be reduced <u>by returns</u>
Troop Support and Aviation	100
Communication and Electronics	20
Missile	20
Armament	5
Tank-Automotive	0

As the chart shows, the Troop Support and Aviation Materiel Readiness Command uses all serviceable returns to reduce demands; the Tank-Automotive Materiel Readiness Command uses none. The following example shows how a 20-percent return limitation would adversely affect the average monthly demand factor used in the requirements formula.

B-162152

<u>Demand reduction computation</u>	<u>20-percent limitation</u>	<u>100-percent demand offset</u>
Total demands (248 items)	248.0	248.0
Demand reduction due to serviceable returns, if no limi- tation (82 items)	-	-82.0
Maximum return offset with 20% limitation (20% x 248)	<u>-49.6</u>	<u>-</u>
Demands used for average monthly demand computation	198.4	166.0
Average monthly demand for requirements computations (\div 24 months)	8.27	6.92

In the example, the 20-percent return limitation caused the net average monthly demand to be overstated by 19.5 percent.

On the basis of an analysis of 115,000 returns of serviceable materiel from the field to DARCOM inventory control points, we estimate that in 1978 the Army wholesale inventory managers received \$106.2 million of serviceable returns for demand-supported items. However, because four of the five inventory control points imposed limitations on the use of serviceable returns to offset demands, serviceable returns worth millions of dollars were not used to reduce the demand base. If this returned materiel had been used to offset past demands, the Army could have avoided inventory procurement and repair costs estimated at tens of millions of dollars.

Views of inventory management
personnel on the validity of
offsetting demands with returns

Officials at the Tank-Automotive Materiel Readiness Command stated that they do not allow serviceable returns to reduce the average monthly demand factor used to forecast requirements because the returns may adversely affect their supply effectiveness. During February 1979, the command's supply effectiveness was 6 to 7 percentage points below

DARCOM's goal of 85 percent. The officials' justification for the return limitation was based on tests of a "few items" when they were converting to a new automated data processing system in October 1977. The command has made no followup studies since it decided to exclude serviceable returns. In our opinion, this is not a sufficient basis for not complying with Army Regulation 710-1, which specifically requires that serviceable returns be considered in the requirements computation process.

Further, as discussed below, the experience of the Troop Support and Aviation Materiel Readiness Command indicates that compliance with the Army policy has no material effect on supply responsiveness.

In a March 8, 1978, report, the Army Audit Agency reported that return limitations resulted in inflated requirements and unnecessary procurement and repair costs. In fact, before the audit, Troop Support and Aviation Materiel Readiness Command officials had recognized that the return limitation was causing an overstatement of requirements and had made a \$13 million downward adjustment to their fiscal year 1977 budget request for funds to purchase stock-funded items and secondary items. After the Army audit report, the command officials removed all limitations and currently apply 100 percent of serviceable materiel returns against the average monthly demand. Before the command removed the return limitation, its supply effectiveness was 85.2 percent. This figure represents the percentage of total requisitions received that can be satisfied from onhand stock. One year after removal of the return limitation, the supply effectiveness rate was almost unchanged at 85.1 percent, which demonstrates that removing the return limitation did not adversely affect supply effectiveness.

CONCLUSION AND RECOMMENDATION

The Army's requirements for procurement or rework of demand-supported items are inflated because four of the five inventory control points are not using 100 percent of serviceable returns to offset demands in their requirements computations, as required by Army regulation.

We recommend that you direct the Army to reduce the projected requirements for materiel by the full amount of forecasted returns of serviceable materiel from customers.

AGENCY COMMENTS

In commenting on our report by letter dated March 28, 1980, you concurred with our recommendation and advised us that the Army has initiated action directing each inventory control point to use 100 percent of serviceable returns as an offset to projected requirements. In addition, assets received as the result of serviceable returns will be applied as an offset against planned procurement actions.

- - - -

As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House Committee on Government Operations and the Senate Committee on Governmental Affairs not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Director, Office of Management and Budget; the Secretary of the Army; and the Chairmen of the appropriate congressional committees.

Sincerely yours,



R. W. Gutmann
Director