

GAO

Briefing Report to the Chairman,
Subcommittee on Oversight of
Government Management, Committee
on Governmental Affairs, U.S. Senate

August 1990

DEFENSE INVENTORY

Information on Disposal of Unrequired Inventory



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National Security and
International Affairs Division

B-239601

August 17, 1990

The Honorable Carl M. Levin
Chairman, Subcommittee on Oversight
of Government Management
Committee on Governmental Affairs
United States Senate

Dear Mr. Chairman:

As requested, we are providing information regarding the disposal of the Department of Defense's (DOD) unrequired inventory. This report summarizes and updates our April 3, 1990, briefing to your staff. Unrequired inventory is stock that is not needed to meet current requirements but is held to satisfy possible future requirements and possible contingencies. Specifically, this report provides information on (1) unrequired inventory available for disposal and sale, (2) the condition of potential excess inventory and the related storage costs, and (3) inventories disposed of and sales proceeds.

Unrequired Inventory Available for Disposal and Sale

DOD reported in its September 1989 Supply System Inventory Report that it had about \$34 billion in four categories of unrequired inventory, including \$10.1 billion in the potential excess category. Potential excess is the category of unrequired inventory that DOD considers available for disposal and sale. DOD classifies spare parts and other secondary inventory items as potential excess when the items' retention cannot be justified for defense or economic reasons. According to a DOD official, the amounts are reported at a standard price (the last purchase price, manufacturer's listing, or market quotation, plus a surcharge for such things as transportation, losses, and inflation). The amounts of potential excess that DOD reported are shown in table 1.

**Table 1: Reported Potential Excess as of
September 30, 1989, by DOD Component**

Dollars in billions	
DOD component	Amount
Army	\$.5
Navy	6.8
Marine Corps	.1
Air Force	1.2
Defense Logistics Agency	1.5
Total	\$10.1

The amount of inventory that should be disposed of may exceed the reported excess. For example, in March 1990, we reported¹ that \$2.3 billion of the \$3.5 billion unrequired Navy ship and submarine parts inventory that we sampled should be considered for deletion and subsequent disposal. This \$2.3 billion consists of unrequired inventory in addition to potential excess and exceeds the \$2 billion the Navy reported as potential excess for ship and submarine parts. Consequently, we believe that deletions and subsequent disposals should be considered for more items than DOD now categorizes as potential excess.

Potential Excess Inventory Condition and Storage Cost

DOD estimates that about two-thirds of the \$10.1 billion potential excess inventory is used material that needs repairing (i.e., not ready for issuance). According to DOD, its records do not indicate how many of the items in need of repair cannot be economically repaired or how many of the issuable items are new.

According to DOD officials, annual inventory storage costs are approximately 1 percent of the cost of the items. Thus, the average annual storage costs are about \$101 million. We are currently reviewing the cost considerations of holding inventory and the implications on inventory management decisions under another review.

Sales Proceeds From Inventory Disposals

According to DOD officials, items classified as excess are turned over to the Defense Logistics Agency's Defense Reutilization and Marketing Service for disposal. The items are available for sale only after they are offered through a screening process to other defense agencies, the General Services Administration, state and local governments, and approved private organizations. Nonfederal organizations do not reimburse the federal government for items transferred during the screening process but do reimburse the federal government for shipping costs. Items not claimed during the screening process are generally sold. Table 2 shows the value (at the standard price) of the property disposed of during fiscal years 1988 and 1989.

¹Defense Inventory: Growth in Navy Ship and Submarine Parts (GAO/NSIAD-90-111, Mar. 6, 1990).

**Table 2: Property Disposals by Method
for Fiscal Years 1988 and 1989**

Dollars in millions		
Disposal method	Value of property	
	1988	1989
Intra- and inter-service transfers	\$1,248	\$1,712
Foreign military sales	12	19
Transferred to other federal agencies	117	251
Donations	293	290
Sale of usable property	1,839	2,113
Scrapped	3,024	3,635
Abandoned, destroyed, or used as targets	393	221
Total	\$6,926	\$8,241

DOD regulations specify that property may be abandoned or destroyed only when a property disposal official has determined in writing that the property has no commercial value or that the estimated cost of care, handling, and preparation for sale would exceed estimated sales proceeds. DOD also requires that selected items be demilitarized (made unusable for their original military purpose) before disposal. According to DOD officials, the value of property used as targets is included with abandoned and destroyed property.

DOD reported that the value of usable property sold was \$1.8 billion² in fiscal year 1988 and \$2.1 billion in fiscal year 1989 and that the proceeds from the sales were \$107.6 million and \$139.7 million, respectively. According to a DOD official, \$72.4 million and \$80.1 million of the proceeds from sales in fiscal years 1988 and 1989, respectively, were deposited in the U.S. Treasury. The remaining amount (\$94.8 million for the 2 fiscal years) was used to reimburse the services for authorized expenses. Table 3 shows the proceeds of foreign military sales and the sale of usable property and scrap for the 2 years. DOD attributes the relatively low return on the sale of the excess property to such factors as the used condition of much of the property sold, limited civilian uses, and surcharges included in the property's reported value.

²The amounts of property disposals and the proceeds from sales include property other than secondary inventory items. DOD does not maintain separate records on the disposal and sale of secondary inventory items.

Table 3: Proceeds From Sales for Fiscal Years 1988 and 1989

Dollars in millions

Type of sale	Proceeds from sales	
	1988	1989
Foreign military sales	\$0.7	\$1.1
Sale of usable property	49.6	61.3
Sale of scrap	57.2	77.2
Subtotal	107.6^a	139.7^a
Less authorized expenses	-35.2	-59.6
Total proceeds deposited in the U.S. Treasury	\$72.4	\$80.1

^aDoes not add due to rounding.

Scope and Methodology

To obtain information on unrequired inventory available for sale and related issues, we interviewed officials from the Office of the Assistant Secretary of Defense (Production and Logistics) and reviewed DOD reports on inventory and on utilization and disposal.

As agreed with your staff, we did not estimate the extent to which items in the budget are excess to requirements, as you had initially requested. DOD's budget is based on projections of what its requirements and its on-hand inventory will be at the beginning of the budget year. The process is designed to budget only for items where the inventory is projected to be less than requirements. Further, our prior work indicates that most items become unrequired after they are ordered and/or received.

We conducted our review between March and April 1990. As requested, we did not obtain written agency comments. However, we discussed a draft of this report with DOD officials and incorporated their comments as appropriate.

As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from its issue date. At that time, we will provide copies to interested congressional committees; the Secretary of Defense; and the Director, Office of Management and Budget. We will also provide copies to other interested parties upon request.

Please call me at (202) 275-8412 if you or your staff have any questions concerning the report. Major contributors to this report were Uldis

Adamsons, Assistant Director, and Louis Modliszewski, Evaluator-in-Charge.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Donna Heivilin". The signature is fluid and cursive, with the first name "Donna" being more prominent than the last name "Heivilin".

Donna M. Heivilin
Director, Logistics Issues

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