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Because the District of Columbia does not have an economical and effective supply system, vital city services such as health care and education sometimes were hindered. Simultaneously, the departments accumulated much unneeded stock. A central management group is needed to establish and direct a citywide supply management program if the District is to improve its supply system. Findings/Conclusions: Although the District has been told several times over the years to establish central management and controls over its supply activities, little or no progress has been made. Unneeded or overstocked items, valued at \$6.9 million in current inventories, could be sold, returned, or used to reduce the inventory to the necessary minimum level. City services should not be disrupted due to this reduction, and the city could possibly save \$7.1 million each year. Recommendations: The Mayor should implement the City Council's resolution concerning the establishment of an effective supply system. In establishing such a system, the Mayor should give authority and responsibility for formulating and implementing the system to a central management group; include in the design for the city's new financial management system financial and other information needed to manage the system; and justify fully to the Congress the positions and operating funds used to implement the system. (Author/SC)

03845



COMPTROLLER GENERAL'S REPORT TO THE CONGRESS AND TO THE MAYOR AND COUNCIL OF THE DISTRICT OF COLUMBIA

What Needs To Be Done To Improve The Supply System Of The District Of Columbia

Because the District of Columbia does not have an economical and effective supply system, vital city services have, on occasion, been hindered by supply shortages. At the same time, much unneeded stock was accumulated.

A central management group with authority and provided with accurate and complete information is needed to establish and direct a citywide supply program. About \$7.1 million may be saved annually by improving supply practices.



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

3-118638

To the President of the Senate and the
Speaker of the House of Representatives
and the Mayor and Council of the
District of Columbia

This report describes the uneconomical decentralized supply operations in the District of Columbia and demonstrates the need for centralizing the management of the citywide supply system.

We made our review pursuant to the District of Columbia Self-Government and Governmental Reorganization Act, approved December 24, 1973 (Public Law 93-198, 87 Stat. 774).

Copies of this report are being sent to the Director, Office of Management and Budget.


Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS AND
TO THE MAYOR AND COUNCIL
OF THE DISTRICT OF COLUMBIA

WHAT NEEDS TO BE DONE
TO IMPROVE THE SUPPLY SYSTEM
OF THE DISTRICT OF COLUMBIA

D I G E S T

Because the District of Columbia does not have an economical and effective supply system, vital city services, such as health care and education, sometimes were hindered. Simultaneously, departments accumulated much unneeded stock.

For example, two departmental supply operations were in short supply or out of stock of many drug, medical, and educational items while at the same time accumulating about \$1.2 million in unneeded supplies. (See pp. 10 and 11.)

A central management group is needed to establish and direct a citywide supply management program if the District is to improve its supply program. Although the District has been told several times over the years (as early as 1912) to establish central management and controls over its supply activities, little or no progress has been made. (See ch. 1.)

Unneeded or overstocked items, valued at \$6.9 million in current inventories, could be sold, returned, or used to reduce the inventory to the necessary minimum level. City services should not be disrupted due to this reduction, and the city could possibly save \$7.1 million each year. (See app. I.)

The District has more supply and procurement personnel, more money invested in inventories, and more storage space than does Baltimore, Maryland, or Milwaukee, Wisconsin. Both cities are comparable to the District in size and population and provide similar services, but both have more centrally managed supply and procurement systems. (See p. 12.)

GGD-77-32

At four major departments, in varying degrees:

- No uniform procedures and guidelines existed for departments to use in (1) deciding what and how much to stock, (2) estimating when and how much to reorder, and (3) identifying, reporting, and disposing of unneeded stock.
- Information normally used to manage and make supply decisions (for example, on inventory balances and estimated supply levels) was usually incomplete and inaccurate. Supervisors failed to make sure that stock records were posted properly or that stock levels were computed accurately. Also physical inventories were either not made or generally accepted accounting and auditing practices for State and local governments were not being followed.
- Costs associated with storing and distributing goods were not considered in deciding whether to stock items. Operating costs could be saved by having more items, particularly those available from Federal supply sources, delivered directly to the user rather than to a warehouse.
- Controls for lessening the investment in inventory, such as stock cataloging, reporting, standardization, and disposal programs, did not exist.
- No central management group monitors the individual department's supply activities to encourage them to follow accepted supply practices.

Except for an abortive attempt in 1974, the Department of General Services has taken no recent steps to establish a citywide supply program (see chs. 1 and 2), even though it is responsible for supply matters in the District.

On May 3, 1976, the Council of the District of Columbia recognized the importance of the problem. It pointed out in a resolution that (1) complete and reliable information was needed to manage supply activities and (2) a central

supply and management group with clear-cut authority was needed to start a citywide program. If the Mayor adopts the Council's resolution, an economical and effective supply system for the District could be established.

After GAO studied the supply operations of four District departments, they made some major improvements in inventory controls, recordkeeping, and supply practices in general. Also each department identified and began to eliminate unneeded stock. The Department of Human Resources identified about \$550,000 worth of unneeded stock and took steps to transfer these items to other departments or return them to supply sources for credit. About \$100,000 worth of undelivered purchase orders were canceled, and as of April 1977 about \$96,000 in credits had been given by suppliers for returned items. (See p. 15.)

The Mayor should implement the Council's resolution concerning the establishment of an effective supply system. In establishing such a system, the Mayor should

- give authority and responsibility for formulating and implementing the system to a central management group,
- include in the design for the city's new financial management system financial and other information needed to manage the system, and
- justify fully to the Congress the positions and operating funds used to implement the system.

The Mayor said that the District was planning to establish a supply management work group which would be responsible for developing a plan for improving and strengthening the District's procurement and supply system. The group will work closely with the commission established to develop an improved financial system for the District, to make sure that the supply management system is integrated in the overall financial management system. (See app. III.)

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ABBREVIATIONS

| | |
|-------------|---|
| DCPS | District of Columbia Public Schools |
| DES | Department of Environmental Services |
| DGS | Department of General Services |
| DHR | Department of Human Resources |
| DOT | Department of Transportation |
| GAO | General Accounting Office |
| GSA | General Services Administration |

CHAPTER 1

INTRODUCTION

EARLIER STUDIES SHOWED LONGSTANDING DISTRICT SUPPLY MANAGEMENT PROBLEMS

Several groups have, since 1912, periodically studied District supply management activities, including our Office. Each study found that, in general, controls over inventories were inadequate and operations were uneconomical--too much inventory and storage space and too many employees. The primary recommendation of each study was that centralized management control over inventories and operations should be established.

House of Representatives report issued in 1912

The House reported that District of Columbia supplies were not economically purchased, properly warehoused, or effectively distributed. Also stocks on hand and deliveries to departments were unknown because of poor recordkeeping practices. The House report suggested establishing a central warehouse under the control of a general storekeeper who could systematically store, maintain, distribute, and account for supplies.

GAO reports issued in 1959 and 1969

In our report "Review of Management Controls of the District of Columbia Government" (B-118538, Mar. 11, 1959), we concluded that decentralized supply operations were generally uneconomical because they resulted in excessive investments in supply inventories. We also suggested centralizing supply and procurement responsibility and establishing proper and reliable supply data for management purposes.

In our March 28, 1969, letter report to the Commissioner of the District of Columbia, we reported that departmental supply data was unreliable; that no reports were made for evaluating the economy and effectiveness of operations; and that a uniform stock numbering (cataloging) system, a key element needed to implement a citywide supply and procurement program, had not been completed. We recommended that the authority for developing and implementing a citywide supply system be clearly defined. We also recommended that the District develop procedures and a catalog for inventory control and requirements planning.

National Institute of Governmental
Purchasing, Incorporated, report issued in 1970 1/

The institute's survey of supply operations in the District disclosed the following weaknesses:

- Overinvestment in inventory, space, and personnel.
- Duplicate stocking of the same item in many places.
- Too many line items carried in inventory.
- No systematic way to determine unneeded stock.
- Slow-moving inventories.
- No coordination on supply matters among departments.

The institute recommended that a centralized supply management group be established and given the responsibility for (1) developing common supply policies and procedures for the departments, (2) reducing the number of line items and inventory investment, and (3) establishing more effective inventory controls.

Nelsen Commission report issued in 1972 2/

This commission estimated that about \$20 million could be saved (about \$10 million in annual recurring savings) by implementing a centrally controlled and operated procurement and supply program in the District. It recommended establishing centralized supply authority to (1) develop and implement uniform policies and procedures and (2) reduce investment in inventory, space, and personnel. The commission suggested it would be administratively easier and more effective to improve conditions by assigning managerial as well as policy control to this central function.

1/"Survey of Supply Operations in the District of Columbia," National Institute of Governmental Purchasing, Incorporated, Washington, D.C., July 23, 1970.

2/"Report of the Commission on the Organization of the Government of the District of Columbia," U.S. Government Printing Office, Washington, D.C., Aug. 17, 1972.

DISTRICT'S APPROACH TO THE PROBLEM

The Department of General Services (DGS) has District-wide responsibility for procurement and supply matters. DGS supply management responsibilities include (1) policy formulation, (2) contract authority for acquiring supplies, (3) surplus property disposal, and (4) implementation of automated supply systems, including procurement and inventory control subsystems.

Each department, however, has its own supply policies, stocks, warehouse facilities, personnel, catalogs, ordering practices, and records. About 30 District organizations maintain supply inventories valued at about \$12.1 million. The District has about 60 locations, throughout the city, with about 2 million square feet of inventory storage space. These supply activities are operated by about 540 supply and procurement personnel.

District Organizations with Supply Inventories for the Period Ended June 30, 1975 (note a)

| <u>Number of organizations</u> | <u>Value of supply inventories</u> |
|------------------------------------|--|
| 14 | \$10,000 and under |
| 6 | \$10,001 to \$49,999 |
| 3 | \$50,000 to \$99,999 |
| 4 | \$100,000 to \$999,999 |
| <u>4</u> | \$1 million and over |
| <u>31</u> | |

a/This date reflects the latest inventory values available on individual District agency supply operations.

Commodity management experiment failed

In November 1974 DGS started an experimental supply program, referred to as commodity management, to implement recommendations of earlier study groups. One department was designated to act as the sole purchaser and supplier for specific groups of items (commodities), such as drugs. Three departments were selected for this experiment: the Department of Human Resources (DHR) for medical supplies and equipment, the Metropolitan Police Department for weapons and ammunition, and DGS for small tools and office machines. This program was expected to realize considerable savings in (1) procurement costs by consolidating departmental requirements for similar items and (2) operating costs by reducing inventory carrying costs.

About 7 days after the program was initiated, DHR was authorized by the Mayor to withdraw. Delays in providing needed hospital supplies were cited as the prime reason for the withdrawal. But DHR officials told us they were not given the necessary additional staff to meet the increased workload. Later the DGS Director discontinued the commodity management experiment. DGS officials said that the experiment could not be continued because it lacked the administrative support and cooperation of DHR, the largest city department.

The District tried to implement the commodity management program contrary to advice given in the Nelsen Commission report. The commission concluded that such a program would not work because (1) operating departments were not set up to perform procurement and supply functions, without extensive realignments, (2) agencies would probably feel that their needs were not given priority, (3) departmental overhead costs to administer the system would detract from proposed savings, (4) overlapping management functions would exist between DGS and the agencies, (5) financial arrangements would be awkward, and (6) existing supply organizations were generally not staffed to handle the increased workload and responsibilities.

SCOPE OF REVIEW

The purpose of this review was to follow up on previous GAO, congressional, and nonprofit organization studies of the District's supply management program. We wanted to find out (1) how effectively and economically materials were being provided to city departments and (2) if benefits would accrue from a more centrally managed supply system. (See ch. 2.)

For our review, we selected four District departments--DHR, the Department of Transportation (DOT), the Department of Environmental Services (DES), and the District of Columbia Public Schools (DCPS)--because they had 74 percent of the District's inventory and warehouse space. Also they employed 62 percent of supply and procurement personnel. We examined their supply policies, procedures, and records and those of DGS. Reports, detailing problems in each department, were issued earlier to each department director.

For comparison purposes, we obtained data on supply operations in the cities of Baltimore, Maryland, and Milwaukee, Wisconsin, because their geographic size and population are similar to the District's. For the most

part, those cities operate a centrally managed supply system. However, we did not evaluate the economy and effectiveness of their supply programs.

We also collected similar data on inventory investment, value, composition, storage, and management from the District's decentralized operations, to assess the comparative economies of centralizing supply operations. (See p. 12.)

CHAPTER 2

CENTRALIZED MANAGEMENT NEEDED TO

CORRECT LONGSTANDING SUPPLY SYSTEM PROBLEMS

In the four departments we reviewed, providing vital city services, such as health care and education, was occasionally hampered because supplies were not available. At the same time, each department accumulated stock which was either obsolete or excess to its operating needs. For example, two departmental supply operations were in short supply or out of stock of many drug, medical, and educational items while at the same time accumulating about \$1.2 million in unneeded supplies. (See pp. 10 and 11.) We estimate that an annual recurring saving of \$7.1 million may be possible by keeping inventory to the minimum number of essential items. Also unmeasurable, nonrecurring savings may be possible through the sale, return, and cross-utilization of \$6.9 million worth of inventory items. (See app. I.)

These conditions were caused by the absence of:

- Uniform procedures and guidelines for departments to use in (1) deciding what and how much to stock, (2) estimating when and how much to reorder, and (3) identifying, reporting, and eliminating unneeded stock.
- Complete and accurate information needed to manage and make supply decisions.
- Controls for minimizing inventory investment, which would include cataloging, reporting, standardizing, and disposing of supplies.
- A management (centralized) group, headed by an individual with authority and expertise, to design and operate a citywide supply program.

DGS has been ineffective in making improvements to longstanding supply problems. Except for an abortive attempt in 1974 (see pp. 3 and 4), DGS has made no recent efforts to design and implement an economical, effective, and centrally managed supply program, even though it is responsible for supply matters. According to DGS officials, they do not have authority and staff to make necessary improvements to supply activities.

**SUPPLY MANAGEMENT DECISIONS ADVERSELY
AFFECTED BY INCOMPLETE AND INACCURATE DATA**

To make effective and economical decisions, supply managers must have accurate and complete information on (1) departmental operating requirements, (2) status of inventory balances, (3) historical usage trends, (4) assessment of alternative methods and costs to obtain materials, and (5) other decision parameters affecting citywide inventory management, such as best sources of supply, most economical storage levels for inventory, and stock available as surplus or excess from other city departments. Otherwise, supply decisions--whether or not to stock an item and when and how much to order--will continue to be little more than guesses.

**Cost information needed to
decide whether to stock an item**

None of the four departments studied nor DGS develops cost information to decide whether or not to stock an item. Such a decision should be based on whether it is cheaper to buy the item for storage and later make distribution or to have the item delivered directly to the user (department) for consumption.

In fiscal year 1975 about 59 percent (\$22.8 million) of the city's supplies was delivered directly to the using activity; the remainder (about \$15.6 million) was issued from warehoused supplies. However, costs of each alternative were not evaluated in deciding whether or not to stock an item.

The Commission on Government Procurement said in its report 1/ that it was not always true that warehousing was essential to maintain continuous support. Attention to an item's unit price is too often emphasized rather than the total cost to the Government, which would include a share of distribution costs. Agencies strive to achieve lower unit prices by obtaining volume discounts without evaluating the impact on the agencies' warehousing and distribution system. The commission recommended direct delivery to the user if lower total economic costs could be achieved.

1/"Report of the Commission on Government Procurement," vol. 3, "Supply Distribution Systems and Alternatives," part D, pp. 32 to 37, Dec. 1972.

The National Association of Wholesalers concluded in its study ^{1/} of wholesale distributor firms that it cost about 25 percent of total inventory value to store and distribute stock to customers (carrying costs). Since the District's organizations perform supply functions similar to those studied by the wholesaler association, they probably incur similar inventory carrying costs.

Inventory Carrying Costs as a
Percent of Total Inventory Value

| <u>Cost</u> | <u>Percent</u> |
|--|----------------|
| Obsolescence | 10.0 |
| Interest on invested capital (note a) | 7.0 |
| Deterioration | 5.0 |
| Handling and distribution | <u>2.5</u> |
| | <u>24.5</u> |

^{a/}Interest figure computed from the average Treasury rate paid on short-term notes and bonds outstanding as of June 30, 1976.

Carrying costs could be avoided if more items were delivered directly to the user, rather than warehousing them first, particularly products available from Federal supply sources, such as the General Services Administration (GSA). For example, about 30 percent of items warehoused (valued at about \$400,000) by DCPS was purchased from GSA. A GSA official told us that, upon request, GSA would deliver most items now shipped to the DCPS central warehouse directly to each school at no additional cost. About \$98,000 might have been saved if GSA-supplied items had been delivered directly to the schools.

DCPS officials agreed that, if GSA were requested to deliver these items directly, more items could be delivered by the September school openings and warehouse and delivery workloads would be lessened during the peak summer months. Also warehousing and distribution costs would be reduced. Other departments would also save money by having stocks delivered directly to users.

^{1/}"What Does It Cost to Carry Inventory?" National Association of Wholesalers, 1974.

Accurate inventory balances and
usage data needed to compute
supply levels and reorder points

Accurate records of onhand quantities and the rate at which items are consumed should be used in computing how much to stock and when and how much to reorder. However, most supply points operated by the four departments studied did not keep accurate records of onhand balances or past issues. As a result, many items were out of stock or sufficient quantities were not being ordered to meet expected needs. In other cases, there was more stock than could conceivably be used over a 2-year period.

Inventory balances

There were usually considerable unexplained differences between balances shown on stock records and physical counts. On five selected items DOT stocked, differences ranged from \$2,600 to \$28,000 per item. As the result of physical inventories taken in calendar year 1975, about 60 percent of the 2,475 items in the DCPS inventories showed differences between actual physical counts and balances recorded on stock cards. A DCPS supply official said that the primary reasons for such discrepancies were posting errors and improper or careless inventory-taking practices.

There were two principal reasons why departmental inventory records contained inaccurate onhand balances and erroneous estimates of reorder points and supply levels. (See pp. 10 and 11.) At most supply points there was no evidence showing that supervisory personnel periodically checked stock cards to find out if all transactions were recorded accurately and if estimated supply levels, reorder points, and reorder quantities were properly computed. Also physical inventory procedures were either not followed or inadequate.

Physical inventories are taken to verify recorded stock balances. The District's accounting manual requires that inventories be taken annually and that adjustments be reported to management. However, in DES a physical inventory was not taken from March 1973 until July 1975. After we brought this to the attention of DES supply management, physical inventories were begun, resulting in the identification of many items previously unrecorded.

In the three other departments, the same group or individual conducting physical inventories also made and approved adjustments to recorded stock balances. For example,

the DHR supply officer was responsible for recording stock transactions, supervising the conduct of physical inventories, and making adjustments to the records. Sound internal management controls require separating these functions to insure that inventory balances are recorded accurately and that differences are fully investigated and brought to management's attention. Separating these duties provides greater assurance that actual stock shortages are not concealed. In Baltimore and Milwaukee, the internal audit staff, an independent public accounting firm, or another department is responsible for supervising the conduct of physical inventories and investigating and reporting adjustments.

Supply levels and reorder points

Quantities of an item to be stocked for the first time are usually difficult to estimate because there is little historical data available to predict usage. Estimates can be based on past procurement actions, assessments by agency personnel using the newly stocked item, engineering estimates, and so forth. However, as soon as actual issue or consumption experience is available, this information should be used in computing supply levels and reorder points. The supply manager must continually review the item's use to find out if it continues to merit stocking and to help insure that inventory levels reflect program needs.

DHR supply reports, between January and April 1975, indicated the following conditions:

- Some items, including drugs (for example, some types of insulin and penicillin) were out of stock, or sufficient quantities were not being ordered to meet estimated supply levels necessary for operating health programs.
- Orders were placed for some items in excess of estimated required supply level.
- In other cases, onhand stock was more than could conceivably be used in over 2 years.

DHR supply officials investigated the causes for and extent of these conditions. They found that in most cases information used to compute supply levels was unreliable, contributing to any one of the three conditions described. The primary reason for the erroneous information, they said, was computer program and operator errors. For example, the computer operator did not use the most recent transaction file which updates

inventory balances, recomputes supply levels, or estimates when and how much to order. Officials also told us that after verifying onhand balances and supply levels, they identified about 1,500 line items, valued at about \$550,000 (out of a total inventory of \$2.4 million), that had over a 2-year supply on hand.

DCPS accumulated large amounts of unneeded stock (estimated to be \$700,000) because supply levels were not computed properly and did not reflect actual procurement lead-times (the period between ordering and receiving an item). At the same time, school items estimated to cost \$780,000 to replenish, such as various types of pencils, writing paper, and chalk, were in short supply or out of stock. In 29 of 30 cases we examined, maximum supply requirement levels were incorrect. On 22 items requirements were overstated by about \$14,000; on 7 items requirements were understated by about \$30,000. In one case, the level was understated by \$24,000 because the correct figure was not posted to a new stock card. Also, for the 30 cases examined, the lead-times experienced were considerably less than the 6-month leadtimes used by supply personnel. For the 30 cases, according to the stock records, there were 23 completed orders. For 12 of these orders, the supplies were received in less than 3 months, and for 6 orders the supplies were received in 3 to 5 months. For the five remaining orders, the supplies were received after the 6-month leadtime.

At several DOT supply points, issues from stock were recorded, but the information was not used to estimate reorder points and supply levels. Instead supply personnel often relied on visual observations of how much stock was on hand. Consequently, in some cases, items were ordered even though quantities on hand were excess to the amount needed to sustain continuous operations.

CENTRALIZED CONTROL OVER SUPPLY ITEMS NEEDED TO MINIMIZE INVENTORY INVESTMENT

A larger-than-needed inventory increases operating costs by requiring (1) unnecessarily high inventory investment, (2) more employees to maintain the inventory, and (3) more warehouse storage space. It also increases the impact of item deterioration and obsolescence. Control over the number of items in the supply system is essential for economy and effectiveness. Also funds tied up in unneeded items are unavailable for obtaining needed supplies. For these reasons, the supply manager must minimize the number and types of items and the total dollar investment in supply inventories.

The four departments studied (1) carried more of some items than was required by operating programs and (2) stocked items similar or identical to those stored by other departments (duplication). In addition, of the 31 organizations maintaining supply inventories and responding to our inquiries, 21 noted that general office supplies represented a large part of onhand inventories. Also several locations carried plumbing, electrical, automotive, and hardware items.

An analysis of supply operations in Baltimore and Milwaukee, which are centralized to a large extent, showed that these cities had much less inventory investment and utilized less space and fewer personnel than did the District.

Comparison of June 30, 1975, Supply Operations

| | Washington, D.C. | Baltimore | Milwaukee |
|--|---------------------|---------------|-------------|
| Population (1970) | 757,000 | 906,000 | 717,000 |
| Square miles in city | 61 | 78 | 96 |
| Number of supply and procurement personnel | 543 | 371 | 174 |
| Number of storage facilities | 58 | 33 | 26 |
| Square feet of storage space | 1,078,000 | 535,000 | 757,000 |
| Inventory value | \$12.1 million | \$6.7 million | \$6 million |
| Line items in inventory | 50,270 | 33,765 | 32,256 |

Except for health care--which Milwaukee does not provide--the District, Baltimore, and Milwaukee provide similar services and are comparable in size and population. Even when all of DHR (the department providing health care services in the District) is excluded, the District maintains more inventory (\$9.7 million) and storage space (866,000 square feet) and has more supply and procurement personnel (394) than does Milwaukee.

To minimize its investment in inventories, the District needs a central supply management group that would establish a (1) uniform cataloging system, (2) departmental reporting system on the status of supply levels, (3) standardization program to reduce the number of sizes, kinds, and types of similar items in stock, and (4) stock disposal program.

Uniform stock numbering (cataloging) system needed to identify similar items

The District has no uniform numbering or cataloging system. Each department, rather than DGS, assigns its own

identification numbers. In departments with multiple supply points, more than one number can be assigned to an identical product.

Cataloging is a process of assigning a unique number to identify items with similar or identical physical descriptions. It provides a common language for supply communication. The benefits of having such a common language and reporting system include:

- Cross-utilizing supplies in and between departments.
- Consolidating orders to obtain volume discounts.
- Reducing the number of similar or identical items kept in departmental inventories.

In DES each supply point assigned stock numbers, which resulted in (1) similar or identical stock being stored at two or more locations (duplication), (2) items being ordered by one location and already available at another supply point having excess quantities, and (3) orders not being consolidated from each location to obtain volume discounts and reduce the administrative costs of making multiple purchases.

Need to standardize items

Another element in reducing inventory investment is a standardization program. This entails reviewing stocked items (types and sizes) in relation to their uses, needs, engineering criteria, costs, and other factors. The results can be used to reduce the number of stocked items to the minimum needed to accomplish operating objectives. Because it lacked a uniform supply catalog and reporting system, the District could not establish a standardized inventory program.

Periodic reports needed to manage supply levels

Department managers above the departmental supply officer did not know how many individual items were over, under, or out of stock. Periodic status reports on individual stocks, which describe whether onhand inventories are above or below required supply levels, were either not prepared (DCPS, DES, and DOT) or prepared from inaccurate data (DHR).

To manage supply levels in each department and District-wide, catalog numbers should be assigned centrally, and stock status reports should be routinely provided to department and central supply management staff for review and monitoring

purposes. DGS neither assigns catalog numbers centrally nor attempts to collect information on the status of individual stocks from departments.

Need for a program to
dispose of unneeded stock

The District could have reduced its fiscal year 1975 inventory by \$6.9 million (57 percent) and achieved its 120-day supply goal (see app. I) by (1) eliminating unneeded stock and (2) setting supply levels that reflect actual procurement leadtimes and usage patterns. Annual recurring savings of \$7.1 million may be possible with such an inventory reduction. In addition, other unmeasurable and non-recurring savings are possible through interdepartmental transfers, sale, or return of all or part of the unneeded \$6.9 million inventory.

The four departments did not have an effective program for identifying and disposing of unneeded items. For example, in DOT reports comparing onhand balances with computed supply levels were not prepared to determine whether items were overstocked or infrequently or no longer used. Although DHR and DCPS had information which identified unneeded stock, management frequently did not sell or dispose of these items.

Departments were reluctant to transfer excess supplies to DGS because (1) the department received no credit from sales made by DGS and (2) they believed the supplies might be used at some unknown future date. Proceeds from such disposals are returned to the District's general fund. DGS officials told us, however, that for several years, very few excess supplies had been transferred for disposal. According to DGS procedures, departments can transfer unneeded stock to other city agencies and receive credit for such transfers. If other agencies do not need this stock, it can be transferred to DGS for disposal.

A central management group for the District could help insure that such unneeded stock is identified and eliminated. As discussed, DGS receives no departmental stock status reports that could be used to identify unneeded stock. Also DGS does not conduct routine departmental inspections or audits to identify unneeded supplies and insure adherence to accepted supply practices and established goals. Further, DGS officials said they had no authority to dispose of unneeded stock in the possession of individual departments, regardless of who identified it.

CHAPTER 3

RECENT EFFORTS TO IMPROVE SUPPLY MANAGEMENT

Little had been done by the District to correct supply conditions, except for recent efforts in the four large departments we reviewed and an unsuccessful attempt in 1974 to implement an economical and effective District-wide supply program. (See pp. 3 and 4.) The supply system is still decentralized, and generally accepted supply practices are not followed.

In May 1976 the Council of the District of Columbia passed a resolution (see app. II) calling for the Mayor to develop a central supply system. We believe this resolution, if implemented, could lead to the development of an effective and economical citywide supply system.

DEPARTMENT ACTIONS TO IMPROVE SUPPLY MANAGEMENT

As a result of our recent reports to the four departments studied, some major improvements have been made, including (1) establishing new stock records and reporting requirements to insure that reliable information is available to management, (2) establishing new procedures for determining requirements and stock levels, and (3) instituting or improving departmental controls over inventory and supply related actions. Also each department has identified and begun to eliminate unneeded stock; for example, DHR supply personnel have identified about 1,500 line items (valued at about \$550,000) that would take 2 or more years to use. On the basis of this information, \$100,000 worth of undelivered purchase orders, including orders for overstocked items, were canceled. Steps were also taken to either transfer these items to other District departments in need or return them to supply sources for credit. To date, several Federal supply agencies and over 100 vendors have been approached. As of April 1977, suppliers have given DHR credits amounting to about \$96,000 for items. In addition, many vendors have agreed to exchange overstocked items for supplies DHR needs.

COUNCIL RESOLUTION

On May 3, 1976, the Council, recognizing the seriousness of reported supply and procurement problems in the District and delays in correcting them, passed a resolution entitled "Material Management Systems Resolution of 1976." (See app. II.) The Council concluded the following:

- Vital city services had, on occasion, been hampered because supplies were not available.
- The city lacked an efficient and effective system to provide current and accurate data on supply trends.
- Many departments had accumulated large amounts of unneeded or obsolete stock.
- Design and implementation of a good system had been hindered because authority and responsibility for supply management were diffused throughout District departments.
- Millions of dollars could be saved annually by establishing an economical and effective supply system.

The Council resolved that the Mayor and the department heads make a commitment to implement an efficient and effective procurement and supply system for the District.

The Mayor was to prepare a tentative plan by September 30, 1976, showing what steps were needed to establish such a system. This plan was to include (1) a clear-cut identification of authority, responsibilities, and working relationships among District organizations, (2) goals and objectives of the supply management program (for example, uniform cataloging and accounting and inventory control methods), (3) adequate money and personnel for implementation, and (4) a timetable for each phase of the plan.

The Council also resolved that, while the overall plan was being formulated, the individual departments should (1) under the supervision of an independent body, inventory all supplies by June 30, 1976, (2) identify supplies excess to departmental needs, (3) develop methods to cross-utilize such stocks in other departments, and (4) dispose of remaining excesses to other non-District sources. As of July 26, 1977, the Mayor had not formally responded to the council's resolution by submitting a plan or ordering that departmental inventories be taken.

NEW FINANCIAL MANAGEMENT SYSTEM FOR THE DISTRICT

In June 1976 Arthur Andersen and Co. reported to the Congress on the "Accounting and Financial Management Practices of the District of Columbia Government." The report concluded that millions of dollars continued to be wasted due to significant and longstanding weaknesses in District

recordkeeping; internal controls; and management reporting systems, including those pertaining to supply management. District-prepared financial statements cannot even be audited. The report recommended that a new financial and accounting system be designed.

Responding to the District's needs, the Congress passed Public Law 94-399 on September 4, 1976. This legislation calls for the design and implementation of a new financial management system that would allow for a formal audit of the District's financial conditions, and which should (1) insure efficient use of available resources and (2) minimize the need for future Federal support. The Congress provided an authorization of \$16 million to fund this legislation (50 percent to come from the District).

CHAPTER 4

CONCLUSIONS, RECOMMENDATIONS, AND AGENCY COMMENTS

CONCLUSIONS

On occasion, the provision of vital city services, such as health care and education, has been hampered by shortages in certain types of supplies. At the same time, many departments have accumulated several million dollars worth of unneeded stocks. Basic causes giving rise to this condition have been the lack of (1) complete and reliable information needed to manage supply activities and (2) a central management group with clear-cut authority to establish, implement, and maintain an economical and effective supply program. Until recently, the District has made little progress in establishing such a program.

The Council recognized the importance of the problem and passed a resolution (see app. II) which, if implemented by the Mayor, should help to establish an improved supply program.

RECOMMENDATIONS

We recommend that the Mayor implement the Council's resolution concerning the establishment of an effective and centrally managed supply system. We also recommend that, in establishing such a system, the Mayor:

1. Give authority and responsibility for formulating and implementing the system to a central management group.
2. Include in the design for the city's new financial management system financial and operational information needed to manage the system.
3. Justify fully to the Congress the positions and operating funds used to implement the system.

AGENCY COMMENTS

According to the Mayor's June 17, 1977, letter (see app. III), the District is planning to set up a supply management work group to develop an action plan for improving and strengthening the District's procurement and supply system, including the use of centralized supply management procedures to the extent feasible. The group will define the needs of

the District's departments and agencies and insure that these needs are accommodated in a citywide system.

The plans and proposals of the work group will be closely coordinated with the work being planned by a commission established by Public Law 94-399 to oversee the development and implementation of improved financial systems for the District. The group will also review the plans developed for financial systems to insure that the supply management system is being fully integrated into the District's overall financial management system.

ESTIMATED SAVINGS IN DISTRICT SUPPLY OPERATIONS

In fiscal year 1975 the District maintained enough supplies to operate for about 280 days. The District's goal, established by DGS, is to maintain 120 days' supply in inventory. To achieve this goal, inventories could be reduced by \$6.9 million (57 percent), from \$12.1 million to \$5.2 million. Table 1 shows that annual recurring savings of \$7.1 million may be possible with such an inventory reduction. In addition, other unmeasurable and nonrecurring savings may be possible by (1) returning unneeded items included in the \$6.9 million inventory to suppliers for credit, (2) selling items to other governments or the public, or (3) cross-utilizing items among District departments.

Table 1--Annual Recurring Savings
from a \$6.9 Million Inventory Reduction

| <u>Cost category</u> | <u>Estimated savings</u> | <u>Table reference</u> |
|--------------------------|--------------------------|------------------------|
| | (000 omitted) | |
| Inventory carrying costs | \$1,691 | 2 |
| Storage costs | 844 | 3 |
| Personnel costs | <u>4,552</u> | 4 |
| Total | <u>\$7,087</u> | |

Table 2--Savings in Inventory Carrying Costs from
a \$6.9 Million Inventory Reduction

| | <u>Percentage saved</u> | <u>Savings</u> |
|---------------------------|-------------------------|----------------|
| | | (000 omitted) |
| Obsolescence | 10.0 | \$ 690 |
| Interest | 7.0 | 483 |
| Deterioration | 5.0 | 345 |
| Handling and distribution | <u>2.5</u> | <u>173</u> |
| Total | <u>24.5</u> | <u>\$1,691</u> |

Table 3--Savings in Storage Costs

| | |
|---|---------------------|
| Average inventory value per square foot of storage space | \$11.20 |
| Total inventory value (\$12.1 million) ÷ total storage space (1.08 million square feet) | |
| Reduced storage space requirements | 616,071 square feet |
| Inventory reduction (\$6.9 million) ÷ average inventory per square foot (\$11.20) | |
| Savings on reduced storage space requirements | |
| Reduced requirements (616,071 square feet) X average per square foot cost paid to lease space by the District (\$1.28 per square foot) = \$788,571 + interest saved at 7 percent = \$55,200 | |
| | \$843,771 |

Table 4--Savings in Personnel Costs

| | |
|---|---------------|
| Average inventory value per supply/procurement employee | \$22,300 |
| Total inventory value (\$12.1 million) ÷ total supply/procurement employees (543) | |
| Reduced personnel requirements | 309 employees |
| Inventory reduction (\$6.9 million) ÷ average inventory per employee (\$22,300) | |
| Savings on reduced personnel requirements | \$4,552,444 |
| Reduced requirement (309 employees) X average cost for a District employee (\$13,769, including salary and 10 percent benefits) = \$4,254,621 + interest saved at 7 percent = \$297,823 | |

COPY

A RESOLUTION

1-276

IN THE COUNCIL OF THE DISTRICT OF COLUMBIA

May 3, 1976

A resolution calling for the design, implementation, and operation of an efficient, effective, and centrally managed procurement and supply system for the District of Columbia; and for other purposes.

RESOLVED, BY THE COUNCIL OF THE DISTRICT OF COLUMBIA, That this resolution may be cited as the "Material Management Systems Resolution of 1976."

Sec. 2. The Council of the District of Columbia finds that:

(a) No unified system of procurement and supply management exists within the District government.

(b) Pilot programs recommended by the Commission on the Organization of the government of the District of Columbia regarding procurement and supply management have not been implemented, or, if experimentally initiated, have now been dismantled.

(c) The provision of vital city services have on occasion been hampered because supplies and services to be contracted for were not available due to a lack of an effective and efficient system, including a lack of complete, current and accurate data on supply trends. At the same time, many departments have accumulated significant amounts

of stock that is either obsolete or excess to their requirements.

(d) There is a diffusion of authority and responsibility for procurement supply management matters among the District departments.

(e) Implementation of modern, business-like procurement and supply methods would--

(1) enable supplies and services to be provided in a more timely manner, preventing disruption of needed city services, and

(2) save millions of dollars each year.

(f) Improvements to be made will enable the Council of the District of Columbia to better perform its oversight function for procurement and supplies activities now scattered throughout more than 60 agencies of the government.

Sec. 3. The Council of the District of Columbia declares that:

(a) A commitment of resources and personnel be established to design and implement an effective, efficient and centrally managed procurement and supply system for the District.

(b) The Mayor prepare a tentative overall plan, for submission to the Council by September 30, 1976, showing what steps will be taken to establish such a system for the District. This proposal should address, but not necessarily be limited, to the following considerations:

(1) clearcut identification of authority, responsibilities, and working relationships that each organization is to fulfill during the development and implementation of the plan as well as the operation of the system once implemented;

(2) goals and objectives of the plan, addressing such procurement and supply matters as, but not limited to, standardization of products, establishment of a uniform cataloging system, accounting and control methods to be used for supplies (e.g. revolving funds), use of EDP, adoption of consolidated procurement techniques, inventory storage and distribution methods, regional purchasing, the extent to which supply and procurement activities will be decentralized, and so forth;

(3) budgeting and personnel commitments needed to carry-out the plan, including specific identification of functions that will be contracted out for;

(4) timetable for beginning and completing each phase of the plan;

(5) identification of matters which require legislation by the Council; and

(6) report quarterly on the progress being made to the Council.

Sec. 4. While the actions in subsection (b) of section 3 of this act are being taken, there are many steps that should be taken to improve the efficiency and effectiveness of departmental supply operations:

(a) As of June 30, 1976, physical inventories of supplies should be taken in each department under the supervision of an independent body to be conducted in accordance with generally accepted accounting and auditing principles for State and local governments.

(b) Supplies, excess to a department's needs should be identified during such inventories, and a method should be developed to cross-utilize such stocks in other departments, or, make such excesses available for return, sale or disposal to vendors or other Federal, State, or local governments.

Sec. 3. This resolution shall take effect upon its adoption.



THE DISTRICT OF COLUMBIA

WALTER E. WASHINGTON
MAYOR

WASHINGTON, D. C. 20004

JUN 17 1977

Mr. Victor L. Lowe, Director
General Government Division
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Lowe:

This is in response to your letter of March 16, 1977 with which you enclosed for our comment your draft report on a review of the District's supply management program. We have completed a review of the report and the following comments are submitted for your consideration.

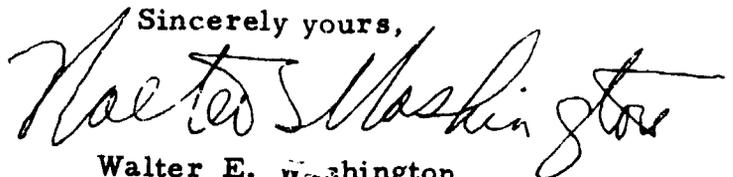
The recommendations contained in your report and the related matters discussed in a resolution of the City Council concern issues which must be considered in the context of the District's overall financial management improvement program. As you know, the Congress in 1976, enacted Public Law 94-399 which established a Commission to oversee the development and implementation of improved financial systems for the District. One of the issues which must be addressed in the development of the District's financial systems is inventory control and the procedures necessary to produce reliable financial data on inventories. Although the Commission has not initiated action to commence the overall systems development project, the District is moving to bring about systems improvements where possible on a "piece meal basis." In the area of supply management, the Department of General Services is currently proceeding with a plan to assist the various departments and agencies in carrying out more efficient and effective supply operations.

The magnitude and complexity of the supply function of the District require that any major improvement effort in this area be adequately planned and coordinated giving due consideration to the needs and special requirements of the departments and agencies. Accordingly, we are planning to set up a supply management work group to develop an overall action plan for improving and strengthening the District's procurement and supply system including the use of centralized supply management procedures to the extent feasible. The group will define the overall needs of the District's departments and agencies and assure that those needs are accommodated in the development of a city-wide system. This group will be chaired by the Mayor's Special Assistant for Financial Systems Development with representation from the Office of Budget and Management Systems, Department of General Services and other selected departments and agencies. Administrative support will be provided by the Office of Budget and Management Systems with DGS providing primary technical systems development support. The plans and proposals of this group will be closely coordinated with the work being planned by the Commission established under Public Law 94-399. The work group will review the plans developed for related financial systems to assure that the supply management system is being fully integrated into the District's overall financial management system.

At such time as the plans are sufficiently firm to determine the budgetary requirements for the project, we will prepare and submit a budget item to obtain the necessary approvals for operating funds.

We appreciate the opportunity to review and comment on this report in draft form. We hope our comments will be useful in the preparation of your final report.

Sincerely yours,



Walter E. Washington
Mayor

PRINCIPAL OFFICIALS OF
THE DISTRICT OF COLUMBIA GOVERNMENT
CONCERNED WITH ACTIVITIES DISCUSSED
IN THIS REPORT

| | <u>Tenure of office</u> | |
|--|-------------------------|-----------|
| | <u>From</u> | <u>To</u> |
| MAYOR (note a): Walter E. Washington | Nov. 1967 | Present |
| DIRECTOR, DEPARTMENT OF GENERAL SERVICES: Sam D. Starobin | June 1970 | Present |
| ASSISTANT DIRECTOR, BUREAU OF MATERIEL MANAGEMENT: Eugene L. Bennett | Dec. 1971 | Present |

a/From Nov. 1967 to Jan. 1, 1975, the title was Commissioner.