

GAO

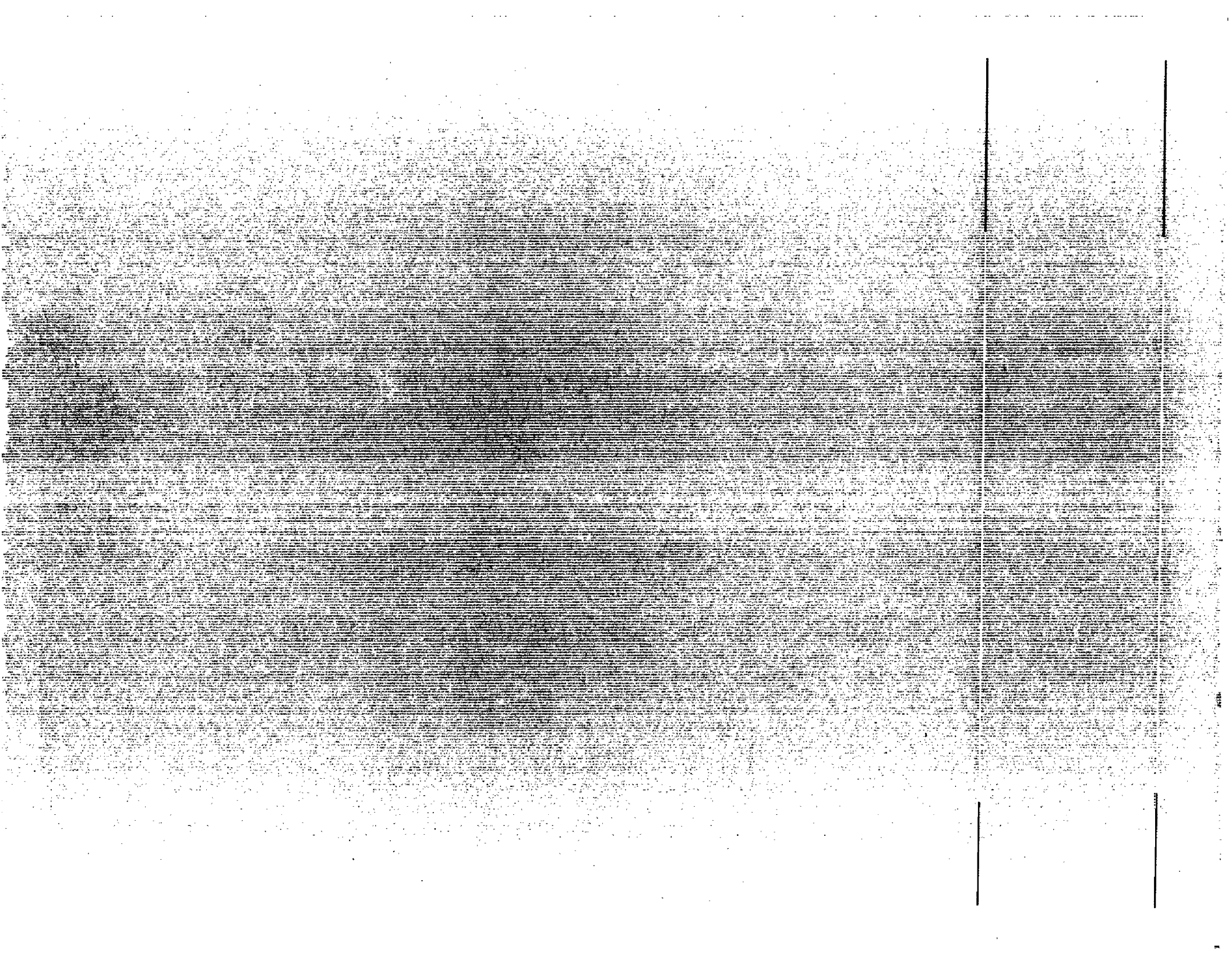
Report to the Chairman, Subcommittee
on Readiness, Committee on Armed
Services, House of Representatives

December 1991

DOD COMMERCIAL TRANSPORTATION

Savings Possible Through Better Audit and Negotiation of Rates







United States
General Accounting Office
Washington, D.C. 20548

145524

**National Security and
International Affairs Division**

B-245288

December 27, 1991

The Honorable Earl Hutto
Chairman, Subcommittee on Readiness
Committee on Armed Services
House of Representatives

Dear Mr. Chairman:

As you requested, we evaluated the effectiveness of the Department of Defense's efforts to control commercial transportation costs. This report contains several recommendations to the Secretary of Defense for improving prepayment audits and making rate negotiations for international ocean cargo and domestic household goods transportation more effective.

We are sending copies of this report to the Secretaries of Defense, the Army, and the Navy; the Commanders of the Transportation Command, the Military Traffic Management Command, and the Military Sealift Command; the Administrator of the General Services Administration; and the Director of the Office of Management and Budget.

Please contact me at (202) 275-4141 if you or your staff have any questions concerning the report. Major contributors to this report are listed in appendix II.

Sincerely yours,

Richard Davis
Director, Army Issues

Executive Summary

Purpose

The Department of Defense (DOD) spends approximately \$3 billion a year for commercial transportation services to move cargo, personnel, and their personal effects worldwide. DOD sometimes overpays its transportation bills or does not effectively negotiate for reduced rates.

The Chairman of the Subcommittee on Readiness, House Committee on Armed Services, asked GAO to assess the effectiveness of DOD's efforts to control commercial transportation costs. He asked specifically that GAO (1) determine whether DOD is preventing excess payments to commercial carriers through preauditing—that is, auditing bills prior to payment—and (2) identify any other areas where DOD could improve its traffic and travel management programs.

Background

Each DOD service and agency budgets for and controls its own commercial transportation expenses and is responsible for determining its shipping requirements. Other transportation managers assist the services and agencies in carrying out their traffic and travel management programs. Under the overall policy direction and guidance of the Assistant Secretary of Defense (Production and Logistics), the Military Traffic Management Command advises the services and agencies how to select domestic freight carriers and route shipments or make travel arrangements. It also negotiates rates for freight transportation in the United States and for household goods transportation worldwide. The Military Sealift Command negotiates rates for ocean freight transportation and provides information to the Military Traffic Management Command for selecting ocean carriers and routing ocean shipments.

Since late 1988, DOD has had the authority to preaudit commercial transportation bills and to retain whatever overcharge amounts it identifies. Prior to that time, DOD paid most of its bills for commercial transportation services prior to audits performed by the General Services Administration (GSA). GSA still performs postaudits for DOD.

Results in Brief

Preauditing since 1988 has prevented nearly \$10 million in domestic freight expenditures that DOD would have otherwise made. It has also helped indirectly, in DOD's opinion, to deter another \$34 million in overcharges by prodding carriers to adopt more careful billing practices. However, GSA's postaudit data shows that some overcharges were not identified during DOD's preaudits. DOD has not compared GSA's audit results with its own results to determine why this may have occurred. Moreover, DOD has not provided feedback to transportation officials at

local installations to make them aware of overcharging so that they can take corrective actions to prevent future overcharges.

DOD may be missing opportunities to control costs more effectively in two other transportation areas. First, the Military Sealift Command, in negotiating container shipping rates with commercial ocean carriers, does not (1) provide prospective offerors useful information about its requirements in terms of the specific commodities to be shipped and shipping origins and destination points or (2) solicit and evaluate rate offers for the same pattern of service for which DOD actually procures the service. Second, the Military Traffic Management Command has not yet implemented or proposed to the household goods moving industry any changes to its process for soliciting domestic rates, as GAO had recommended in a February 1990 report, to ensure competitive bidding for DOD business. The existing bidding process does not provide carriers adequate incentives to encourage them to offer DOD their lowest rates.

Principal Findings

Strengthened Preauditing Would Help Lower Domestic Freight Costs

While DOD's system of preauditing has helped prevent millions of dollars of overcharges on domestic freight costs, DOD has not tested the audits to determine whether they are detecting all overcharges. The data to perform such tests could be obtained from GSA. For example, in GAO's review of 135 DOD-preaudited bills of lading issued in fiscal year 1989 in conjunction with training exercises at Ft. Irwin, California, GAO found subsequent GSA-identified overcharges on about 16 percent of the bills, involving more than \$75,000.

DOD has not routinely provided transportation personnel initiating the shipments with preaudit results. Consequently, these officials have been unable to meet with local carrier representatives to correct repeated overcharging at the earliest opportunity.

Improved Rate Negotiation Strategy Would Enhance Competition for Containerized Ocean Cargo Shipping Service

The Military Sealift Command, in attempting to negotiate favorable rates with the containerized ocean carriers, does not provide prospective offerors specific information about the commodities, number of containers, and the shipping origin and destination points. Without such information, carriers are handicapped in formulating informed offers. Further, the Command's ability to evaluate the reasonableness of rates

offered is weakened because it cannot precisely compare the offers with the carriers' commercial rates.

In addition, the Command complicates rate negotiations by soliciting and evaluating rates by segments—that is, from inland origin to port, port to port, and port to inland destination—and not for the through shipment. Since transportation services are procured on a through basis, segmented rate solicitation and evaluation distorts the significance of the rate offers and complicates the evaluation process.

Negotiating Process for Moving Domestic Household Goods Continues to Lack Incentives for Offering Low Rates

The Military Traffic Management Command's process for soliciting rates for moving the domestic household goods of DOD personnel does not provide carriers an incentive to offer their best rates up front. Its two-step bidding process allows carriers to match the bids of the initial low-bid carriers and to share equally in all the DOD shipments. GAO identified this problem in a previous report and recommended that the Command replace or modify its bidding process to reward the initial low bidders. Although DOD concurred with the recommendation and offered a plan to revise the process, it has not met its milestones for implementing the plan or offered the carriers any proposals for change.

Recommendations

GAO recommends that the Secretary of Defense

- direct the Military Traffic Management Command and other units performing preaudits to (1) test the effectiveness of their preaudits by comparing the results with bills audited after payment and (2) develop a system for ensuring the timely notification of local installation transportation officials when the auditing activities detect overcharges;
- direct the Military Sealift Command to (1) develop and provide to all prospective offerors detailed information on what it has shipped in terms of specific commodities and number of containers in specific traffic patterns, and its best estimate of what it will be shipping in the future, and (2) change its solicitations to request rates for the same pattern of service for which DOD actually procures the service; and
- direct the Military Traffic Management Command to accelerate implementation of GAO's previous recommendation to replace or modify the current domestic household goods bidding process so that all carriers have an incentive to initially bid the lowest possible rates and the lowest bidder is appropriately rewarded.

Agency Comments and GAO Evaluation

DOD concurred with the report recommendations concerning preauditing and said that it will formally request GSA postaudit results and compare them with DOD's preaudit results. It also said that it will implement a system for ensuring timely notice to local transportation officials when the preauditors detect overcharges.

DOD generally agreed with GAO's recommendations concerning ocean rate negotiation but believed that detailed shipping information was already available to those bidders who desire it. GAO believes that the Military Sealift Command should provide such information to the carriers with the request for proposals without the carriers having to ask for it.

DOD believed that changing the solicitation process to obtain through-shipment rates would complicate, rather than simplify, the process. Nevertheless, DOD stated that the Military Sealift Command, in conjunction with the Military Traffic Management Command, would investigate the feasibility of soliciting, in its next request for proposals, single factor rates for the highest-volume point-to-point routes. GAO believes that this is a step in the right direction.

DOD supported the timely modification of the domestic household goods rate bidding process but said that implementation of the action plan had been delayed, in part, as a result of Operation Desert Storm. DOD said that a revised action plan should be implemented in late 1992.

Contents

Executive Summary		2
<hr/>		
Chapter 1		8
Introduction	Transportation Budgeting and Cost Responsibilities	8
	DOD Began Preauditing in 1988	9
	Objectives, Scope, and Methodology	9
<hr/>		
Chapter 2		12
Preaudits Are Useful but Can Be Further Strengthened to Help Reduce Domestic Freight Costs	Activities Directed to Establish Preaudit Capability	12
	Domestic Freight Bills Are Being Preaudited	12
	Preauditing Is Helping DOD Avoid the Loss of Transportation Dollars	13
	DOD Has Not Used GSA Postaudit Results to Test the Adequacy of Its Preaudits	15
	Local Installation Transportation Officials Not Apprised of Preaudit Findings	15
	Conclusions	16
	Recommendations	17
	Agency Comments	17
<hr/>		
Chapter 3		18
Ocean Rate Negotiation Should Be Strengthened	Rate Negotiation and Procurement	18
	Problem of Ensuring That Rates Are Fair and Reasonable	19
	MSC Does Not Provide Carriers Necessary Information for Making Informed Offers	20
	Rates Are Not Requested on the Same Basis as DOD Procures the Service	24
	Conclusions	25
	Recommendations	25
	Agency Comments and Our Evaluation	25
<hr/>		
Chapter 4		27
Progress Slow in Implementing Changes to Household Goods Rate Negotiation Process	Rate Process Involves "Me-Too" Negotiation	27
	Prior GAO Report Identified Weaknesses in Rate Negotiation Process	28
	Progress in Making Any Change Has Been Slow	29
	Recommendation	29
	Agency Comments and Our Evaluation	30

Appendixes

Appendix I: Comments From the Department of Defense	32
Appendix II: Major Contributors to This Report	61

Tables

Table 2.1: Preaudit Status of GBLs Covering Rail Shipments to and From the National Training Center	13
Table 2.2: Results of Preaudits	14
Table 2.3: Preaudit Accomplishments for GBLs Covering Rail Shipments to and From the National Training Center	15
Table 3.1: Most Frequently Used Commodity Codes for Containers Shipped From the East and Gulf Coasts During January 1991	23

Abbreviations

DOD	Department of Defense
GAO	General Accounting Office
GBL	government bill of lading
GSA	General Services Administration
MSC	Military Sealift Command
MTMC	Military Traffic Management Command

Introduction

The Department of Defense (DOD) relies heavily on commercial transportation services to meet its national defense mission. Each year, DOD pays approximately \$3 billion for commercial transportation services to move its cargo, passengers, and their personal effects worldwide. It is DOD policy to procure safe, secure, reliable, and quality commercial transportation services that will meet DOD requirements at the lowest overall cost. It is also DOD policy to review applicable carrier rates and charges on DOD movements to ensure that they are fairly, reasonably, and properly applied, and to take action to obtain relief from rates or charges found to be unfairly, unreasonably, or improperly applied.

Transportation Budgeting and Cost Responsibilities

Each branch of service and DOD agency is responsible for budgeting for and controlling its transportation expenses. Each determines its shipping requirements—what, when, and where to ship—and how much funding is needed to meet these requirements.

Transportation officials at military bases, posts, and other activities and DOD offices procure the services individually or have other DOD components procure the services for them. The Military Traffic Management Command (MTMC)—an Army component of the U.S. Transportation Command—is responsible for negotiating domestic freight and international and domestic household goods rates and maintaining carrier tariffs and rate tender files. MTMC is also responsible for routing carload and truckload shipments and other shipments requiring premium or specialized services and for providing local transportation personnel with general routing guidance for all other shipments. It also selects the routing for ocean shipments and books shipments to specific ship voyages. The Military Sealift Command (MSC)—a Navy component of the Transportation Command—is responsible for negotiating ocean cargo rates and serves as DOD's procuring and contracting office. All transportation activities and personnel are subject to overall policy direction and guidance by the Assistant Secretary of Defense (Production and Logistics).

Procurement documentation for commercial transportation services, except ocean cargo services procured under MSC contracts and agreements, is governed by rules issued by the General Services Administration (GSA). GSA requires the use of the government bill of lading (GBL) to procure domestic commercial freight and all commercial household goods transportation. GBLs are issued at military installations and Defense offices throughout the United States but are paid centrally. Army, Air Force, and Defense agency GBLs are paid at the Defense

Finance and Accounting Service, Indianapolis, Indiana; Navy GBLs at the Naval Station, Norfolk, Virginia; and Marine Corps GBLs at the Marine Corps Logistics Base, Albany, Georgia. MSC procures most ocean service under shipping and container agreements and contracts. Ocean service is ordered and paid on the basis of shipping or clearance orders, cargo manifests, and equivalent documents. Charges are paid at MSC offices at Bayonne, New Jersey; Oakland, California; and overseas locations.

DOD Began Preauditing in 1988

It has not been unusual for government shippers to overpay for transportation services, and DOD is no exception. Sometimes it has overpaid single GBLs by thousands of dollars. For example, in a 1988 report, Army Transportation: Alleged Overcharges on Rail Shipments to and From Ft. Irwin, California (GAO/NSIAD-88-174, May 13, 1988), GAO found that DOD was repeatedly overpaying railroad carriers to ship training equipment to and from Ft. Irwin, California, and recommended that the Army begin to audit these bills of lading prior to payment.

Until 1986, federal statutes prohibited the federal government from auditing transportation charges on GBLs prior to payment. Charges were paid and subsequent auditing was performed by GSA. Any DOD overcharges recouped by GSA were returned to DOD, but because the audits were performed a year or more after payment, DOD's authority to reuse the money had often expired. Moreover, information about the overcharges was not timely for use in helping prevent future overcharges.

Public Law 99-627 (Nov. 7, 1986) changed the rules for auditing GBL transportation payments. No longer was GSA required to return the money it had collected to DOD, but it could use the money to pay the audit expenses and return what was left to the U.S. Treasury. For the first time, however, GSA could audit bills prior to payment and delegate preaudit authority to other departments and agencies.

DOD requested preaudit authority soon after the law was passed but did not receive the authority until July 26, 1988. Its first preaudits began in late 1988.

Objectives, Scope, and Methodology

The Chairman of the Subcommittee on Readiness, House Committee on Armed Services, asked us to follow up on our May 1988 report concerning rail shipments to and from Ft. Irwin, California, and assess

whether DOD is preventing excess transportation payments to commercial carriers through preauditing. He also asked that we identify any other areas where DOD could improve its traffic and travel management programs. Our review focused on three areas of transportation—domestic freight, international ocean cargo, and domestic household goods—because these were areas where we had identified problems in the past.

We met with officials of the Assistant Secretary of Defense (Production and Logistics) to discuss DOD policies for auditing transportation vouchers, paying transportation bills, and other matters related to transportation cost controls. We also interviewed officials of the GSA Office of Transportation Audits, Washington, D.C., the unit responsible for conducting transportation rate audits and for reviewing requests for preaudit delegation authority, and reviewed the laws and regulations concerning preaudit authority. We also reviewed various Defense, Logistics Management Institute, Army Audit Agency, and Air Force Audit Agency reports related to transportation procurement and payment audits.

We visited the three central military transportation payment centers to observe the payment and preaudit activities in place. We also met with officials at MTMC-Eastern Area, Military Ocean Terminal, Bayonne, New Jersey, and observed the audits being conducted there.

To follow up on our May 1988 report, we met with MTMC officials responsible for establishing a preaudit unit in MTMC and for routing shipments. We also met with transportation personnel responsible for monitoring and preparing documentation for the shipments discussed in the May 1988 report at the U.S. Forces Command, Ft. McPherson, Georgia, and the National Training Center, Ft. Irwin, California. We subsequently met with transportation officials at Ft. Carson, Colorado, and Ft. Stewart, Georgia, to observe the procedures they followed to prepare GBLs and procure rail transportation services.

To verify that GBLs were being preaudited at MTMC, we reviewed GBLs covering shipments moving by railroad into and out of the National Training Center. Transportation officials at Ft. Irwin provided us a listing of all fiscal years 1989 and 1990 railroad GBLs issued in conjunction with training exercises at the National Training Center, and we examined whether they had been preaudited and what action, if any, GSA had taken on them in its postaudits.

To identify potential improvements for procuring ocean cargo services, we met with MSC officials at the Command's headquarters in Washington, D.C., and at the Atlantic area office, Military Ocean Terminal, Bayonne, New Jersey, to discuss matters related to the negotiation of rates, payments, and voucher audits. In addition, we reviewed carrier protests submitted to the Comptroller General concerning the procedures used by MSC to evaluate ocean cargo rates.

Finally, to identify potential improvements for procuring household goods services, we met with MTMC officials responsible for negotiating household goods rates and observed the preaudits being performed at the central payment offices.

We performed our review from June 1990 to August 1991 in accordance with generally accepted government auditing standards. DOD provided written comments on a draft of this report. DOD's comments and our evaluation are discussed in chapters 2, 3, and 4, and a complete copy of the comments is included as appendix I.

Preaudits Are Useful but Can Be Further Strengthened to Help Reduce Domestic Freight Costs

DOD has implemented a system of preauditing that has helped it prevent millions of dollars in overcharges, but some aspects of the auditing could be strengthened. DOD has not taken necessary steps to obtain reasonable assurances that its preaudits are thorough. GSA postaudit data shows that some overcharges were not uncovered during preauditing. Even when overcharging has been detected, DOD has not provided feedback to transportation officials at local installations who prepare the shipment documentation to make them aware that overcharging has occurred so that they can take corrective actions to prevent overcharges in the future.

Activities Directed to Establish Preaudit Capability

On July 26, 1988, DOD received authority to conduct its own preaudits. Two months later, the Assistant Secretary of Defense (Production and Logistics) advised the assistant secretaries of each branch of service and the directors of the Defense agencies that DOD could save millions of dollars a year by auditing its transportation vouchers prior to payment. He said that with a significant opportunity to reduce budget shortfalls, it was critical that DOD immediately implement a preaudit capability. Accordingly, he directed the three military payment offices and MTMC to immediately establish the capability to preaudit domestic freight GBLs. MTMC was to assist the payment offices by developing the data bases required to support the audits. MTMC was also to develop procedures to manually audit GBLs offering a high potential return.

Each of the central payment offices established the capability to perform preaudits, some using in-house staff and others using contractors or a combination of in-house staff and contractors. MTMC also established a preaudit unit at Bayonne, New Jersey, in January 1989 to assist the payment offices with a portion of their work load.

MTMC's auditors explained to us that preauditing was intended to (1) detect overcharges early, thereby avoiding the lengthy delay inherent in the GSA postaudit process; (2) prevent DOD from losing transportation funds through overcharges, as had been occurring in the past when GSA audited the vouchers only after payment; and (3) provide the shippers, MTMC, and the carriers timely feedback about the overcharges so that the overcharging could be reviewed and remedial action taken.

Domestic Freight Bills Are Being Preaudited

Our review of the GBLs issued by transportation offices showed that most domestic freight GBLs are being properly sent by the military payment offices to MTMC for preaudit. By agreement with MTMC, the central

Chapter 2
Preaudits Are Useful but Can Be Further
Strengthened to Help Reduce Domestic
Freight Costs

payment offices flag certain GBLs and make copies available to MTMC for preaudit. At first, only GBLs with charges of \$10,000 or more and those from certain depots were sent to MTMC. The dollar threshold was lowered to \$8,000 in April 1989 and then to \$5,000 in June 1989.

MTMC, which at the time of our review had six full-time preauditors, audited the GBLs within 2 weeks of receiving them and reported back to the payment offices on the amounts that should be paid. The payment offices then advised the billing carriers of any reductions to their bills. Carriers could appeal any reductions through the payment offices to MTMC and, if necessary, to GSA. MTMC reported that in fiscal year 1990 it preaudited more than 8,000 GBLs.

Our review of rail shipment GBLs issued in connection with training exercises at the National Training Center during fiscal years 1989 and 1990 showed that most GBLs were preaudited as called for in the agreements. Of the 209 GBLs that met the dollar threshold and were issued after MTMC began conducting preaudits, 204, or 97.6 percent, had been sent to MTMC. Program officials could not explain why the other five had not been sent to MTMC for preaudit; however, we do not consider that number to be significant. Table 2.1 provides a summary of the GBLs.

Table 2.1: Preaudit Status of GBLs
Covering Rail Shipments to and From the
National Training Center (Fiscal Years
1989 and 1990)

	Fiscal year		Total
	1989	1990	
GBLs meeting the preaudit dollar threshold	165	73	238
GBLs issued before MTMC began preaudits or unpaid at the time of our review	28	1	29
GBLs that should have been preaudited	137	72	209
GBLs that were preaudited	135	69	204
Percentage preaudited	98.5	95.8	97.6

Preauditing Is Helping
DOD Avoid the Loss of
Transportation Dollars

Since DOD began preauditing in 1988, it has identified nearly \$10 million in overcharges, according to data provided by the Office of the Assistant Secretary of Defense (Production and Logistics). The \$10 million represents freight, household goods, and other carrier charges DOD had been billed but did not pay based on the auditors' findings.

DOD estimated that another \$34 million in overcharges was avoided because the existence of the preaudits deterred overcharging. GSA data showed that fewer overcharges were being identified during postaudit after DOD began preauditing its bills. DOD's calculation of the \$34 million,

**Chapter 2
Preaudits Are Useful but Can Be Further
Strengthened to Help Reduce Domestic
Freight Costs**

however, cannot be verified, inasmuch as it is only an estimate of how the carriers changed their bills considering that they would be preaudited. A DOD summary of overpayments prevented or considered to have been deterred is shown in table 2.2.

Table 2.2: Results of Preaudits

Dollars in millions

Military payment center	Fiscal year			Total ^a
	1988	1989	1990	
Army				
Overpayments prevented	\$1.1	\$2.4	\$5.4	\$8.9
Overcharges deterred	4.5	11.4	16.8	32.8
Total^a	5.6	13.8	22.2	41.6
Navy				
Overpayments prevented	0	0.3	0.6	1.0
Overcharges deterred	0	1.0	0.8	1.8
Total^a	0	1.4	1.4	2.8
Marine Corps				
Overpayments prevented	^b	^b	^b	^b
Overcharges deterred	^b	0.1	^b	0.2
Total^a	0.1	0.1	0.1	0.3
All services				
Overpayments prevented ^a	1.1	2.8	6.1	9.9
Overcharges deterred ^a	4.6	12.6	17.6	34.8
Total^a	\$5.6	\$15.4	\$23.7	\$44.7

^aTotal dollar amounts may not add due to rounding.

^bFigure is less than \$50,000

Note: The amounts attributed to each payment center include figures provided by both MTMC and each center.

Source: DOD.

A specific example that DOD is avoiding unnecessary payments through preauditing involves the GBLs paid for shipments moving by railroad into and out of the National Training Center at Ft. Irwin, California. MTMC's preaudits enabled the payment offices to avoid paying more than \$500,000 on fiscal year 1989 and 1990 GBLs. Table 2.3 summarizes the results of preauditing on these GBLs.

**Chapter 2
Preaudits Are Useful but Can Be Further
Strengthened to Help Reduce Domestic
Freight Costs**

**Table 2.3: Preaudit Accomplishments for
GBLs Covering Rail Shipments to and
From the National Training Center (Fiscal
Years 1989 and 1990)**

	Fiscal year		Total
	1989	1990	
Amount presented for payment	\$24,132,230	\$18,714,656	\$42,846,886
Amount approved for payment following preaudit	23,660,671	18,610,349	42,271,020
Overcharge prevented	471,559	104,307	575,866
Percentage of GBLs with overcharges	16.3	26.1	19.6
Average overcharge	\$21,434	\$5,795	\$14,397

**DOD Has Not Used
GSA Postaudit Results
to Test the Adequacy
of Its Preaudits**

The effectiveness of preaudits could be determined by comparing the results of bills audited before payment with those audited after payment; however, DOD is not making these comparisons. At the same time, GSA continues to identify overcharges after DOD's preaudits.

To compare the results of DOD's preaudits with those of GSA's postaudits, we asked GSA to provide us with the audit status of all the MTMC-preaudited railroad GBLs issued in conjunction with training exercises at the National Training Center during fiscal years 1989 and 1990. GSA found overcharges on about 16 percent of the fiscal year 1989 GBLs that had been preaudited. The overcharges totaled more than \$75,000. Because GSA performs postaudits nearly a year after payment, not all 1990 preaudited GBLs had been postaudited at the time of our review.

MTMC's auditors were unaware that GSA had identified further overcharges on the preaudited GBLs. MTMC officials advised us that some time ago they had asked for GSA results but that GSA was not able to provide the information. Our discussion with GSA officials indicates that the data is now available, and it could be used to provide some type of measure of the effectiveness of the preaudits. We also found no record to show that payment office personnel were aware that GSA had identified an overcharge on a GBL they or their contractors had preaudited. Again, GSA had such information and could have provided it to the offices for their use in comparing audit results.

**Local Installation
Transportation
Officials Not Apprised
of Preaudit Findings**

One of the primary benefits of preauditing is that it surfaces billing problems early and can provide for timely analysis of billing problems. DOD, however, has not taken advantage of this opportunity for analysis. Transportation personnel initiating the shipments have not been informed of the overcharging. Consequently, repeated overcharging is not corrected.

As shown in table 2.3, nearly one of every five GBLs issued in connection with rail shipments to and from the National Training Center at Ft. Irwin, California, was found to have an overcharge. However, none of the local transportation officials we spoke with who issue GBLs at Ft. Irwin, California; Ft. Carson, Colorado; or Ft. Stewart, Georgia, for example, was notified about the overcharging. Most of their GBLs involved more than \$100,000, some more than \$1 million, and had overcharges amounting to thousands of dollars.

In our May 1988 report, we concluded at that time that DOD was being overcharged in connection with moves to and from the Ft. Irwin primarily because the railroads were not billing properly for the cars ordered or because the transportation officers had not prepared the GBLs correctly. Subsequently, in July 1989, Forces Command internal auditors found that overcharging related to cars was still occurring. The internal auditors found that in the six exercises they reviewed, the Army had been overcharged nearly \$500,000 and MTMC preaudits had not detected them. They concluded that the overcharges had occurred because the GBLs had been prepared incorrectly, the instructions for preparing GBLs had been inadequate, or the carriers had billed improperly.

During our current review, we found that the instructions for preparing GBLs are clearer and that the GBLs are being prepared more accurately; nevertheless, overcharges are still occurring. In no case, however, did we find that a local transportation officer had been alerted about the overcharges to learn what may have caused them or whether actions could be taken to prevent them from happening in the future. In fact, many of the officials were surprised that they had been overcharged because it was their understanding that under the terms of the rail agreements, carriers were required to notify them if there was a disagreement with the estimated charges the local officials had annotated on the GBLs. According to these officials, no carrier had inquired about disparate charges. Had they been informed, the officials said, they could have possibly avoided an overcharge. The local officials also believed that had they known about the overcharges, they could have used the information to confront the local carrier representatives about overcharging and helped deter future overcharging.

Conclusions

DOD has not taken necessary steps to obtain reasonable assurances that its preaudits are thorough. GSA postaudit data shows that some overcharges were not uncovered during preaudit, but DOD has not

Chapter 2
Preaudits Are Useful but Can Be Further
Strengthened to Help Reduce Domestic
Freight Costs

obtained the GSA results to evaluate its preaudits. Use of GSA postaudit results would help ensure that the preaudits are thorough.

Even when overcharging has been detected during preaudit, DOD has not provided feedback to local installation transportation officials who prepare the shipment documentation to make them aware that overcharging has occurred. Consequently, overcharging was continuing. Were the local officials advised that overcharges had been detected during preaudit, they could have taken steps to see that the overcharging was not repeated.

Recommendations

We recommend that the Secretary of Defense direct the Military Traffic Management Command and other units performing preaudits to (1) test the effectiveness of their preaudits by comparing the results with bills audited after payment and (2) develop a system for ensuring the timely notification of local installation transportation officials when preaudits detect overcharges.

Agency Comments

DOD concurred with our findings and recommendations and is initiating action to implement the recommendations. According to DOD, in the second quarter of fiscal year 1992, GSA will be formally asked to provide the results of its postaudits. The GSA results will be compared with the DOD preaudits to assess the effectiveness of the preaudits.

DOD also indicated that in fiscal year 1992, MTMC and other units performing preaudits would implement a system for ensuring the timely notification of local installation transportation officials when the auditing activities detect overcharges.

Ocean Rate Negotiation Should Be Strengthened

MSC needlessly complicates its negotiations with the commercial ocean carrier industry at a time when reduced competition among carriers is impeding MSC's ability to obtain favorable rates. As the size of the U.S. shipping fleet declines, fewer carriers compete for DOD shipments. Thus, each year MSC faces a more difficult task relying on competition to produce fair and reasonable rates or rates appropriate for a shipper of DOD's size. In this context, the manner in which MSC negotiates rates does little to put it in a favorable negotiating position. Because MSC has not developed and does not provide carriers adequate proposal information—such as specific commodities, number of containers, and traffic patterns—carriers are handicapped in making offers and MSC's ability to effectively evaluate these offers is weakened because they cannot be compared with commercial rates.

Further, MSC solicits and evaluates rates for segments of a shipment—that is, from inland origin to port, port to port, and port to inland destination. Since the required service will eventually be procured as a through shipment from inland origin to the ultimate destination, such segmented evaluation distorts the significance of the rate offers and complicates the process for evaluating offers.

Rate Negotiation and Procurement

Each year DOD spends about \$600 million for commercial ocean transportation. MSC negotiates rates for millions of tons of DOD cargo, the bulk of which moves in intermodal containers. These are basically 20- and 40-foot-long boxes in which the cargo can be hauled by truck, railroad, or ship without further rehandling of the contents.

MSC's negotiations occur at 6-month intervals under terms of the government's Federal Acquisition Regulation. Offers are based on (1) ocean route—further delineated as to the direction in which cargo will be moving, broad type of cargo (general, refrigerated, or vehicular), and size of container (basically, 20-foot or 40-foot) in which the cargo will move—and (2) land route or drayage area—that is, the route from origin to the port or from the port to the ultimate destination in which the container will move in conjunction with its ocean voyage.

MSC bases its evaluation on criteria stated in requests for proposals. Criteria generally include comparisons of old and new rates, of one offeror's rates with those of another offeror, and of the offerors' rates with commercial rates. MSC advises the offerors that it has the right to reject a rate outright, to negotiate with them for better rates, or to

accept a rate without any negotiation. Accepted rates are provided to MTMC, which uses them to route shipments.

Problem of Ensuring That Rates Are Fair and Reasonable

MSC is faced with competing objectives: (1) obtaining the lowest rates possible for DOD and (2) maintaining an adequate sealift base for mobilization. On most of the routes for which it sought rates, MSC historically found adequate competition to produce low rates and still have adequate lift capability. Accordingly, it did not have to engage in extensive face-to-face negotiations with carriers to obtain low rates. Carriers, however, complained to DOD and Congress that the system resulted in destructive competition, driving rates excessively low and forcing carriers out of business. They argued that the heavy dependency of the U.S. merchant marine on Defense cargo and MSC's policy of distributing the preponderance of its cargo to the low-cost carrier over the entire 6-month contract period often meant that one carrier could receive substantial DOD business in one 6-month period but almost none the next, effectively threatening its survival.

DOD recognized that distributing all its cargo to the low-cost carrier might not be in its best interests. In 1974 it began limiting the amount of cargo any one carrier could receive on certain major routes. For example, MTMC, which books the cargo with specific carriers, is required to see that no carrier on the East Coast to continental Europe and the United Kingdom route, the East Coast to the western Mediterranean area route, and the West Coast to the Far East area route receives more than 75 percent of the total container cargo moving on these routes.

Cargo allocation, however, has not necessarily supported a mobilization base that DOD had in the past. The U.S. fleet continues to decline in size. Only a few years ago, four carriers offered DOD service from the East Coast to Europe. Now there are only two carriers. A few years ago, five carriers served the West Coast to the Far East route. Now there are only two carriers.

The allocation system has not necessarily provided DOD the lowest possible rates either. Carriers sometimes lack incentives to offer their lowest rates. With fewer carriers, often of varying cargo-carrying capability, competition does not work as well as it had in the past. For example, a carrier with a large carrying capacity competing against a smaller carrier can intentionally offer a high rate knowing that the overflow cargo from the smaller carrier will be substantial and produce significant revenues. On the other hand, the smaller carrier can also offer a

high rate knowing that whatever cargo comes its way under the cargo limitation rules will produce significant revenues for it, too. Therefore, past incentives for low offers are often no longer operative.

One way MSC has attempted to address this problem has been to take a closer look at the rate offers by comparing them with commercial rates. MSC determined that some offers were not fair and reasonable and concluded that they should be rejected. This, however, has resulted in a series of disputes with the carriers over what constitutes fair and reasonable. Not obtaining satisfaction with MSC, the carriers have brought many of these rejections to the Comptroller General's attention for resolution. In a number of instances, the Comptroller General has found the rejections insupportable.

MSC Does Not Provide Carriers Necessary Information for Making Informed Offers

In soliciting rates for the movement of military cargo, MSC asks carriers to make offers without benefit of information on the specific types of commodities and the number of containers to be moved between specific origins and destinations—information that the carriers need to make informed offers and MSC needs to evaluate them properly. Without such information, carriers do not have the basic foundation as to how to formulate their proposals. Also, to the extent that it has not developed this information, MSC may be left without a sound basis for deciding whether a rate is fair and reasonable.

Military Rate Descriptions Broader Than Those of Commercial Rates

Instead of providing prospective offerors information about commodities and volumes between specific origins and destinations, MSC's semi-annual requests for proposals simply say that the cargo intended to be shipped is "military cargo and cargo owned by or intended for sale to servicemembers and their families (herein 'military cargo') (not for resale in commerce) and mail, with usual characteristics of shipments in substantial volume and varied makeup." They provide statistics showing tonnages shipped on ocean routes during some prior year but urge caution to offerors intending to use the figures for predicting future cargo movements.

Carriers are to submit the ocean rates as either "cargo, not otherwise specified," "refrigerated cargo," or "vehicles." These broad categories are in sharp contrast with commercial shipping practices, where rates are generally formulated on the basis of specific commodity descriptions and volumes of cargo between specific origins and destinations. Commercial rates are named for many different specific commodities—for

example, beverages, film, paint, rocket motors, and weed killers. These rates, however, are sometimes conditioned on shipping a minimum number of containers over a specified period of time and from one named point or through one named point to another. Although carriers maintain commercial rates for shipments described in MSC's terms—"cargo, not otherwise specified"—they use them essentially for shipments moving in irregular, low-volume patterns. Consequently, these rates are usually higher than specific commodity rates.

MSC Evaluates Offers Using Commercial Rates

Despite the differences between military cargo rates and commercial shipping rates, MSC uses commercial rates to attempt to determine whether the carriers' offers are fair and reasonable. However, instead of using the carriers' "cargo, not otherwise specified" rates for comparisons, MSC selects other rates, those with more specific descriptions and having certain other restrictions. For example, MSC may select a rate specifically applicable to clothing or one requiring the shipper to move 50 containerloads a year of some named commodity, compare it with the "cargo, not otherwise specified" rate, and decide the offered rate is too high and should be rejected. Many such rates have been rejected in the past year and a half.

Carriers argue that such comparisons are unfair because MSC should not be allowed to reject a rate on the basis of a commercial rate that may or may not apply to traffic DOD will be shipping. The carriers are not told what DOD is planning to ship or how much and they are not told what rates MSC will be using to make the comparisons.

Carriers have protested or supported others in protesting these rejections to the Comptroller General and have had their arguments supported. MSC's efforts to find and reject unfair and unreasonable rates are laudable, but unless MSC provides the carriers information about what they are submitting offers on and what their proposals will be compared with, its efforts are not likely to be successful.

Providing Specific Commodity Descriptions Could Help Ensure Reasonable Rates

In a 1981 report we previously voiced our concern about carriers having to compete for unknown requirements.¹ We recommended that MSC canvas each of its shippers to identify—in terms of origin/destination, volume of cargo over time and per container, and type of cargo—its specific requirements; review this data to establish what DOD shipping patterns existed; and make these requirements known to the carrier industry. MSC did not concur with our recommendations and, accordingly, took no action on them.

The situation seems to us to have changed since that report in that the number of carriers offering rates has dropped significantly. Where four or five carriers may have offered rates on a route before, now only two or three are doing so. To ensure that DOD will continue to receive favorable rates, MSC could provide the carriers its most detailed historical shipping data, specifically that showing the specific commodities it has shipped, and then use that data to compare the offers with commercial rates.

In addition, if MSC clearly stated in its requests for proposals that it will use specific descriptions to compare carriers' offers with commercial rates, there would be no misunderstanding that commercial rates would serve as a factor for determining whether a rate is fair and reasonable.

Specific Commodity Information Is Readily Available

Specific commodity data that MSC could provide to carriers is readily available from MTMC. Commodity descriptions—those basically adequate for comparing military rates with those for commercial shipments—are coded on the manifests MTMC prepares in connection with every container it books. The commodity codes are listed and spelled out in DOD Regulation 4500.32-R, "Military Standard Transportation and Movement Procedures," and must be assigned by each shipper to all shipments moving in ocean transportation. There are more than 400 such codes, many very specific, covering commodities such as furniture, household goods, medical supplies, beverages, and beer, as are used in connection with commercial rates.

To validate that such codes are used, we reviewed the containers shipped outbound from the East and Gulf coast ports in January 1991. A total of 10,737 containers were listed, with 194 different commodity codes. Although the code used most often—16.72 percent of the time—

¹Weaknesses in Negotiating Rates and Services for Commercial Containerized Sealift (GAO/PLRD-81-27, April 28, 1981).

**Chapter 3
Ocean Rate Negotiation Should
Be Strengthened**

was applied to "general cargo, not otherwise specified," more than 62 percent had some specific code suitable for comparing military cargo with commercial cargo.

Table 3.1 summarizes the number of containers by code for the most frequently used codes. The list covers about 75 percent of the containers shipped during January 1991.

Table 3.1: Most Frequently Used Commodity Codes for Containers Shipped From the East and Gulf Coasts During January 1991

Code	Commodity description	Number of containers
700	General cargo, NOS ^a	1,795
500	Subsistence, NOS ^a	659
70X	Hazardous materials, other than ammunition or explosives	600
70D	Consumer commodity goods	496
51A	Meals, combat	472
867	Vehicles, military ambulances, buses, trucks, not exceeding 2-1/2-ton capacity	455
192	Freeze subsistence, NOS ^a	351
505	Beverages, nonalcoholic, in tins	342
534	Medical supplies, NOS ^a	276
51J	Combat rations, sundry pack	269
320	Automobiles, space required	262
401	Bulk propellants, hazardous	227
503	Beer	227
603	Petroleum, lubricating or similar oils	204
613	Parcel post, sacked	173
712	Furniture, new, other than household goods	149
882	Vehicles, military trucks, exceeding 2-1/2-ton capacity	133
664	Barbed wire	127
102	Beef, chilled, boxed or carcass	121
741	Troop issue clothing and equipment	104
501	Bakery goods	101
634	Cylinders, compressed gas, filled or empty	95
635	Chemicals, other than drugs or sundries, NOS ^a	91
515	Flour, prepared, in packages	90
586	Vehicle parts, other than automobile, NOS ^a	86
130	Chill subsistence, NOS ^a	84
721	Paper, other than napkins or towels	84

^aNot otherwise specified.

Rates Are Not Requested on the Same Basis as DOD Procures the Service

When DOD buys containerized service using MSC's negotiated rates, the individual rates for each segment of the movement—that is, from inland origin to port, port to port, and port to inland destination—lose their significance because DOD procures the service as a through shipment. That one carrier, for example, may have a \$10 land rate and another a \$1 rate is not important if the higher land rate is offset by a lower ocean rate. Yet, MSC continues to solicit and evaluate each segment rate on its own, a practice that distorts and complicates the offer and evaluation process.

In our 1981 report, we pointed out this problem, noting that MSC did not allow carriers to offer single factor rates based on specific traffic patterns—that is, specific origin and destination combinations. Instead, MSC required carriers to offer separate rates: (1) the U.S. inland route rate, (2) the ocean rate, and (3) the overseas inland route rate. MSC evaluated, accepted, rejected, or negotiated each type of rate separately and then ranked each carrier from low to high in order of its rates for each segment. But, ultimately, when MTMC used these rates to determine the low-cost route for individual shipments, it discarded these rankings for one of its own—the total cost (land-ocean-land) rank.

As it is DOD policy to procure safe, secure, reliable, and quality commercial services that will meet DOD requirements, DOD shippers are advised to ship direct from vendors to users whenever it is economical and consistent with the need to consolidate shipments to obtain lower transportation costs. The majority of DOD containerized cargo, therefore, is loaded at source, meaning the cargo does not have to be taken out of the containers until it arrives at its final destination. It moves over land, ocean, and land, and DOD is charged for using the three separate (land, ocean, land) rates. What is important is not each rate, but the sum of the rates.

MTMC's manifest data indicates that DOD's containers commonly move in well-established patterns from U.S. inland origins to overseas inland destinations. For example, during January 1991, hundreds of containerloads of cargo originated at military cargo consolidation points, such as those at New Cumberland and Mechanicsburg, Pennsylvania, and Robins Air Force Base, Georgia, and moved to specific overseas depots or units in regular patterns. Hundreds more moved from GSA, Army-Air Force Exchange Service, and Navy Resale System Office distribution centers and vendors in regular, established distribution patterns. All these containers generally moved in a combination land-ocean-

land service. Only a relatively small percentage of containers, principally those carrying privately owned vehicles or military members' household goods, moved only in ocean service.

Conclusions

DOD can improve its rate negotiations for containerized ocean cargo service. Too often carriers are submitting offers for DOD traffic without adequate information on what they are competing on. MSC can provide the prospective offerors with substantial data on commodity descriptions in planned shipping patterns. Such data would allow carriers to formulate their offers more intelligently and would place MSC in a better position to negotiate for lower rates.

Also, MSC is not requesting rates in a manner that allows evaluation of the total costs of actual shipments. By reviewing and evaluating rates for segments of a shipment, MSC misses opportunities to enhance competition for DOD's major shipping routes. Asking for single factor rates covering the overall route should place MSC in a better position to negotiate effectively.

Recommendations

We recommend that the Secretary of Defense direct MSC to

- develop and provide to all prospective offerors detailed information on what it has shipped in terms of specific commodities and number of containers between specific traffic patterns, as well as its best estimate of what it will be shipping in the future, and
- change its solicitations to request rates for the same pattern of service for which DOD actually procures the service.

Agency Comments and Our Evaluation

DOD commented that MSC, in conjunction with MTMC, would make specific historical data readily available to all carriers. However, the comments indicated that DOD was not convinced that all carriers would want additional information and that additional information in and of itself would not ensure more reasonable rates. Nonetheless, DOD stated that carriers would be advised that detailed information was available and that it would be provided at their request.

We believe, however, that MSC should provide such information to the carriers with the request for proposals without the carriers having to ask for it.

DOD generally agreed with the recommendation that MSC change its solicitations to request rates in line with the actual pattern of cargo movements of significant volume. DOD asserted, however, that to solicit single factor rates for more than the highest-volume routes would severely complicate the solicitation process. Nevertheless, DOD stated that MSC, in conjunction with MTMC, would investigate the feasibility of soliciting, in its next request for proposals, single factor rates for the highest-volume point-to-point routes.

We believe that soliciting single factor rates for the highest-volume routes is a step in the right direction and when this hopefully proves to be advantageous to DOD, such solicitations will be expanded to other relatively high volume routes next and so on down the line.

Our additional annotated evaluations of DOD's comments are presented in appendix I.

Progress Slow in Implementing Changes to Household Goods Rate Negotiation Process

DOD's process for negotiating rates for moving the domestic household goods of DOD personnel continues to lack an incentive for carriers to offer their best rates. In a February 1990 report, Household Goods: Competition Among Commercial Movers Serving DOD Can Be Improved (GAO/NSIAD-90-50, Feb. 12, 1990), we found that DOD's negotiating process inhibited competition among commercial household goods carriers. Because DOD allowed all carriers to meet the low rate bid during the initial bidding phase, carriers had little incentive to offer their best rates up front. We recommended that DOD replace or modify its bidding process. DOD agreed to consider our recommendation but has made slow progress in implementing any change. Although an implementation plan has been prepared, as of the time of our review, no date had been set for any change and no proposal had been submitted to industry representatives for comment.

Rate Process Involves "Me-Too" Negotiation

DOD pays commercial carriers about \$400 million a year to move the personal effects of military members and civilian employees within the continental United States. MTMC is DOD's agent for negotiating rates for the movement of household goods.

Twice each year MTMC solicits rates from the domestic moving industry to meet DOD's household goods shipping requirements. Bidding is done in two steps under a "me-too" type of negotiation. In the first step, each carrier submits a qualifying bid—stated as a percentage of a specified rate—for each route it intends to serve. Once these bids are accepted, they are made public for review by all bidders. In the second step, which is commonly called the "me-too" phase, carriers are permitted to change any rate they had offered to match that of a lower bidder.

The carriers' final bids are ranked in a low-to-high order and provided to the local shipping office officials for routing shipments. Where more than one carrier qualified to serve that location has offered the same low rate, the officials are required to distribute the shipments as equally as possible to each carrier regardless of which submitted the low rate first. In other words, the carrier that initially submitted the low bid is not entitled to any greater reward than another carrier that met the low rate during the "me-too" bidding phase. When there are more shipments than the carriers with the lowest rate can handle, the officials are required to move up the rate ladder to the next level and distribute the shipments as equally as possible to all qualified carriers at that level.

Prior GAO Report Identified Weaknesses in Rate Negotiation Process

In our February 1990 report, we said that DOD's two-step process for obtaining rates was not truly competitive. When carriers submitted bids in the first phase, they had little incentive to offer DOD their lowest rates. Knowing that they would have the opportunity to match the lowest rate offered and to eventually share equally in any traffic generated, most carriers made no effort to bid competitively during the initial bidding phase. Instead, most carriers merely bid a qualifying rate—often the same rate for every route they intended to serve—and then rebid, as necessary, at lower levels during the second phase of bidding. As a result, there was often little difference among many carriers' rates, and those carriers that did make the effort to initially submit the lowest rates were not given any greater reward than those that simply waited to match whatever other rates had been offered.

We also found that under this bidding process, many carriers set up subsidiary companies that were nothing more than "paper" companies whose sole function was to obtain a larger share of the DOD business for the larger corporate enterprise. These paper companies added nothing to the industry's capability to increase its capacity for handling DOD traffic. By providing an equal share of the traffic to paper companies, DOD's process was inequitable to the bidders that did not establish such companies.

In contrast to this process, the international rate solicitation process was more equitable, we found in our report. At one time DOD had employed a similar "me-too" bidding process to obtain rates for its international moves. In 1976 we reviewed that process and concluded that introducing more competition by rewarding the carrier offering the initial low rate would reduce rates, thereby resulting in savings to DOD in transportation costs.¹ Rates on a test route were reduced by an average of 19 percent when the "me-too" process was modified. Responding to our 1976 report, DOD revised its international rate-setting procedure. It modified the two-step bidding process to reward the carrier that offered the low rate first with a guaranteed percentage of traffic on the given route.

In our 1990 report we concluded that a change was needed in the domestic bidding process to encourage carriers to offer their lowest rates during the initial bidding phase and then reward those with the best bids. We said that replacing the current two-step bidding process with a one-step process, whereby all carriers had equal incentive to bid

¹Adoption of a Single Method of Shipping Household Goods Overseas—Pros and Cons (GAO/LCD/76-225, May 6, 1976).

the lowest possible rates and those offering the lowest rates for each route were rewarded with all the traffic they could handle, would probably provide the carriers the most incentive to offer their lowest rates initially. However, if DOD determined that such a bidding process would not provide it the moving capability needed or would result in an unacceptable quality of service, it could modify the process so that the carrier offering the lowest rate during the first phase was at least allocated a greater share of the traffic than any other carrier simply meeting the low rate.

We recommended that MTMC replace or modify the current two-step bidding process so that all carriers have an incentive to initially bid the lowest possible rates and the lowest bidder is rewarded for offering the lowest rate.

Progress in Making Any Change Has Been Slow

MTMC continues to solicit rates using the "me-too" bidding process in the same manner we reported on in February 1990. To date, DOD has not changed the domestic household goods rate bidding process, made any tests of a revised process, or offered industry representatives any proposals for comment.

On June 20, 1990, the Assistant Secretary of Defense (Production and Logistics) responded to our report by saying that DOD concurred with all the findings and recommendations. He said that MTMC would be tasked to revise the bidding process, although the time frame for replacing the current process would be at least 12 to 18 months.

In October 1990, MTMC offered the Assistant Secretary an implementation plan indicating that it would be at least March 1991 before any revision would be released to industry representatives for coordination and comment and that no final plan would be included in a solicitation before October 1991. No proposed revision had been released to industry representatives. Even if such a proposal were submitted today, and no opposition were offered, it would probably be November 1992 before any change in the solicitation process would be implemented.

Recommendation

We recommend that the Secretary of Defense direct MTMC to accelerate its efforts to implement our recommendation to replace or modify the current two-step bidding process so that all carriers have an incentive to initially bid the lowest possible rates and the lowest bidder is appropriately rewarded.

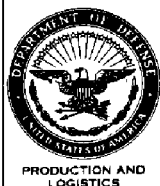
Agency Comments and Our Evaluation

DOD commented that changes to the solicitation process had been delayed 6 months because of manpower constraints associated with Operation Desert Storm and the evacuation of military household goods from the Philippines in the wake of volcanic eruptions. DOD noted that since rates are solicited only twice a year and MTMC missed its last window of opportunity, the corrective action plan cannot be accelerated. The remaining milestones of the implementation plan have accordingly been set back 6 months, with implementation now planned for November 1992.

It has been nearly 2 years since we first made our recommendation, and we urge MTMC to continue moving forward with its implementation plan.

Comments From the Department of Defense

Note: GAO comments supplementing those in the report text appear at the end of this appendix.



THE ASSISTANT SECRETARY OF DEFENSE

WASHINGTON, DC 20301-8000

November 1, 1991

(L/TP)

Mr. Frank C. Conahan
Assistant Comptroller General
National Security and
International Affairs Division
U.S. General Accounting Office
Washington, DC 20548

Dear Mr. Conahan:

This is the Department of Defense (DoD) response to the General Accounting Office (GAO) draft report, "DOD COMMERCIAL TRANSPORTATION: Some Programs Can be Made More Effective," dated August 20, 1991, (GAO Code 393394), OSD Case 8810. The DoD generally concurs with the report recommendations; however, further clarification and/or explanation is necessary with respect to several of the report findings.

The report addresses three DoD commercial transportation programs. First, the GAO concludes that the DoD needs to verify the effectiveness of its program for conducting prepayment audits of transportation bills and to notify local installation officials of results of the audits. The DoD concurs and is initiating action to implement these recommendations.

Second, the GAO recommends that the Military Sealift Command (1) provide prospective bidders with more detailed shipment information and (2) change its solicitations to request rates for the same pattern of service for which DoD actually procures services. The DoD is in general agreement with these recommendations, but contends that detailed information is now available to those bidders who desire it. Also, it is the DoD view that changing the solicitation process to obtain single factor rates would complicate, rather than simplify, the process.

Finally, the GAO recommends that the Military Traffic Management Command accelerate its efforts to replace or modify the current two-step bidding system for the procurement of household goods moving

Appendix I
Comments From the Department of Defense

services. The DoD supports the timely resolution of that issue. Due to manpower constraints the Military Traffic Management Command was unable to effect the recommended changes with the latest bidding cycle. Accordingly, the proposed changes cannot be accelerated any faster than called for under the revised corrective action plan.

The DoD appreciates the opportunity to review and provide comments to the GAO draft report. The detailed DoD comments addressing the report findings and recommendations are provided in the enclosure.

Sincerely,



David J. Berteau
Principal Deputy Assistant Secretary of
Defense (Production and Logistics)

GAO DRAFT REPORT - DATED AUGUST 21, 1991
(GAO CODE 393394) OSD CASE 8810

"DOD COMMERCIAL TRANSPORTATION: SOME PROGRAMS
CAN BE MADE MORE EFFECTIVE"

* * * * *

DEPARTMENT OF DEFENSE COMMENTS

- **FINDING A: Transportation Budgeting and Cost Responsibilities.**
The GAO observed that each Military Service and Defense agency is responsible for budgeting for and controlling transportation expenses. The GAO explained that each such component determines how much money is needed, what to ship, how much to ship, when to ship, and where to ship.

The GAO found that local installation and Defense office transportation personnel procure the services or have other Defense components procure the services. The GAO pointed out, however, that the Military Traffic Management Command is responsible for (1) approving carriers to serve the DoD, (2) negotiating domestic freight and international and domestic household goods rates, and (3) maintaining rates files. The GAO further reported that the Military Traffic Management Command also is responsible for routing carload and truckload shipments and other shipments requiring premium or specialized services.

The GAO observed that the Military Sealift Command is responsible for negotiating ocean cargo rates and serves as the DoD procuring contracting office for the Military Sealift Command shipping and container agreements and contracts. The GAO learned that the Military Sealift Command audits all agreement and contract payments prior to payment. The GAO noted, however, that until 1986, as was required by statute, the Federal Government paid Government Bill of Lading transportation charges prior to audit. The GAO pointed out that subsequent auditing was done by the General Services Administration, and that any overcharges recouped by the General Services Administration were returned to the DoD. The GAO found, however, that because the audits were performed a year or more after payment, the authority for the DoD to reuse the money had expired. The GAO further found that information about the overcharges was not timely for use in helping prevent future overcharges.

ENCLOSURE

Now on pp. 2, 8-9.

The GAO cited Public Law 99-627 (November 7, 1986), which changed the rules for auditing Government Bill of Lading transportation payments. The GAO explained that the General Services Administration no longer is required to return the money collected to the DoD, but it can use the money to pay the audit expenses and returns what is left to the Treasury. The GAO further explained that, for the first time, the General Services Administration could audit bills prior to payment and delegate prepayment audit authority to other departments and agencies. The GAO found that the DoD requested such prepayment audit authority soon after the law was passed, but did not receive the authority until July 26, 1988. (pp. 2-7, pp. 11-13/GAO Draft Report)

DOD RESPONSE: Concur.

• **FINDING B: Activities Directed to Establish Preaudit Capability.**

The GAO observed that the Assistant Secretary of Defense (Production and Logistics) advised the Assistant Secretaries of the Military Services and the Directors of the Defense Agencies that the DoD could save millions of dollars a year by auditing transportation vouchers prior to payment. The GAO reported the Assistant Secretary further advised that, with a significant opportunity to reduce budget shortfalls, it was critical that the DoD immediately implement a preaudit capability.

The GAO found out that, when the DoD received authority to conduct prepayment audits on July 26, 1988, the Assistant Secretary of Defense (Production and Logistics) directed each Military payment office and the Military Traffic Management Command to begin by immediately establishing the capability to preaudit domestic freight Government Bills of Lading. The GAO noted that the Military Traffic Management Command was to assist the payment offices by developing the data bases required to support the preaudits. The GAO further noted that the Military Traffic Management Command was to develop procedures to audit Government Bills of Lading manually, which offered a high potential return. The GAO found that each central payment office established preaudit capability--some using in-house staff and others using contractors or a combination of in-house staff and contractors.

According to the GAO, the Military Traffic Management Command auditors explained that preauditing was intended to do the following:

- detect overcharges early, thereby avoiding the lengthy delay inherent in the General Services Administration post-payment audit process;
- prevent the DoD from losing transportation dollars through overpayments, as had been occurring in the past when the General Services Administration audited the vouchers only after payment; and
- provide the shippers, the Military Traffic Management Command, and the carriers timely feedback about the overcharges so that the overcharging could be reviewed and remedial action taken. (pp. 3-7, pp. 16-17/GAO Draft Report)

Now on p. 12.

DOD RESPONSE: Concur.

- **FINDING C: Domestic Freight Bills Are Being Preaudited.** The GAO examined Government Bills of Lading issued by transportation offices and found that most domestic freight Government Bills of Lading were being sent correctly by the military payment offices to the Military Traffic Management Command for prepayment audit. The GAO reported that, by agreement with the Military Traffic Management Command, the central payment offices flag certain Government Bills of Lading and make copies available to the Military Traffic Management Command for preaudit. The GAO noted that, at first, only Government Bills of Lading with charges of \$10,000 or more and Government Bills of Lading moving at guaranteed traffic rates from certain depots were sent to the Military Traffic Management Command. The GAO further noted however, that the dollar threshold was lowered to \$8,000 in April 1989--and then down to \$5,000 in June 1989.

The GAO indicated that the Military Traffic Management Command, which had six full-time prepayment auditors, audited the Government Bills of Lading within 2 weeks of receiving them and reported back to the payment offices on the amounts that should be paid. The GAO further indicated that the payment offices then advised the billing carriers of any reductions to their bills. The GAO explained that carriers could appeal any reductions

through the payment offices to the Military Traffic Management Command--and to the General Services Administration, if necessary. The GAO reported that, according to the Military Traffic Management Command, in FY 1990, it (the Command) preaudited more than 8,000 Government Bills of Lading.

The GAO reviewed rail shipment Government Bills of Lading issued in connection with training exercises at the National Training Center during FY 1989 and FY 1990. The GAO found that most Government Bills of Lading were flagged and preaudited, as called for in the agreements. The GAO determined that, of the 209 Government Bills of Lading meeting the dollar threshold and issued after the Military Traffic Management Command began conducting preaudits, 204 or 97.6 percent, had been flagged and sent to the Military Traffic Management Command. The GAO noted that the DoD could not explain why the other five Bills of Lading had not been flagged and preaudited; however, the GAO did not consider that number to be significant. (pp. 3-7, pp. 17-18/GAO Draft Report)

DOD RESPONSE: Concur.

- **FINDING D: Prepayment Auditing is Helping DoD Avoid Losing Transportation Dollars.** The GAO estimated that, since the DoD prepayment auditing began, the DoD has identified nearly \$10 million in overcharges. The GAO explained that the \$10 million represents freight, household goods, and other carrier charges the DoD had been billed but did not pay based on the auditor findings.

The GAO pointed out that the DoD estimated that another \$34 million in overcharges were avoided because the existence of the prepayment audits made the carriers less likely to overcharge (i.e., sentinel effect). The GAO found that, since the DoD began preauditing, the General Services Administration has been identifying fewer overcharges during the postaudits--and the reduction is greater than the amount identified during the preaudits. According to the GAO, both the DoD and the General Services Administration attribute the improved situation primarily to the more careful billing habits by the carriers after they recognized that preauditing would prevent a payment that, in the past, probably would have been made. The GAO observed, however, that the DoD calculation of the \$34 million cannot be verified, inasmuch as it is based only

Now on pp 12-13.

on a guess of how the carriers changed their bills because they would be preaudited.

As an example of how the DoD is avoiding unnecessary payments through prepayment auditing, the GAO reviewed the Government Bills of Lading paid for shipments moving by railroad into and out of the National Training Center at Fort Irwin, California. The GAO indicated that the preaudits conducted by the Military Traffic Management Command enabled the Fort Irwin payment offices to avoid paying more than \$500,000 on FY 1989 and FY 1990 Government Bills of Lading. (pp. 3-7, pp. 18-21/GAO Draft Report)

DOD RESPONSE: Concur.

- **FINDING E: Prepayment Audits Can Be Further Strengthened.** The GAO concluded that prepayment auditing could be strengthened to help prevent even more overpayments. The GAO found that the DoD had not tested the audits to determine if all overcharges were being uncovered. According to the GAO, the General Services Administration post-payment audit data shows that some overcharges were not uncovered during preauditing. The GAO further found that, even when overcharging has been detected, the DoD had not provided feedback to the local installation transportation officials preparing the shipment documentation to make them aware that overcharging has occurred. The GAO pointed out that such feedback permits the local offices to take corrective actions to prevent future overcharges.

The GAO explained that the effectiveness of preaudits could be determined by comparing the results of bills audited before payment with those audited after payment. The GAO found, however, that the DoD is not making such comparisons. The GAO reviewed the audit status of all the Military Traffic Management Command-preaudited railroad Government Bills of Lading issued in conjunction with training exercises at the National Training Center during FY 1989 and found overcharges on about 16 percent of the FY 1989 Government Bills of Lading that had been preaudited.

The GAO reported that the Military Traffic Management Command auditors were unaware that any post-payment overcharge had been identified on a preaudited Government Bill of Lading. The GAO further reported that, according to the Military Traffic

Now on pp. 2-3, 13-15.

Appendix I
Comments From the Department of Defense

Management Command official, they had asked for the General Services Administration results of post-audits--but the General Services Administration was not able to provide the information.

The GAO discussed that with the General Services Administration and found that the data are now available, and could be used to provide some type of measure of the effectiveness of the preaudits.

The GAO previously addressed the overcharging problems in connection with moves to and from Fort Irwin in a May 1988 report (OSD Case 7570). The GAO noted that, in July 1989, which was subsequent to that report, Forces Command internal auditors found overcharging related to car charges was still occurring.

During its current review, the GAO found that the instructions were better and that the Government Bills of Lading were prepared more accurately; nevertheless, overcharges were still occurring. In no case, however, did the GAO find that a local transportation officer had been alerted about the overcharges or advised about the cause--or whether the overcharges could have been prevented. According to the GAO, many of the officials were surprised to learn they had been overcharged because it was their understanding that, under the terms of the rail agreements, carriers were required to notify them if there was a disagreement with the estimated charges the local officials had annotated on the Government Bills of Lading. The GAO noted those officials indicated that no carrier had inquired about disparate charges. The GAO reported that, if the carriers had inquired about charges, the officials indicated they could have possibly avoided an overcharge. (pp. 3-7, pp. 21-24/GAO Draft Report)

DOD RESPONSE: Concur.

- **FINDING F: Rate Negotiation and Procurement.** The GAO observed that each year the DoD spends about \$600 million for commercial ocean transportation. The GAO explained that the Military Sealift Command negotiates rates for millions of tons of the DoD cargo--the bulk of which moves in intermodal containers. The GAO described intermodal containers as 20- and 40-foot-long trailers in which the cargo can be hauled by truck, railroad, or ship--without further rehandling of the contents.

The GAO reported that the Military Sealift Command negotiations occur at 6-month intervals under terms of the Federal Acquisition

Now on pp. 2-3, 15-16.

Appendix I
Comments From the Department of Defense

Regulations. The GAO pointed out that bidding is based on the following:

- ocean route--further delineated as to the direction in which cargo will be moving--broad type of cargo (general, refrigerated, or vehicular)--and the size of container (basically, 20-foot and 40-foot) in which the cargo will move; and
- land route or drayage area--that is, the route from origin to the port or from the port to the ultimate destination in which the container will move in conjunction with its ocean voyage.

The GAO found that the Military Sealift Command bases its evaluation on criteria stated in the requests for proposals. According to the GAO, those criteria generally include comparisons (1) of old and new rates, (2) of the rates of one bidder with those of another bidder, and (3) of the bidder rates with commercial rates. The GAO pointed out the Military Sealift Command also advises the bidders that it has the right to reject a rate outright, or to negotiate with them for better rates, or to accept a rate without any negotiation. The GAO stated that accepted rates are provided to the Military Traffic Management Command, which uses them to route shipments.
(pp. 3-7, pp. 25-26/GAO Draft Report)

Now on pp. 18-19.

See comment 1.

DOD RESPONSE: Partially concur. The GAO report gives the incorrect impression that the Military Sealift Command evaluation relies almost exclusively on a comparison of rates offered with commercial rates. The GAO does not, however, fully define the Military Sealift Command's evaluation criteria, which are as follows:

- compliance with the 1904 Cargo Preference Act (which makes it unlawful for carriers to charge the Government more than private persons for carriage of like goods);
- on certain routes, comparison of 20-foot container rates with 40-foot container rates; and
- whether prices are fair and reasonable, pursuant to Federal Acquisition Regulation 15.805, evaluated separately for each route except for specified routes having similar market conditions or service.

Federal Acquisition Regulation 15.805-2 provides for price analysis, which includes (1) comparison of prices received under the solicitation, (2) comparison with prior proposal prices, (3) comparison with competitive published lists, and (4) comparison with Government estimates.

Therefore, under the current evaluation criteria used by the Military Sealift Command, comparison with commercial rates is only one of several evaluation criteria.

- **FINDING G: Problem of Ensuring That Rates Are Fair and Reasonable.** The GAO observed that the Military Sealift Command is faced with competing objectives--(1) obtaining the lowest rates possible for the DoD and (2) maintaining an adequate sealift base for mobilization. The GAO found that, on most of the routes for which it sought rates, the Military Sealift Command historically found adequate competition to produce low rates and still have adequate lift capability. The GAO pointed out that the Command did not have to engage in extensive face-to-face negotiations with carriers to obtain low rates.

The GAO noted, however that the carriers complained to the DoD and the Congress that the bidding system resulted in destructive competition--driving rates excessively low and forcing carriers out of business. The GAO reported the carriers argued that the heavy dependency of the U.S. merchant marine on Defense cargo and the Military Sealift Command policy of distributing the preponderance of cargo to the low cost carrier over the entire 6-month contract period often meant that one carrier could receive substantial DoD business in one 6-month period, but almost none the next--effectively threatening survivability of the carrier.

The GAO observed that the DoD had recognized that distributing all cargo to the low-cost carrier might not be in the best interest of the Department. The GAO explained that, as a result, the DoD began limiting the amount of cargo any one carrier would receive on certain major routes. The GAO concluded, however, the cargo allocation has not necessarily supported a mobilization base that the DoD had in the past. The GAO noted that the U.S. fleet continues to decline in size. The GAO cited an example

Appendix I
Comments From the Department of Defense

where only a few years ago, four carriers offered the Military Sealift Command service from the U.S. East Coast to Europe, but now there are only two carriers.

The GAO also found that the allocation system has not necessarily provided the DoD the lowest possible rates either. The GAO explained that carriers sometimes lack incentives to offer their lowest rates. The GAO concluded that, with fewer carriers, often of varying cargo carrying capability--competition is not working as well as it had in the past. The GAO further concluded that past incentives for bidding low are often no longer operative.

The GAO observed that--as one way of addressing the problem of decreased competition--the Military Sealift Command is taking a closer look at the offers by comparing them with commercial rates. The GAO reported that, as a result, the Military Sealift Command found some offers were not fair and reasonable, and determined that they should be rejected. The GAO further reported, however, that the process has resulted in a series of disputes with the carriers over what is fair and reasonable. The GAO noted that the carriers have brought many of the rejections to the attention of the Comptroller General for resolution. The GAO reported that, in a number of instances, the Comptroller General held the rejections to be unsupportable--effectively leaving the rate evaluation process in a state of uncertainty. (pp 3-7, pp. 26-28/GAO Draft Report)

Now on pp. 19-20.

See comment 2.

DOD RESPONSE: Partially concur. A 1989 study of the Military Sealift Command competitive sealift procurement system by Harbridge House concluded that, "It is inaccurate to attribute to DoD procurement policies the reduction in the number of U.S. liner vessels and operators that has occurred since World War II." The Harbridge House study attributed those reductions to factors such as high U.S. crew and vessel costs, sharp reductions in unit transportation costs due to the use of increasingly larger container ships, and the economic advantage enjoyed by large, vertically integrated transportation companies. The Harbridge House study also found that rates paid by the Military Sealift Command were comparable to those paid by commercial shippers, and pointed out that DoD cargo historically has provided a large, stable, and assured supply of cargo for U.S.-flag carriers over routes otherwise characterized by wide fluctuations in cargo volumes.

The GAO report also does not mention that, following an earlier 1988 review of the Military Sealift Command procurement practices, the GAO reported to the House Committee on Merchant Marine and Fisheries that: "MSC's present methods of contracting for ship operation and maintenance and cargo rate setting focus on obtaining the least cost to the Government, which is consistent with Government policy. If changes are to be made in order to support the U.S. maritime industry, which result in additional costs, it is important that those costs be identified and fully disclosed. Decision makers will then be in a position to make informed judgments about the cost and benefits associated with such a program."

The DoD disagrees with the GAO statement, "In a number of instances, the Comptroller General has found the rejections unsupported, effectively leaving the rate evaluation process in a state of uncertainty." The Military Sealift Command is aware of only one procurement over a 25-five year period, in a bid proceeding with two carriers, where the GAO found the Military Sealift Command rejection of rates was not supported fully. Also, as noted above, the Military Sealift Command revised its rate evaluation criteria in light of the GAO finding. In a subsequent finding, the GAO approved the method employed for rate reviews.

The DoD is currently evaluating the methods used for procuring sealift in conjunction with proposals to improve the DoD Sealift Readiness Program.

- **FINDING H: Military Sealift Command Does Not Provide Carriers Necessary Information for Making Informed Bids—Military Rate Descriptions Broader Than Those of Commercial Rates.** The GAO found that, instead of providing prospective bidders information about commodities, volumes, or patterns, the Sealift Command semi-annual requests for proposals simply say that the cargo intended to be shipped is "Military cargo not for resale in commerce and mail with usual characteristics of shipments in substantial volume and varied makeup." The GAO observed that, while the requests do provide statistics showing tonnages shipped on ocean routes during some prior year, they also urge caution to bidders intending to use the figures for predicting future cargo movements.

See comment 3.

Appendix I
Comments From the Department of Defense

The GAO explained that carriers are to submit the ocean rates as either "cargo, not otherwise specified," "refrigerated cargo," or "vehicles." The GAO concluded that those broad categories were in sharp contrast with commercial shipping practices, where rates are generally formulated on the basis of specific commodity descriptions, anticipated volumes of cargo, and traffic patterns. The GAO pointed out that commercial rates were named for hundreds of specific commodities--for example, beverages, hand tools, air conditioners, lumber, paint, clothing, and household goods.

According to the GAO, often those rates were conditioned on shipping a minimum number of containers over a specified period of time and from one named point or through one named point to another. The GAO indicated that, although carriers maintain commercial rates for shipments described in the Military Sealift Command terms, particularly, "cargo, not otherwise specified," they use them only in isolated instances--essentially for shipments moving in irregular, low-volume patterns. The GAO concluded, therefore, that those rates are the highest the carriers maintain. (pp. 3-7, pp. 28-32/GAO Draft Report)

Now on pp. 20-21.

DOD RESPONSE: Partially concur. The DoD generally agrees that military rate descriptions are broader than commercial rate descriptions. Commercial tariffs contain literally thousands of specific commodity rates, reflecting market place and competitive factors. Accordingly, broad commodity descriptions such as "cargo, not otherwise specified" are published in commercial tariffs to provide a rate in the event a specific rate is not available. While they may be the highest commercial rates, in actuality these rates are rarely, if ever, used. Since the DoD cargo is not for resale in the commercial sense, it is not subject to the same pricing constraints as commercial cargo. There is no need for the DoD to establish thousands of commodity rates found in a commercial tariff. Likewise, from the carrier standpoint, it should not matter what the DoD puts into a container. The per container cost to the carrier to transport a container is the same no matter what it contains. However, since the preponderance of DoD cargo moves outbound from the U.S., when the preponderance of the commercial cargo is moving in the opposite direction, carriers make economic decisions to price DoD cargo incrementally in order to receive some contributions to fixed costs that might otherwise go unrecovered. The DoD

See comment 4.

recognizes a need and provides carriers with general information concerning the nature of the cargo (e.g., whether it is hazardous or whether it is "weight" cargo). However, the DoD disagrees with the GAO statements (on pages 25 and 28 of the report) that the carriers need information on the specific types of commodities to be moved in order to make an "intelligent" or an "informed" bid.

Reducing Military cargo descriptions to the level of specificity to which commercial carriers define commodities would be inefficient for both the DoD and the carriers. The DoD tariff rates are greatly simplified and far less burdensome than commercial tariffs for carriers. These commodity descriptions have evolved over 25 years of use and carriers have never suggested that they be changed.

Finally, Military Standard Transportation and Movement Procedures commodity codes are contained in the cargo documentation provided to the carriers with the loaded containers and on the cargo manifest provided to the carriers by the Military Traffic Management Command. These codes can be translated by the carrier into the specific commodities that are being shipped by the DoD, and between what origin and destination points.

- **FINDING I: Military Sealift Command Does Not Provide Carriers Necessary Information for Making Informed Bids--the Military Sealift Command Evaluates Bids Using Commercial Rates.** The GAO observed that, despite the differences between military cargo rates and commercial shipping rates, the Military Sealift Command uses commercial rates in an attempt to determine whether offers by the carriers are fair and reasonable. The GAO found, however, that instead of using the carrier "cargo, not otherwise specified" rates for comparisons, the Command selects other rates, those with more specific descriptions and having certain other restrictions. The GAO cited an example where the Command may select a rate specifically applicable to clothing or one requiring the shipper to move 50 container loads a year of some named commodity--compare that rate with the "cargo, not otherwise specified" rate, and decide whether the offered rate is too high and should be rejected. The GAO learned that many such rates have been rejected in the past year and a half.

The GAO noted the carriers argue that such comparisons are unfair because the Sealift Command should not be allowed to reject a rate on the basis of a commercial rate, which may or may not apply to the traffic the DoD will be shipping. The GAO pointed out that the carriers are not told what the DoD plans to ship, how much, or between which points, or what rates the Command will be using to make the comparisons.

The GAO observed that several carriers have protested or supported others in protesting the rejections to the Comptroller General and, generally, have had their arguments supported. The GAO concluded that, although the Military Sealift Command efforts to find and reject unfair and unreasonable rates are laudable, unless the Command provides the bidders information on what they are bidding on and what their offers will be compared with, their efforts are not likely to be successful. (pp. 3-7, pp. 28-32/GAO Draft Report)

Now on p 21.

DOD RESPONSE: Nonconcur. While correct in stating the Military Sealift Command reviews commercial rates in accordance with the Cargo Preference Act of 1904 to determine whether a carrier's rates are fair and reasonable, the GAO is incorrect in stating that the Military Sealift Command may reject a carrier's offered general cargo rate as too high (i.e., not fair and reasonable) based on a comparison with "a" (i.e., one only) commercial rate. The Military Sealift Command currently performs an independent Government Rate Estimate of proper price level or value of services being purchased by utilizing a statistically based weighted average of commercial commodity rates. The latest historical data covering the movement of DoD cargos by Military Standard Transportation and Movement Procedures number is utilized to establish the general category of specific rates sought. That general category, is then weighted by the volume of DoD cargo shipped to establish an aggregated rate, which provides a commercial "benchmark" for reviewing rate offerings.

See comment 5.

The GAO assertion that a "cargo, not otherwise specified" rate more clearly reflects a more direct comparison with DoD cargo rates is clearly an oversimplification. Such a rate is placed in commercial tariffs to allow carriers the opportunity to publish a lower rate without an extended waiting period and, in unusual circumstances, to provide a rate in the event that no other rate applies. In normal commercial practice, the commercial carrier does not contemplate extensive use of such a

rate, since it is generally the highest rate in the tariff. Thus, such a rate does not reflect in any way a valid comparison with the cargo shipped by the DoD. The Military Sealift Command does not use commercial rate comparisons that are predicated on volume minimums, service contract filings, or other limited restrictions, as the GAO states. Specific commercial rates are not used to reject offered rates unless the description corresponds exactly with the offered rate description.

The GAO also states that the carriers are not told what the DoD plans to ship, how much, or between which points, or what rates the Command will use to make the comparisons. As previously noted, knowledge of the specific commodity (dry cargo, privately-owned vehicles, etc.) is unnecessary in order for the carrier to construct a rate. Cargo manifest data indicating specific military container cargo descriptions is provided to carriers on request by the Military Traffic Management Command on an ongoing basis. The carriers analyze the data in conjunction with their internal sales forecasting information to arrive at pricing strategies. Additionally, requests for proposal during the acquisition cycle include historical cargo movement data for trade routes covered for similar movements in prior years. That information is aggregated in terms of general commodity descriptions and stated in the requests for proposal. The carriers have been engaged in the business of transporting military cargo for many years and have knowledge of all the major continental United States origin and overseas destination points. They construct sophisticated marketing reports. The Department asserts that the level of DoD cargo is very stable and predictable over long periods of time, based on troop deployments.

- **FINDING J: Military Sealift Command Does Not Provide Carriers Necessary Information for Making Informed Bids--Providing Specific Commodity Descriptions Could Help Ensure Reasonable Rates.** In a prior 1981 report (OSD Case 5702), the GAO had voiced concern about not giving the carriers specific commodity descriptions of anticipated shipments. The GAO recommended that the Military Sealift Command canvas each shipper and identify--in terms of (1) origin/destination, (2) volume of cargo over time and per container, and (3) type of cargo--what the specific requirements were--review the data to establish what DoD shipping patterns existed, and make those requirements known to the carrier industry. The GAO pointed out that the Department of

Defense did not concur with the 1981 recommendations and, accordingly, took no action on them.

The GAO reported that, since 1981, the situation seems to have changed in that the number of carriers bidding rates has dropped significantly. The GAO noted that, where four or five carriers may have had bid rates on a route before, now only two or three are bidding. The GAO concluded that, to ensure the DoD will continue to receive favorable rates, the Military Sealift Command could provide the carriers its most detailed historical shipping data--showing the specific commodities that had been shipped, and then using that data to compare the offers with commercial rates.

The GAO further concluded that, if the requests for proposal clearly state specific descriptions will be used to compare carrier offers with commercial rates, there would be no misunderstanding that commercial rates would serve as a factor for determining whether a rate is fair and reasonable. (pp. 3-7, pp. 28-32/GAO Draft Report)

Now on pp. 3-4, 22.

DOD RESPONSE: Partially concur. The Military Sealift Command already provides the carriers detailed historical shipping data, showing the specific commodities it has shipped. The DoD will continue to make the data readily available to all carriers, as it has in the past. The Department is not convinced, however, that additional information will, in and of itself, ensure reasonable rates. The DoD asserts it is the fundamental economic factors that will always influence the level of rates offered the DoD.

See comment 6.

- **FINDING K: Military Sealift Command Does Not Provide Carriers Necessary Information for Making Informed Bids--Specific Commodity Data Is Readily Available from the Military Traffic Management Command.** The GAO observed that commodity descriptions--those that basically would be adequate for comparing Military rates with those for commercial shipments--are coded on the manifests the Traffic Management Command prepares in connection with every container booked. The GAO further observed that the commodity codes are listed and spelled out in DoD Regulation 4500.32-R, Military Standard Transportation and Movement Procedures, and must be assigned by each shipper to all shipments moving in ocean transportation. The GAO found that there were more than 400 such codes that were used in connection with commercial rates--with many very specific, covering such

commodities as (1) beverages, (2) hand tools, (3) air conditioners, (4) lumber, (5) paint, (6) clothing, and (7) household goods.

The GAO reviewed the containers shipped outbound from the East and Gulf coast ports in January 1991, to validate that such codes are used. The GAO found that 10,737 containers were listed, indicating 193 different commodity codes. The GAO found that the code used most often was applied to "general cargo, not otherwise specified" (16.74 percent of the time). The GAO concluded that more than 62 percent had some specific code suitable for comparing military cargo with commercial cargo. (pp. 3-7, pp. 28-32/GAO Draft Report)

DOD RESPONSE: Concur.

- **FINDING L: Rates Are Not Requested on the Same Basis as DoD Procures the Service.** The GAO found that, when the DoD buys containerized service using the Military Sealift Command negotiated rates, the individual rates for each segment of the movement loses its significance because the DoD procures the service as through shipment. The GAO further found, however, that the Sealift Command nevertheless continues to solicit and evaluate each segment rate on its own, as though the segment rate were important. The GAO concluded the described practice distorts and complicates the bidding and evaluation process.

The GAO stated that its 1981 report (OSD Case 5702) pointed out this problem, noting that the Sealift Command did not allow carriers to bid rates based on specific traffic patterns. The GAO reported that the Sealift Command required carriers to bid three separate rates: (1) the United States inland linehaul or drayage rate, (2) the ocean rate, and (3) the overseas linehaul or drayage rate. The GAO explained that the Sealift Command evaluated, accepted, rejected, or negotiated each type of rate separately and then ranked each carrier from low to high in order of its rates for each segment. The GAO emphasized, however, that when the Traffic Management Command used those rates to determine the low-cost route for individual shipments, it discarded the ranking for the total cost (land-ocean-land) rank, established by the Traffic Management Command.

The GAO found that the Traffic Management Command cargo manifests indicate that most of the DoD containers move in well-defined,

Now on pp. 22-23

U.S. inland points to overseas inland points. According to the GAO, only a relatively small percentage of containers, principally those carrying privately owned vehicles and household goods, move only from port to port.

The GAO pointed out, however, that the Sealift Command does not ask for, and consequently does not compare or evaluate, rates on the basis of those patterns. The GAO concluded that asking for rates over such patterns would enhance competition among carriers and reduce the rates. (pp. 3-7, pp. 32-34/GAO Draft Report)

Now on pp. 3-4, 24-25.

DOD RESPONSE: Partially concur. The GAO concludes that asking for rates governing carriers' intermodal movement patterns (as opposed to the Military Sealift Command's current practice of soliciting segmented rates) would enhance competition among competing carriers and reduce rates. The GAO does not, however, elaborate on the factual basis for the statement or the analytical reasoning behind it. Despite the lack of explanation, the Department agrees generally with the GAO premise in connection with through cargo movements of significant cargo volume. The Department asserts, however, that to solicit single factor rates for more than the highest volume routes would complicate, rather than simplify, the solicitation process, and force the Military Sealift Command to evaluate significantly more rates.

See comment 7.

Many of the inland linehaul rates are used in connection with more than one ocean route, both domestically and overseas. Consequently, linehaul rates take on a generic quality and may be used to create many different shipping combinations within the cargo movements of a given carrier. Automated analysis of the various carrier inland and water rate combinations results in booking cargo at the least cost to the Government for the through movement. Additionally, a need would still exist for individual linehaul rates to accommodate origin point to discharge port or discharge port to destination point shipments. In summary, the DoD agrees that limited implementation of the related recommendation may accrue certain benefits to the Government. The Department asserts, however, that implementation across the entire spectrum of potential intermodal rates would place an insupportable burden on the Military Sealift Command and further complicate the rate evaluation process. In particular, in the absence of commercial rates between the same origin and destination points, and unless

ocean rates are stated separately, it will adversely affect the ability of the Military Sealift Command to evaluate rates for compliance with the Cargo Preference Act of 1904. Nevertheless, the Military Sealift Command, in conjunction with the Military Traffic Management Command, will investigate the feasibility of soliciting in its next request for proposals certain single factor rates for the highest volume, point-to-point routes.

- **FINDING M: Rate System Involves "Me-too" Negotiation.** The GAO observed that the DoD pays commercial carriers about \$400 million a year to move the personal effects of Military members and civilian employees within the continental United States. The GAO reported that the Military Traffic Management Command is the DoD agent for negotiating rates for the movement of household goods.

According to the GAO, twice each year the Traffic Management Command solicits rates from the domestic moving industry to meet the DoD household goods shipping requirements. The GAO explained that bidding is done in two steps under a "me-too" type of negotiation. The GAO noted that, in the first step, each carrier submits a qualifying bid--stated as a percentage of a specified rate--for each route it intends to serve. The GAO further noted that once the bids are accepted, they are made public for review by all bidders.

The GAO described the second step, which is commonly called the "me-too" phase, which allows carriers to change any rate they had offered to match that of a lower bidder.

The GAO found that the final bids submitted by the carrier are ranked in a low-to-high order and provided to the local shipping office officials for routing shipments. The GAO pointed out that, where more than one carrier qualified to serve a location had offered the same low rate, the officials were required to distribute the shipments as equally as possible to each carrier, regardless of which one submitted the low rate first. The GAO explained that, in other words, the carrier that initially submitted the low bid is not entitled to any greater reward than another carrier that met the low rate during the "me-too" bidding phase. The GAO further found that, when there are more shipments than the carriers with the lowest rate can handle, the officials are required to move up the rate ladder to the next level and distribute the shipments as equally as possible to all qualified carriers at that level. (pp. 3-72, pp. 36-37/GAO Draft Report)

Now on pp. 3-4, 27.

DOD RESPONSE: Concur. The Department concurred with a GAO recommendation that addressed the same issue in the February 1990 GAO report entitled, "HOUSEHOLD GOODS: Competition Among Movers Serving DoD Can Be Improved" (OSD Case 8270). The DoD response stated that the Military Traffic Management Command would revise its bidding system to maximize competition and to reward the lowest bidder for the movement of domestic household goods. However, due to the lead time required to develop a new solicitation procedure, coordinate the procedure with industry, solicit rates in sequence with scheduled 6-month bid cycles, and modify automated systems, changing the solicitation process would take at least 12 to 18 months. Accordingly, the earliest the changes could be implemented would be the solicitation cycles for the fall of 1991 or spring of 1992. Changes to the solicitation process subsequently have been delayed another 6 months due to manpower constraints associated with Operation DESERT STORM and the evacuation of Military household goods shipments from the Philippines in the wake of volcanic eruptions. The Military Traffic Management Command expects to incorporate changes in the method of negotiating rates effective the fall of 1992. Since rates are solicited only twice a year, and the Military Traffic Management Command missed its last window of opportunity, the corrective action plan cannot be accelerated.

- **FINDING N: Prior GAO Report Identified Weaknesses in Rate Negotiation System.** The GAO referenced a February 1990 report (OSD Case 8270) in which it had concluded that the DoD two-step system for obtaining rates was not truly competitive. The GAO found that, when carriers submitted bids in the first phase, they had little incentive to offer the DoD their lowest rate initially because they would have the opportunity to match the lowest rate offered and eventually to share equally in any traffic generated. The GAO reported that, instead, most carriers merely bid a qualifying rate--often the same rate for every route they intended to serve--and then rebid at lower levels during the second "me-too" phase of bidding. The GAO had concluded that, as a result, there was often little difference among many carrier rates and, those carriers that did make the effort to submit the lowest rates initially were not given any greater reward than those that simply waited to match whatever other rates had been offered.

The GAO also had found that, under the current bidding system, many carriers set up subsidiary companies--most of which were

nothing more than "paper" companies, whose sole function was to obtain a larger share of the DoD business for the larger corporate enterprise. The GAO had concluded that those paper companies added nothing to the capability of the industry to increase the capacity for handling DoD traffic. The GAO concluded that, by providing an equal share of the traffic to paper companies, the DoD system was inequitable to the bidders who did not establish such companies.

In the prior report, the GAO had observed that the international rate solicitation system was more equitable. According to the GAO, at one time the DoD had employed a similar "me-too" bidding system to obtain rates for its international moves. The GAO observed a 1976 report (OSD Case 4126) had found that introducing more competition by rewarding the carrier offering the initial low rate would reduce rates, thereby resulting in savings in transportation costs. The GAO reported that, as a result of the prior report, the DoD revised the international rate-setting procedure by modifying the two-step bidding system to reward the carrier that offered the low rate first with a guaranteed percentage of traffic on the given route. The GAO calculated that rates on a test route were reduced by an average of 19 percent when the "me-too" system was modified.

The GAO noted that in the 1990 report (OSD Case 8270), it had concluded that a change also was needed in the domestic bidding system to encourage carriers to offer their lowest rates during the initial bidding phase and then reward those with the best offers. The GAO had recommended replacing the current two-step bidding system with a one-step system, whereby all carriers had equal incentive to bid the lowest possible rates and those offering the lowest rates for each route were rewarded with all the traffic they could handle. The GAO observed that would probably provide the carriers the most incentive to offer their lowest rates initially. (pp. 3-7, pp. 37-39/GAO Draft Report)

DOD RESPONSE: Concur.

- **FINDING O: Progress in Making Any Changes Has Been Slow.** The GAO found that the Military Traffic Management Command continues to solicit rates using the "me-too" bidding system in the same manner reported on in February 1990. According to the GAO, the DoD has not (1) changed the domestic household goods rate bidding

Now on pp. 3-4, 28-29.

Appendix I
Comments From the Department of Defense

system, (2) made any tests of a revised system, or (3) offered industry representatives any proposals for comment.

The GAO referred to the June 20, 1990 response, in which the DoD had concurred in all the findings and recommendations--and indicating that (1) the Military Traffic Management Command would be tasked to revise the bidding system and (2) the time frame for replacing the current system would be at least 12 to 18 months. The GAO found that, in October 1990, the Military Traffic Management Command offered the Assistant Secretary of Defense (Production and Logistics) an implementation plan, indicating that it would be at least March 1991 before any revision would be released to industry representatives for coordination and comment and no final plan would be included in a solicitation before October 1991. The GAO asserted however, that as of July 1991, no proposed revision had been released to industry representatives. The GAO pointed out that, even if such a proposal were submitted today (and no opposition were offered), it would probably be October 1992 before any change in solicitation is implemented. (pp. 3-7, pp. 39-40/GAO Draft Report)

DOD RESPONSE: Partially concur. As indicated in the response to Finding M, the Military Traffic Management Command is unable to accelerate changes to its household goods solicitation process. The original plan called for implementing program changes with the spring 1992 bid cycle. However, manpower constraints associated with Operation DESERT STORM and the emergency evacuation of household goods shipments from the Philippines in the wake of volcanic eruptions have delayed changes to the bidding process until the next bidding cycle (fall 1992).

Now on pp. 3-4, 29.

RECOMMENDATIONS

- **RECOMMENDATION 1:** The GAO recommended that the Secretary of Defense direct the Military Traffic Management Command and other units performing prepayment audits to test the effectiveness of their preaudits by comparing the results with bills audited after payment. (pp. 7-8, p. 24/GAO Draft Report)

DOD RESPONSE: Concur. In the second quarter of FY 1992, the General Services Administration will be formally requested to provide results of post prepayment audits. The General Services Administration results will be compared with DoD prepayment audits to assess the effectiveness of the DoD audit programs.

- **RECOMMENDATION 2:** The GAO recommended that the Secretary of Defense direct the Military Traffic Management Command and other units performing prepayment audits to develop a system for ensuring the timely notification of local installation transportation officials when the auditing activities detect overcharges. (pp. 7-8, p. 24/GAO Draft Report)

DOD RESPONSE: Concur. In FY 1992, the Military Traffic Management Command and other units performing prepayment audits will implement a system for ensuring the timely notification of local installation transportation officials when the auditing activities detect overcharges.

- **RECOMMENDATION 3:** The GAO recommended that the Secretary of Defense direct the Military Sealift Command to develop and provide to all prospective bidders detailed information on what it has shipped in the past in terms of (1) specific commodities, (2) number of containers, and (3) traffic patterns--as well as its best estimate of what it will be shipping in the future. (pp. 7-8, p. 34/ GAO Draft Report)

DOD RESPONSE: Partially concur. The Military Sealift Command, in conjunction with the Military Traffic Management Command, will make specific historical data readily available to all carriers. The Department is not convinced that all carriers will want additional information nor will additional information in and of itself, ensure reasonable rates. Carriers will be advised that detailed information is available and will be provided at their request.

Now on pp. 4, 17.

Now on pp. 4, 17.

Now on pp. 4, 25.

Appendix I
Comments From the Department of Defense

Now on pp. 4, 25.

- **RECOMMENDATION 4:** The GAO recommended that the Secretary of Defense direct the Military Sealift Command to change its solicitations to request rates for the same pattern of service for which the DoD actually procures the service. (pp. 7-8, p. 34/GAO Draft Report)

DOD RESPONSE: Partially concur. The DoD agrees generally with the GAO recommendation in connection with through cargo movements of significant cargo volume. The Department asserts, however, that to solicit single factor rates for more than the highest volume routes would severely complicate rather than simplify the solicitation process. Many of the inland linehaul rates are used in connection with more than one ocean route, both domestically and overseas. Consequently, linehaul rates take on a generic quality and may be used to create many different shipping combinations within the cargo movements of a given carrier. Nevertheless, the Military Sealift Command, in conjunction with the Military Traffic Management Command, will investigate the feasibility of soliciting in its next request for proposals single factor rates for the highest volume, point-to-point rates.

Now on pp. 4, 29.

- **RECOMMENDATION 5:** The GAO recommended that the Secretary of Defense direct the Military Traffic Management Command to accelerate its efforts to implement the 1990 recommendation to replace or modify the current two-step bidding system so that all carriers have incentive to initially bid the lowest possible rates and the lowest bidder is appropriately rewarded. (pp. 7-8, p. 40/GAO Draft Report).

DOD RESPONSE: Partially concur. The DoD agrees with the recommendation to replace or modify the current two-step bidding system that was identified in the GAO February 1990 report "HOUSEHOLD GOODS: Competition Among Movers Serving DoD Can Be Improved (OSD Case 8270)." The Military Traffic Management Command had developed an implementation plan to comply with the report recommendation, citing a 12-18 month implementation process. Accordingly, the earliest the changes could have been implemented would have been during the solicitation cycles for the fall of 1991 or spring of 1992. Due to delays caused by manpower constraints associated with Operation DESERT STORM and the emergency evacuation of household goods shipments out of the Philippines in the wake of volcanic eruptions, the Military Traffic Management Command will implement the remaining key milestones as follows:

Appendix I
Comments From the Department of Defense

<u>DATE</u>	<u>EVENT</u>
Present to January 15, 1992	Change/Revise Concept (Phase II)
February 1, 1992 - April 1, 1992	Finalize Concept (Phase III)
April 15, 1992	Release Solicitation to Industry
November 1, 1992	Implementation

Since the rates are solicited only twice a year, the earliest cycle for implementing the recommendation is now November 1, 1992, and therefore, cannot be accelerated.

The following are GAO's comments on DOD's letter dated November 1, 1991.

GAO Comments

1. We did not mean to imply that MSC relied exclusively on a comparison of rates offered with commercial rates. Comparison of rates offered with commercial rates was only one of the criteria listed, as the report notes.
2. Our present findings centered not on the entire 25-year period since MSC began negotiating rates competitively (1966), but only on the period of time since September 1989 when MSC first began rejecting hundreds of carrier rates. Thus, we do not believe that the Harbridge House study or the testimony we prepared for the House Merchant Marine Committee prior to September 1989 are germane to our findings about MSC's rejection of rates beginning in September 1989.
3. A number of carriers have filed protests with the Comptroller General concerning MSC's rejection of rates. These included (1) Topgallant Lines, Inc., and American President Lines, Ltd., following MSC's rejection of rates in September 1989; (2) Lykes Bros. Steamship Co., Inc., and American President Lines (supported by Sea-Land Service, Inc.), following MSC's rejection of rates in March 1990; and (3) American President Lines, both before and after MSC rejected rates in early 1991. Not all these protests were carried through to a decision, as the carriers withdrew the protests when MSC subsequently decided not to reject some of the offers. All in all, the protests involved hundreds of rates. In Lykes Bros. Steamship Co., Inc., B-236834.4, July 23, 1990, the carrier submitted approximately 3,400 rates and MSC rejected more than 900 of them. The Comptroller General found that many of the rejections were insupportable. In American President Lines, Ltd., B-236834.3, July 20, 1990, MSC likewise rejected numerous carrier rates, and the Comptroller General found that all but six were improperly rejected.
4. We are not proposing that MSC establish thousands of commodity rates. We believe that MSC needs to know how its commodities translate to commercial commodity rate descriptions so that MSC can have the information it needs to compare the more generically described military rates with the more specifically described commercial rates. We also believe that more specific information about what DOD is intending to ship, using past shipments as a basis for forecasting future shipments, is vital to helping carriers formulate informed offers and that the same information is vital to helping MSC evaluate the comparability of offers

with commercial rates. MSC, therefore, should give such information to the prospective offerors prior to the bidding and not place the burden for obtaining it on them.

5. In our report, we said that MSC used commercial rates to attempt to determine whether carriers' offers were fair and reasonable. We said that MSC may select a commercial rate applicable to a specific commodity and compare it with the carrier's offered "cargo, not otherwise specified" military rate. We did not, however, say that MSC used a single rate comparison for rejecting a rate.

With respect to DOD's explanation of its use of an independent government rate estimate, we assume that DOD was referring to its use of a "market basket" of DOD commodity descriptions. For example, MSC used 23 descriptions, including items such as combat rations, bakery goods, beer, and nonalcoholic beverages, to represent its "cargo, not otherwise specified" traffic and 13 descriptions to represent its refrigerated cargo. While we agree that a market basket could be used to compare offers with commercial rates, MSC did not establish that DOD was shipping the market basket commodities on each route for which it made the comparisons.

We did not say that "cargo, not otherwise specified" rates more clearly reflected a direct comparison with DOD rates. We said that if MSC did not know the commodities, volumes, or actual routes on which it was shipping, it had no other rate to compare the offers with.

For MSC to say it does not use commercial rate comparisons that are predicated on volume minimums or service contract filings is a misstatement of fact. The record of rate rejections clearly shows, for example, that service contracts were used to compare military rates with commercial rates.

Finally, while we recognize that historical shipping data is available for the carriers should they ask for it, we believe that it would make much more sense for MSC to provide it to the carriers with the request for proposals without the carriers having to ask for it. The primary benefits of this practice are that it would allow them to make informed offers by seeing the actual forecast of specific shipments DOD is planning and would provide MSC with information that it could use in comparing the offers with commercial rates.

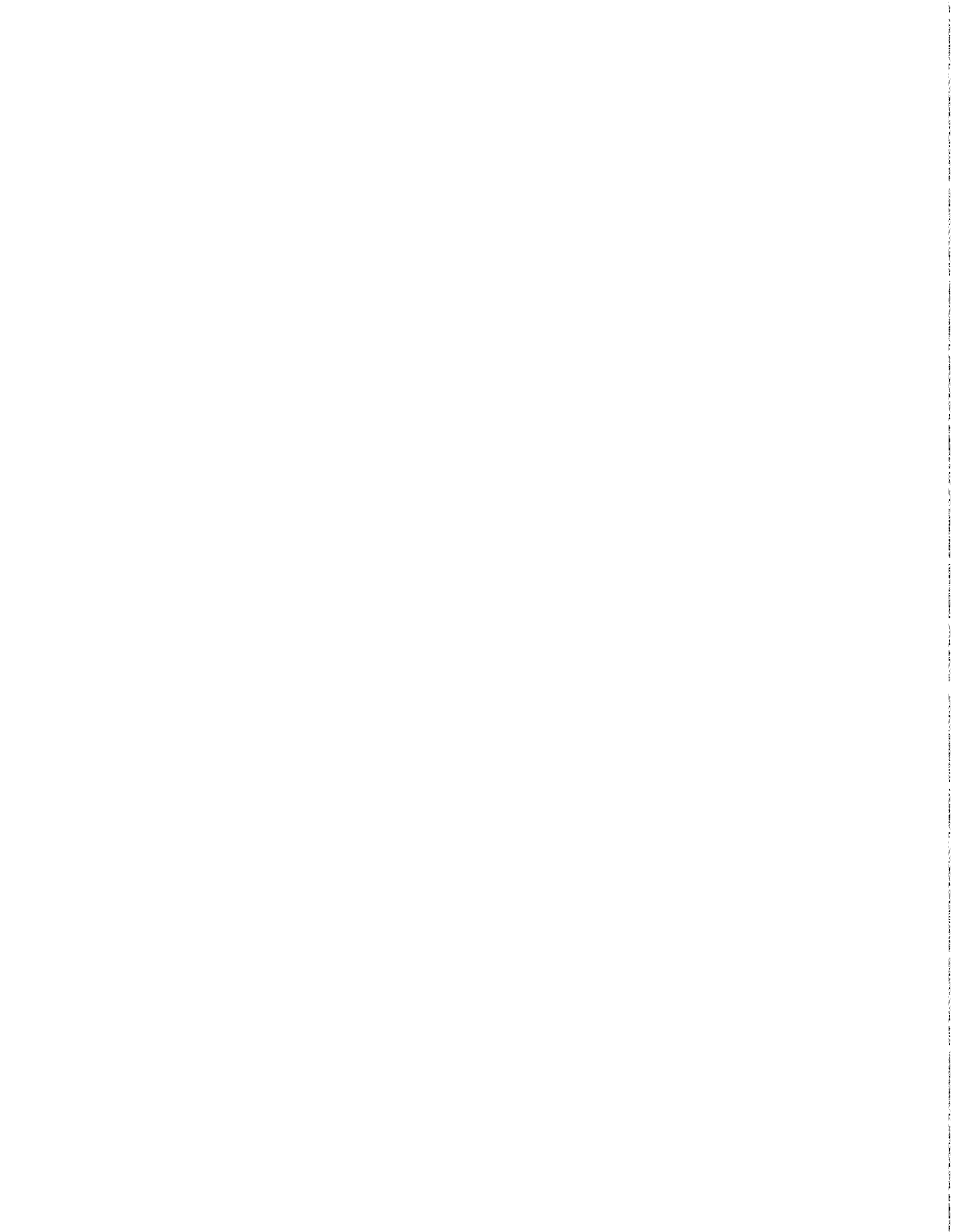
6. As we stated previously, we believe that it would make more sense for MSC to provide such information to the carriers with the request for proposals without the carriers having to ask for it.

7. We did not say that MSC should solicit single factor rates for every possible combination of origins and destinations. We believe that soliciting single factor rates for the highest-volume routes is a step in the right direction and when this hopefully proves to be advantageous to DOD, such solicitations will be expanded to other relatively high volume routes next and so on down the line.

Major Contributors to This Report

National Security and
International Affairs
Division, Washington,
D.C.

Henry L. Hinton, Associate Director
Edward M. Balderson, Assistant Director
J. Kenneth Brubaker, Evaluator-in-Charge



Ordering Information

The first copy of each GAO report is free. Additional copies are \$2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

**U.S. General Accounting Office
P.O. Box 6015
Gaithersburg, MD 20877**

Orders may also be placed by calling (202) 275-6241.

**United States
General Accounting Office
Washington, D.C. 20548**

**Official Business
Penalty for Private Use \$300**

**First-Class Mail
Postage & Fees Paid
GAO
Permit No. G100**
