

GAO

Fact Sheet for the Chairman, Committee
on Governmental Affairs, U.S. Senate

August 1993

DOD INVENTORY

Reporting Exclusions and Valuation Procedures



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National Security and
International Affairs Division

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August 11, 1993

The Honorable John Glenn
Chairman, Committee on Governmental Affairs
United States Senate

Dear Mr. Chairman:

As you requested, we are providing you with information on (1) categories of items that are excluded from the Department of Defense's (DOD) Supply System Inventory Report and (2) the status of DOD's efforts to establish a uniform system for inventory valuation. This fact sheet provides the results of our work.

DOD annually reports the amounts of its inventories of principal and secondary items¹ in the Supply System Inventory Report. The report is used to monitor changes and trends in the inventory. For reporting, DOD breaks out its inventories into five categories. These categories are defined in the glossary.

Exclusions From Reporting in DOD's Supply System Inventory Report

Historically, DOD has excluded 10 categories of principal and secondary items from reporting in the Supply System Inventory Report. In January 1993, DOD issued DOD 4140.1-R, "DOD Materiel Management Regulation," which modified and combined some of the exclusions. According to a DOD official, the objective of the regulation is to exclude from reporting items that DOD does not (1) consider to be in its supply system and (2) have control over because the items have been issued to users. The 10 categories and the specific reasons for excluding them are discussed below.

Exclusion 1 is for ships, aircraft, intercontinental ballistic missiles, intermediate range ballistic missiles, and space vehicles. DOD considers these items to be complete weapon systems, not principal or secondary inventory items that are reported in the Supply System Inventory Report.

Exclusion 2 is for secondary items aboard combat ships and assigned to troop units, including National Guard and reserve components. DOD does

¹Principal items include end items, such as trucks in storage, and replacement assemblies, such as aircraft circuit cards, of such importance that centralized individual item management is needed throughout the supply system. Secondary items are consumable—items that are not repairable—and repairable items other than principal items. They include spare and repair parts, fuel, construction materials, clothing and textiles, and medical and dental supplies.

not report these items because it considers them to be in use and no longer available for issue through the supply system.

Exclusion 3 is for items held for use by DOD's industrial activities such as shipyards. DOD does not report these items because they are not available for issue to customers of the supply system. These items include raw materials and bench stocks that are used in the industrial processes and repair programs.

Exclusions 4 through 6 are for items (1) acquired for civil function purposes, (2) issued to the Defense Nuclear Agency, and (3) issued to the National Security Agency and classified programs. According to DOD, these are consumable items similar to those managed by the Defense Logistics Agency (DLA). DOD excludes these items because when they are issued to the using agency, they are out of the supply system and no longer available for use.

Exclusion 7 is for surplus and foreign excess equipment. According to DOD, the surplus items are principal and secondary items that are undergoing the DOD screening process for disposal. The items are physically located in a disposal facility and are no longer available to be issued to supply system customers. Foreign excess equipment refers to items that have been sold as part of the foreign military sales program, but are still in DOD's possession.

Exclusion 8 is for industrial plant equipment. According to DOD officials, industrial plant equipment represents principal items such as plant machinery that are reported to the Defense Industrial Plant Equipment Center and are not part of the supply system.

Exclusions 9 and 10 are for (1) materiel stored in DOD component facilities that are owned by another DOD component or another federal agency and (2) items installed or incorporated in an assembly that is reported. According to DOD officials, these exclusions prevent counting the same inventory more than once and exclude items that are not owned by DOD.

Status of Inventory Valuation Initiatives

For the September 1990 Supply System Inventory Report, DOD components used different methods for determining inventory values. For example, the Army and the Air Force used the latest acquisition cost as a basis for valuing their inventories. The Navy compared the estimated original acquisition costs to the latest acquisition cost and used the lower of the

two amounts. DLA valued its inventory using "standard prices," which were based on acquisition cost plus costs for transportation and inventory losses.

To establish a uniform system for valuing inventory, DOD directed the military services and DLA to follow DOD Comptroller guidance for reporting in the September 1991 Supply System Inventory Report. The components were to (1) value all inventory at the latest acquisition cost, (2) reduce the value of items needing repair by estimated repair costs, and (3) reduce the value of potential reutilization/disposal stock to its salvage value (2.2 percent of an item's latest acquisition cost). DOD subsequently formalized this inventory valuation policy in its materiel management regulation (DOD 4140.1-R).

The Army, Navy, and Air Force and DLA followed the DOD criteria in valuing their secondary inventory for the September 1991 report. The Army, the Navy, and DLA used September 30, 1991, financial inventory data for the report. The Air Force developed its inventory figures from March 1991 inventory management reports. Consequently, the Air Force data represented inventory levels as of March 1991 while the other components reported September data. For the September 1992 report, the Air Force used September data.

Scope and Methodology

We held discussions with and obtained pertinent documents from officials at the Office of the Secretary of Defense, and DLA and the Army, Navy, and Air Force. We also reviewed the procedures that the military services and DLA used for valuing their secondary inventory.

We did not obtain written agency comments, but we did discuss the information in this fact sheet with officials from the Office of the Secretary of Defense, the military services, and DLA, and have incorporated their comments as appropriate.

Unless you publicly announce the contents of this fact sheet earlier, we plan no further distribution until 30 days from its issue date. At that time, we will send copies to the Chairmen, House and Senate Committees on Appropriations and on Armed Services; the Secretaries of Defense, the Army, the Navy, and the Air Force; and the Directors, Defense Logistics Agency and Office of Management and Budget. We will also make copies available to others on request.

Please contact me on (202) 512-8412 if your or your staff have any questions regarding this fact sheet. Major contributors to this fact sheet are John Klotz, Assistant Director; Louis Modliszewski, Evaluator-in-Charge; and Colin Chambers, Evaluator.

Sincerely yours,



Donna M. Heivilin, Director
Defense Management and NASA Issues

Glossary

Approved Acquisition Objective	The approved acquisition objective is the quantity of an item authorized for peacetime and wartime requirements to equip and sustain U.S. and allied forces in accordance with DOD policies and plans.
In-transit Stock	In-transit stock are materials that are between storage locations, being shipped from vendors, in-use or on loan with contractors or schools, or materiel that cannot otherwise be categorized.
Economic Retention Stock	Economic retention stock represents items in excess of the approved acquisition objective that have been determined to be more economical to retain for future use rather than dispose of the items and procure or repair other items to satisfy future needs.
Contingency Retention Stock	Contingency retention stock represents items in excess of the approved acquisition objective and the economic retention stock for which there is no predictable demand or quantifiable requirements and that is being retained for specific contingencies.
Potential Reutilization/Disposal Materiel	Potential reutilization/disposal materiel stocks represent items that (1) have been identified for possible disposal, but have the potential for reutilization or (2) have been sent to the Defense Reutilization and Marketing Service for possible reutilization or disposal.

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