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DOD EXCESS PROPERTY: INVENTORY CONTROL BREAKDOWNS PRESENT A SECURITY RISK

HEARING

BEFORE THE

SUBCOMMITTEE ON NATIONAL SECURITY, EMERGING THREATS, AND INTERNATIONAL RELATIONS

OF THE

COMMITTEE ON GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED NINTH CONGRESS

SECOND SESSION

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CONTENTS

	Page
Hearing held on July 25, 2006	1
Statement of:	
Kutz, Gregory D., Managing Director, Forensic Audits and Special Investigations, U.S. Government Accountability Office, accompanied by Gayle L. Fischer, Assistant Director, Forensic Audits and Special Investigations; John J. Ryan, Assistant Director/Special Agent, Forensic Audits and Special Investigations; Richard C. Newbold, Special Agent, Forensic Audits and Special Investigations; Alan F. Estevez, Assistant Deputy Under Secretary of Defense, Supply Chain Integration, Department of Defense; Major General Bennie E. Williams, Director for Logistics Operations, Defense Logistics Agency; and Paul Peters, Director, Defense Reutilization and Marketing Service, Department of Defense	19
Estevez, Alan F.	34
Kutz, Gregory D.	19
Peters, Paul	65
Williams, Bennie E.	48
Letters, statements, etc., submitted for the record by:	
Estevez, Alan F., Assistant Deputy Under Secretary of Defense, Supply Chain Integration, Department of Defense, prepared statement of	36
Kutz, Gregory D., Managing Director, Forensic Audits and Special Investigations, U.S. Government Accountability Office, prepared statement of	21
Ryan, John J., Assistant Director/Special Agent, Forensic Audits and Special Investigations, followup questions and responses	95
Shays, Hon. Christopher, a Representative in Congress from the State of California:	
Comments from the Department of Defense	109
Prepared statement of	3
Waxman, Hon. Henry A., a Representative in Congress from the State of California, prepared statement of	10
Williams, Major General Bennie E., Director for Logistics Operations, Defense Logistics Agency:	
Followup questions and reponses	92
Prepared statement of	50

DOD EXCESS PROPERTY: INVENTORY CONTROL BREAKDOWNS PRESENT A SECURITY RISK

TUESDAY, JULY 25, 2006

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON NATIONAL SECURITY, EMERGING THREATS, AND INTERNATIONAL RELATIONS,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 2 p.m. in room 2154, Rayburn House Office Building, Hon. Christopher Shays (chairman of the subcommittee) presiding.

Present: Representatives Shays, Kucinich, Waxman, Duncan, Marchant, Turner, Van Hollen, and Platts.

Staff present: J. Vincent Chase, chief investigator; R. Nicholas Palarino, Ph.D., staff director; Robert A. Briggs, analyst; Robert Kelley, chief counsel; Raj Lalla, Jake Parker, and Jeff Hall, interns; Karen Lightfoot, minority communications director/senior policy advisor; Jeff Baran, minority counsel; Andrew Su, minority professional staff member; Earley Green, minority chief clerk; and Jean Gosa, minority assistant clerk.

Mr. SHAYS. A quorum being present, the Subcommittee on National Security, Emerging Threats, and International Relations hearing entitled, "DOD Excess Property: Inventory Control Breakdowns Present a Security Risk," is called to order.

Over the course of several hearings and related investigations, our subcommittee found chronic, dangerous, and excessive problems in the Department of Defense excess property system run by the Defense Logistics Agency, DLA. We continued to discover problems in the system, and they must be corrected.

The mission of DLA is to provide our war fighters what they need to fight our enemies. Unfortunately, the Defense Logistics Agency may be simultaneously supplying the terrorists what they need to fight us.

Four years ago we discovered DOD had been selling top-grade chemical protective suits to the public while military units were waiting in line to acquire exactly the same gear. In 2003 we revealed DOD sold items on the internet that could be used to make a biological warfare agent laboratory. This equipment was sold for pennies on the dollar, making it both inexpensive and easy to buy.

At a June 2005 subcommittee hearing we learned DOD was transferring, donating, or selling excess property in new or good condition at the same time it was purchasing the same or similar

equipment. At that hearing, DOD asserted that offensive, defensive, and highly sensitive equipment could not be bought privately.

So we asked the Government Accountability Office, GAO, to investigate whether DOD was right. Posing as private citizens, GAO purchased sensitive military equipment from the DOD liquidation contractor.

Some of the equipment GAO inventories bought or obtained for free is here today. A time selector unit used to assure the accuracy of global positioning systems: the original acquisition price for this unserviceable but repairable item was $343,695; GAO bought the unit for $65. Two guided missile launcher mounts which provide the electrical connection between a missile and its tracker and contain a remote firing mechanism: the original acquisition cost for the two launchers, clearly sensitive military equipment, was $6,246; our investigators acquired them for free. An all-band antenna, which is high-powered, portable unit used by the Air Force to track aircraft: the new, unused antenna had an original cost of $120,000; this, too, was provided for free. Other sensitive equipment obtained by GAO includes body armor, guided weapons, radar test sets used to check the operation of data link antennas on weapons systems, and circuit card assemblies used in a variety of military systems.

Contrary to the claim of DOD made at the June 7, 2005, hearing, this investigation confirms sensitive military equipment is being sold or given to the public, posing a serious national security risk.

The sensitive nature of these items requires stringent internal security controls, and that is not happening. The time is long past for marginal fixes to a fundamentally broken system. This is our fourth hearing. The time is long past for marginal fixes to a fundamentally broken system.

As supplier to the war fighter and steward of immense fiscal resources, DOD must have control over the purchase, transportation, storage, use, and final disposition of the military inventory. Most importantly, DOD must eliminate any opportunities for unauthorized purchase of sensitive military equipment.

Today we welcome representatives from the Government Accountability Office who conducted the investigation, the Department of Defense officials who will explain the corrective action to prevent sensitive items from being sold or given to unauthorized individuals. We thank all the witnesses for taking the time to appear before us today, and we hope that we have an informative hearing.

I want to say before I recognize Mr. Kucinich the purpose of this hearing is not "I got you." The purpose of this hearing is to document what is happening and to get it stopped.

[The prepared statement of Hon. Christopher Shays follows:]

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Statement of Rep. Christopher Shays
July 25, 2006

Over the course of several hearings and related investigations, our Subcommittee found chronic, dangerous and excessive problems in the Department of Defense (DoD) excess property system run by the Defense Logistics Agency (DLA). We continue to discover problems in this system and they must be corrected.

The mission of DLA is to provide our warfighters what they need to fight our enemies. Unfortunately, the Defense Logistics Agency may be simultaneously supplying the terrorists what they need to fight us.

Four years ago, we discovered DoD had been selling top-grade chemical protective suits to the public while military units were waiting in line to acquire exactly the same gear.

In 2003, we revealed DoD sold items on the Internet that could be used to make a biological warfare agent laboratory. This equipment was sold for pennies on the dollar, making it both inexpensive and easy to buy. At a June 2005 Subcommittee hearing, we learned DoD was transferring, donating or selling excess property in new or good condition at the same time it was purchasing the same or similar equipment.

At that hearing, DoD asserted that offensive, defensive and highly sensitive equipment "could not be bought privately." We asked the Government Accountability Office (GAO) to investigate whether DoD was right. Posing as private citizens, GAO purchased sensitive military equipment from the DoD liquidation contractor.

Some of the equipment GAO investigators bought or obtained for free is here today:

- A *Time Selector Unit* used to assure the accuracy of global positioning systems. The original acquisition price for this unserviceable, but reparable item was $343,695. GAO bought the unit for $65.

- Two *Guided Missile Launcher Mounts* which provide the electrical connection between a missile and its tracker and contain a remote firing mechanism. The original acquisition cost for the two launchers (clearly sensitive military equipment) was $6246. Our investigators acquired them for free.

- An *All-Band Antenna* which is a high-powered portable unit used by the Air Force to track aircraft. The new, unused antenna had an original cost of $120,000. This too was provided for free.

- Other sensitive equipment obtained by GAO include *body armor, guided weapons radar test sets* used to check the operation of data link antennas on weapons systems and *circuit card assemblies* used in a variety of military systems.

Contrary to the claim of DoD, made at the June 7, 2005 hearing, this investigation confirms sensitive military equipment is being sold or given to the public, posing a serious national security risk. The sensitive nature of these items requires stringent internal security controls, and that is not happening.

The time is long past for marginal fixes to a fundamentally broken system. As supplier to the warfighter, and steward of immense fiscal resources, DoD must have control over the purchase, transportation, storage, use and final disposition of the military inventory. Most importantly, DoD must eliminate any opportunities for unauthorized purchase of sensitive military equipment.

Today we welcome representatives from the Government Accountability Office who conducted the investigation, and Department of Defense officials who will explain the corrective action to prevent sensitive items from being sold or given to unauthorized individuals.

We thank all the witnesses for taking the time to appear before us today.

Mr. SHAYS. Mr. Kucinich.

Mr. KUCINICH. Thank you very much, Mr. Chairman.

At last June's hearing the GAO informed us that some $400 million worth of A-condition goods, new or excellent condition commodities, were transferred, donated, sold, or destroyed by the Department of Defense in the previous 3 years instead of being re-utilized by other military units who needed the items. Whether it was given away for free, bought for pennies on the dollars, or sold on the internet, the Pentagon has demonstrated time and time again that it plays fast and loose with the American taxpayers' dollar. There is little or no accountability, and Secretary Rumsfeld simply has not made financial accountability a very high priority for the Department of Defense, yet the Pentagon continues to ask Congress for billions of dollars in supplemental and bridge funding for military operations.

The amount of waste is extraordinary, and the millions of dollars that are gone could have been put to better use elsewhere. Certainly, an extra $400 million in the Nation's coffers could help prevent many of the economic difficulties faced by people in my own District.

Department of Defense officials under oath told us fixes would be made by the beginning of the year and assured the subcommittee that the GAO only was able to purchase and obtain excess equipment because they were the GAO. Today we will learn just how easy it was to obtain sensitive military equipment. The cost of a new gas engine, $355; the cost of an X-ray enclosure, $2,914; an ounce of common sense at the Department of Defense equipment depots, priceless.

Whatever it is you need, they have in stock—guided missile launcher mounts, body armor, or electric radar—all for less than you would pay if you were actually authorized to use them. In fact, DOD personnel may even help you load your brand new toys into your own truck.

Mr. Chairman, the lack of security and lack of accountability is appalling, yet it is unsurprising in this administration. In May, VA officials lost a laptop containing tens of millions of sensitive personnel records. The VA Inspector General stated that VA officials reacted with indifference, a lack of urgency. That same attitude appears to be the case in the Department of Defense.

The subcommittee has heard for years of the extravagant waste and abuse discovered at DLA and DRMS depot sites examined by the Government Accountability Office, and even more so at how easily GAO was able to obtain some of this A-condition merchandise. The GAO findings demonstrate again what we already know: that the Department of Defense is bloated, it is inefficient, mismanaged, and it needs to be streamlined.

Finally, year after year Congress spends half of its discretionary budget on Defense, seldom scrutinizing how the money is being spent. As a result, the Pentagon has become sloppy and careless with taxpayer dollars.

Thank you, Mr. Chairman.

Mr. SHAYS. I thank the gentleman.

At this time we are doing to recognize Mr. Duncan, because he has to get on his way.

Mr. DUNCAN. Thank you very much, Mr. Chairman. I have to go give a speech to a group in a few minutes, but I do appreciate so much your calling this hearing. You do such an outstanding job in this subcommittee.

I was here a little over a year ago when we had a similar hearing, and at that time—and I wrote about part of this in a newsletter I sent to my constituents—the Department of Defense sold 172 pairs of brand new cold weather boots valued collectively at more than $23,330 for just $69, not $69 for each pair of boots, $69 total, brand new boots. That is less than the cost of one pair of shoes that they bought for $23,330. The GAO also found at that time that the Department of Defense had purchased at least $400 million of identical items, instead of using materials that were already available.

Now, according to the latest report, we find out that this situation is not getting better. In fact, it is getting worse. As the chairman mentioned, we were just shown a $120,000 all-band antenna that the GAO got for nothing by filing a bogus form, and a digital signal converter, $800,000, that they got for nothing. In fact, the GAO, according to this report, identified at least 79 buyers of 2,669 sensitive items just between November 2005 and June 2006. And you have heard these other examples that the chairman and Mr. Kucinich just mentioned.

The worst one is this purchase of these time selector units for $65, a unit that had an original acquisition cost of $343,000. And the unit purchased, according to the GAO, was listed as unserviceable, but it was in good working order.

Now, we have, as we all want, we have the best fit, best paid, best equipped troops, military, in the whole world. Counting our supplemental appropriations and our military construction bills, along with the regular Department of Defense budget, we are spending more on Defense than all the other nations of the world combined. Yet, even any bureaucracy is wasteful. Small ones are wasteful. Large ones are wasteful. Gigantic bureaucracies such as the Department of Defense seem to be the most wasteful of all.

We all want to support the military, especially in a time of war. Everybody is bending over backward to try and prove how patriotic they are, but I can tell you this: it is not patriotic to just blow money in this way. In fact, it should be criminal.

And I can tell you this: anybody who is not horrified—we heard Mr. Kucinich mention that there is indifference or even joking about this report—anybody who is not horrified about this cannot legitimately call themselves a fiscal conservative, and everybody seems to like to claim that title. We need more fiscal conservativism. But this is shameful, it is ridiculous, it is every bad adjective that you can apply to allow this to continue.

I hope that at least somebody in the Department of Defense is ashamed that this is happening.

Thank you, Mr. Chairman.

Mr. SHAYS. I thank the gentleman.

I now recognize the ranking member of the full committee, Mr. Waxman.

Mr. WAXMAN. Thank you, Mr. Chairman, and thank you for holding today's important hearing.

Last year in this same room we held a hearing on this very topic and we heard from the Government Accountability Office an account of massive waste at the Department of Defense. A year ago GAO told the subcommittee that over $3 billion worth of A-condition equipment was designated as excess by the Defense Department and simply given away, sold on the internet for pennies on the dollar.

Even worse, GAO reported that a huge portion of this equipment was being dumped at fire sale prices at the same time the Pentagon was buying identical equipment from contractors at full price.

Two years ago our subcommittee held another hearing. We learned from GAO that the Defense Department sold equipment on the internet that could be used to produce anthrax, and yet at another hearing GAO told the subcommittee that the Defense Department sold brand new chem-bio protective suits on the internet for $3 each, while it was buying identical suits at the same time for the full price of $200 apiece.

Each time we have these hearings GAO brings the proof. They display the equipment, as they have again today, they purchased on the tables of the hearing room. And each time the Defense Department officials come before the subcommittee and promise that the administration will be a responsible steward of taxpayer dollars and that these problems will be fixed. Yet here we are again in 2006. The problems have not been fixed. They have gotten worse.

Here are four key findings from GAO's most recent investigation:

First, the Defense Department is needlessly selling equipment as excess that it currently buys new. GAO found X-ray machines, gasoline generators, and a host of other equipment for sale on the internet, even though the Pentagon was still buying these items new.

Second, the Pentagon is practically giving away. For just $65, GAO obtained a classified time selector technology unit which is used to prevent soldiers in the field from exposing their positions. The taxpayers pay not $65 but over $340,000 for this equipment.

Third, much of this equipment is in critical demand by our soldiers in Iraq and Afghanistan. The body armor components, in particular, are items that families of service members have been forced to purchase and send to loved ones in Iraq.

Fourth, many of these items are classified national security items that were never supposed to be sold to the public, including micro circuits for F–14 fighter planes, high-powered portable antenna units that track aircraft, and even shoulder-fired guided missile launcher mounts.

As a result, GAO concludes that controls broke down at virtually every step, that thousands of military items were inappropriately sold to the public at a fraction of the original cost, demonstrating continuing waste and inefficiency and posing a national security risk.

Mr. Chairman, Einstein once said that insanity is doing the same thing over and over again expecting a different result. Einstein was right, and let me give you Waxman's corollary: when there is no accountability, insanity is rewarded and repeated.

In last year's hearing, Mr. Chairman, you said, "Those who buy too much this year have to know they will pay a price when the

equipment for sale on the internet next year for one-tenth of the acquisition cost." But here we go again. It is next year and the Defense Department is not paying any price for its incompetence. It is the American taxpayer who is paying the price and our service members in Iraq that don't have the critical equipment they need.

Mr. Chairman, our Nation needs a new direction. The Bush administration is treating the taxpayers like its own private piggy bank and Congress is doing nothing to stop it.

[The prepared statement of Hon. Henry A. Waxman follows:]

Opening Statement of
Rep. Henry A. Waxman, Ranking Minority Member
Committee on Government Reform
Before the Subcommittee on National Security, Emerging Threats and International Relations
Hearing on Defense Department Excess Property

July 25, 2006

Thank you, Mr. Chairman. And thank you for holding today's important hearing.

Last year, in this same room, we held a hearing on this very topic. And what we heard was GAO's account of massive waste at the Department of Defense.

A year ago, GAO told the Committee that over $3 billion worth of "A Condition" equipment was designated as "excess" by the Defense Department and simply "given away," sold on the Internet for pennies on the dollar.

Even worse, GAO reported that a huge portion of this equipment was being dumped at fire-sale prices at the same time the Pentagon was buying identical equipment from contractors at full price.

Two years ago, our Committee held another hearing. We learned from GAO that the Defense Department sold equipment on the Internet that could be used to produce anthrax.

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Each time we have these hearings, GAO brings the proof. They display the equipment they purchased on these tables in the hearing room. And each time, Defense Department officials come before the Committee and promise that the Administration will be a responsible steward of taxpayer dollars and that these problems will be fixed.

Yet … here we are again … in 2006. The problems haven't been fixed. They've gotten worse.

Here are four key findings from GAO's most recent investigation:

- First, the Defense Department is needlessly selling equipment as "excess" that it currently buys new. GAO found X-ray machines, gasoline generators, and a host of

other equipment for sale on the Internet even though the Pentagon was still buying these items new.

- Second, the Pentagon is practically giving this valuable equipment away. For just $65, GAO obtained a classified time selector technology unit, which is used to prevent soldiers in the field from exposing their positions. The taxpayers paid over $340,000 for this equipment.

- Third, much of this equipment is in critical demand by our soldiers in Iraq and Afghanistan. The body armor components, in particular, are items that families of service members have been forced to purchase and send to loved ones in Iraq.

- And fourth, many of these items are classified national security items that were never supposed to be sold to the public, including microcircuits for F-14 fighter planes, high-powered portable antenna units that track aircraft, and even shoulder-fired guided missile launcher mounts.

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At last year's hearing, you said: "Those who buy too much this year have to know they will pay a price when the equipment appears for sale on the Internet next year for one-tenth the acquisition cost."

But here we are again – it's next year – and the Defense Department is not paying any price for its incompetence. It's the American taxpayer who is paying the price, and our service members in Iraq that don't have the critical equipment they need.

Mr. Chairman, our nation needs a new direction. The Bush Administration is treating the taxpayer like its own private piggy bank, and Congress is doing nothing to stop it.

Mr. SHAYS. The Chair would recognize Mr. Marchant, the Vice chairman.

Mr. MARCHANT. Thank you, Mr. Shays, for holding this hearing today on this very important subject. What the Department of Defense does with its excess inventory is probably not something that enters the public's mind; however, the fact that the Defense Logistics Agency is responsible for the management of the inventory of $89 billion requires reasonable oversight by the Congress.

In addition, when you think about the types of property the DOD possesses, such as tanks, aircraft, weapons components, etc., it becomes clear that much of this inventory is extremely sensitive in nature. Furthermore, even when we are not talking about sensitive, classified, or dangerous items, it is our duty as stewards to make sure that this excess property is being properly managed.

Obviously, our No. 1 goal should be to make sure that our troops are well supplied. The next goal should be to keep dangerous or sensitive excess items from falling into the wrong hands. Last, excess inventories should be managed in a most efficient and cost efficient manner as possible.

Again, Chairman Shays, I am looking forward to testimony today. Thank you.

Mr. SHAYS. I thank the gentleman.

Mr. Turner, you have the floor.

Mr. TURNER. Thank you, Mr. Chairman. I want to thank you for holding this hearing today and I want to echo the comments of Mr. Duncan concerning the amount of waste that we see as a result of these studies.

Mr. Chairman, you have been a leader in stopping Government waste, and also the issues of national security. This is the third in a series of hearings that our chairman has held on this issue highlighting the lack of controls by the Defense Logistics Agency in dealing with excess property. As GAO pointed out, they were able to purchase numerous items that are sensitive in nature. The work done by GAO was done over a short period of time, so we don't actually know the full extent of the problem. GAO also did not address the issue of the types of people or groups that are purchasing these items.

Although it apparently states on the govliquidation.com Web site that foreign nationals are prohibited from purchasing demilitarized equipment, we do not actually know if or how they are prevented. I believe this would be an excellent topic for the GAO to examine, and I congratulate our subcommittee chairman on his continuing focus in addressing this issue.

Thank you, Mr. Chairman.

Mr. SHAYS. I thank the gentleman.

Before recognizing witnesses I want to read from the June 7, 2005, hearing that we had on this very issue. At one point I was asking Colonel O'Donnell, who was testifying, "Is it your statement the only way GAO was to buy this restrictive property is because they were GAO and that they would not have been able to buy it if they had tried to buy it privately?" Colonel O'Donnell, "That's correct, sir. These items up on the podium, they are requisitioned through DRMS using a DUDAC that had been assigned a Depart-

ment of Defense activity address code that had been assigned to GAO enabling them to acquire property from us."

For us that statement was like Gary Hart telling the press, "I am doing nothing wrong. Come follow us."

What I find objectionable about the last hearing was the fact that I don't think DOD took that hearing seriously enough. This is not an attempt to get you, but it is an attempt to get you to wake up.

With that, I would like to announce our panel. It is Mr. Gregory D. Kutz, Managing Director, Forensic Audits and Special Investigations, U.S. Government Accountability Office; accompanied by Ms. Gayle L. Fischer, Assistant Director; Mr. John J. Ryan, Assistant Director/Special Agent; Mr. Richard C. Newbold, Special Agent. The last three I mentioned will be here to respond to questions but not to give testimony. We then have Mr. Alan F. Estevez, Assistant Deputy Under Secretary of Defense, Supply Chain Integration, Department of Defense; General Bennie E. Williams, Director for Logistics Operations, Defense Logistics Agency; Mr. Paul Peters, Director, Defense Reutilization and Marketing Service, Department of Defense.

Would you please stand and we will swear you in.

[Witnesses sworn.]

Mr. SHAYS. Note for the record all our witnesses have responded in the affirmative. Those on the second right of way to testify, we will make sure that the names get in and we know who is testifying.

I would like at this time to take care of business. I ask unanimous consent that all members of the subcommittee be permitted to place an opening statement in the record and that the record remain open for 3 days for that purpose. Without objection, so ordered.

I ask further unanimous consent that all witnesses be permitted to include their written statement in the record. Without objection, so ordered.

I will just make mention of the fact we could have had two panels. I am not looking for arguments among panel members. I don't think that is really what anyone is looking for. But I do want to be able to go back to GAO if there is a claim that something took place that had nullified the significance of GAO. For instance, I am sure we will have a dialog about the protective gear and that is not the most up-to-date protective gear. We might have a dialog about whether something is repairable or not. But I think what you see in front of us speaks for itself. It is pretty astonishing.

We will start with you, Mr. Kutz.

STATEMENTS OF GREGORY D. KUTZ, MANAGING DIRECTOR, FORENSIC AUDITS AND SPECIAL INVESTIGATIONS, U.S. GOVERNMENT ACCOUNTABILITY OFFICE, ACCOMPANIED BY GAYLE L. FISCHER, ASSISTANT DIRECTOR, FORENSIC AUDITS AND SPECIAL INVESTIGATIONS; JOHN J. RYAN, ASSISTANT DIRECTOR/SPECIAL AGENT, FORENSIC AUDITS AND SPECIAL INVESTIGATIONS; RICHARD C. NEWBOLD, SPECIAL AGENT, FORENSIC AUDITS AND SPECIAL INVESTIGATIONS; ALAN F. ESTEVEZ, ASSISTANT DEPUTY UNDER SECRETARY OF DEFENSE, SUPPLY CHAIN INTEGRATION, DEPARTMENT OF DEFENSE; MAJOR GENERAL BENNIE E. WILLIAMS, DIRECTOR FOR LOGISTICS OPERATIONS, DEFENSE LOGISTICS AGENCY; AND PAUL PETERS, DIRECTOR, DEFENSE REUTILIZATION AND MARKETING SERVICE, DEPARTMENT OF DEFENSE

STATEMENT OF GREGORY D. KUTZ

Mr. KUTZ. Mr. Chairman and members of the subcommittee, thank you for the opportunity to discuss DOD excess property.

Previously we testified that DOD was selling new, unused chem-bio suits needed in Iraq, equipment that could be used to produce anthrax, and new, unused items that were still in demand by the military services for pennies on the dollar. You asked us to test progress made in the excess property system using undercover operations. The bottom line of my testimony today is that we were able to obtain sensitive military items on the internet and using social engineering. Further, we were able to purchase unused items that were still in demand by the military services.

My testimony has two parts: first, sensitive military items and, second, examples of waste.

First, posing as a private citizen we purchased sensitive military equipment on the internet. Some of these items required us to obtain an end use certificate, which is intended to provide assurance that property is sold to legitimate buyers. We prepared an application for the certificate using bogus information. Subsequently, a DOD official called to ask us about our applicant and why they had no credit or other history. We socially engineered the situation, provided a bogus utility bill, and our application was approved. We used the certificate to purchase several of our items.

Let me discuss several of these purchase, which are on my left and will also be shown on the monitors.

First, we purchased 12 micro circuits for use on the F–14 fighter aircraft. As I will discuss, these are of particular concern to law enforcement officials. This lot also had two guided weapon radar test sets related to the FA–18 Hornet. We used our bogus end use certificate to obtain these items. And we purchased three ceramic body armor inserts currently used in Iraq and Afghanistan.

As was mentioned, in addition to the items we bought, we identified at least 79 other buyers that purchased over 2,600 sensitive military items. Some of these buyers outbid us on lots that we had targeted for purchase.

We also obtained at no cost $1.1 million of sensitive military equipment by posing as DOD contractor employees. Specifically, we used publicly available information and developed fictitious identi-

ties as contractor personnel. We then entered two DOD warehouses in June 2006 seeking excess property. DOD and contractor staff helped our investigators find targeted items and they helped us load them into our rented van.

Let me discuss a few of these items which are on my left center here and will also be shown on the monitor.

First, we obtained two guided missile mounts which fire dragon anti-tank missiles, six kevlar body armor fragmentation vests, an all-band antenna used by the Air Force to track aircraft, and 10 older-version body armor vests.

Although many of the items you see on my left are not DOD's latest, all of them are of concern. For example, Homeland Security and Defense investigators met with us several weeks ago and informed us that they are spending considerable resources chasing after items that are getting out of DOD. They are particularly concerned about aircraft parts such as the F–14 parts that we obtained, and they told us that these parts are being resold to Iran.

Also, another question: should DOD be selling military quality body armor on the internet to the highest bidder?

My second point is that we were able to purchase new and unused items that DOD is continuing to buy or that are in demand by the military services. As we have previously reported, we believe that this is a waste of taxpayer resources.

Let me discuss a few of these items, which are on my right and will also be shown on the monitor.

First, 10 wet weather parkas. We paid $87, DOD paid $359. Then we have 10 cold weather parkas. We paid $373, DOD paid $1,400. The next item is a portable field X-ray processing enclosure. We paid $87, DOD paid over $7,000. Finally, we purchased 20 locks that are used to secure the back bay of trucks. We paid $59, DOD paid $1,600.

DOD has made some progress in this area. Specifically, DOD initiatives have saved a reported $38 million through June 2006.

In conclusion, the most troubling aspect of our investigation is the sale of sensitive military equipment to the public. In addition to national security issues, sales of items like body armor to the public pose homeland security risks.

With respect to waste, we are encouraged that DOD initiatives have saved a represented $38 million. We see the potential for several hundred million more of savings.

Mr. Chairman, this ends my statement. We look forward to your questions.

[NOTE.—The GAO report entitled, "DOD Excess Property, Control Breakdowns Present Significant Security Risk and Continuing Waste and Inefficiency," may be found in subcommittee files.]

[The prepared statement of Mr. Kutz follows:]

United States Government Accountability Office

GAO

Testimony

Before the Subcommittee on National Security, Emerging Threats and International Relations, Committee on Government Reform, House of Representatives

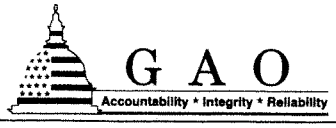
For Release on Delivery
Expected at 2:00 p.m. EDT
Tuesday, July 25, 2006

DOD EXCESS PROPERTY

Control Breakdowns Present Significant Security Risk and Continuing Waste and Inefficiency

Statement of Gregory D. Kutz, Managing Director
Forensic Audits and Special Investigations

John P. Ryan, Assistant Director
Forensic Audits and Special Investigations



GAO-06-981T

July 25, 2006

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Highlights

Highlights of GAO-06-981T, testimony before the Subcommittee on National Security, Emerging Threats and International Relations, Committee on Government Reform, House of Representatives

DOD EXCESS PROPERTY

Control Breakdowns Present Significant Security Risk and Continuing Waste and Inefficiency

Why GAO Did This Study

In light of GAO's past three testimonies and two reports on problems with controls over excess DOD property, GAO was asked to perform follow-up investigations to determine if (1) unauthorized parties could obtain sensitive excess military equipment that requires demilitarization (destruction) when no longer needed by DOD and (2) system and process improvements are adequate to prevent sales of new, unused excess items that DOD continues to buy or that are in demand by the military services.

What GAO Recommends

GAO briefed DOD management on the results of its follow-up investigation and provided additional perspectives on ways to resolve the control breakdowns that resulted in public sales of sensitive excess military equipment and new, unused excess items that the military services continue to use. In its comments on GAO's draft report, DOD stated that given the time allotted to comment, the department was not able to do a detailed review and has no comments at this time. DOD also commented that it continues to implement changes to procedures based on GAO's May 2005 report (GAO-05-277).

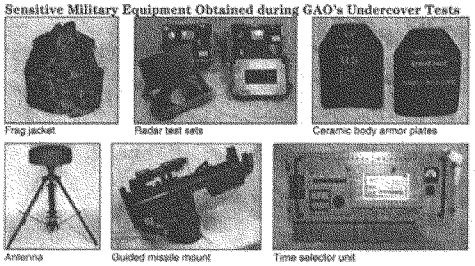
www.gao.gov/cgi-bin/getrpt?GAO-06-981T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Gregory D. Kutz at (202) 512-7455 or kutzg@gao.gov.

What GAO Found

GAO investigators posing as private citizens purchased several sensitive military equipment items from DOD's liquidation sales contractor, indicating that DOD has not enforced security controls for preventing sensitive excess military equipment from release to the public. GAO investigators at liquidation sales purchased ceramic body armor inserts currently used by deployed troops, a cesium technology timing unit with global positioning capabilities, a universal frequency counter, two guided missile radar test sets, 12 digital microcircuits used in F-14 fighter aircraft, and numerous other items. GAO was able to purchase these items because controls broke down at virtually every step in the excess property turn-in and disposal process. GAO determined that thousands of military items that should have been demilitarized (destroyed) were sold to the public. Further, in June 2006, GAO undercover investigators posing as DOD contractor employees entered two excess property warehouses and obtained about $1.1 million in sensitive military equipment items, including two launcher mounts for shoulder-fired guided missiles, several types of body armor, a digital signal converter used in naval surveillance, an all-band antenna used to track aircraft, and six circuit cards used in computerized Navy systems. At no point during GAO's warehouse security penetration were its investigators challenged on their identity and authority to obtain DOD military property. The table below shows examples of sensitive military equipment obtained during GAO's undercover operations.

Sensitive Military Equipment Obtained during GAO's Undercover Tests



Frag jacket | Radar test sets | Ceramic body armor plates

Antenna | Guided missile mount | Time selector unit

Source: GAO, Moog Corporation for antenna.

GAO investigators posing as private citizens also bought several new, unused items currently being purchased or in demand by the military services from DOD's excess property liquidation sales contractor. Although military units paid full price for these items when they ordered them from supply inventory, GAO paid a fraction of this cost to purchase the same items, demonstrating continuing waste and inefficiency.

Mr. Chairman and Members of the Subcommittee:

Thank you for the opportunity to discuss our recent investigation of Department of Defense (DOD) excess property controls. This testimony is the fourth in a series of testimonies and reports to this Subcommittee,[1] detailing serious breakdowns in management processes, systems, and controls that have resulted in lost and missing property and substantial waste and inefficiency in DOD's excess property reutilization program. Our June 2002 testimony and our November 2003 report documented instances where DOD sold to the public items such as Joint Service Lightweight Integrated Suit Technology (JSLIST)[2] and other chemical and biological protective suits and related gear that should have been restricted to DOD-use only. Our November 2003 report also identified several examples to show that at the same time DOD excessed biological equipment items in good or excellent condition and sold many of them to the public for pennies on the dollar, it was purchasing the same or similar items. Our May 2005 report stated that DOD reported $466 million in lost, damaged, and missing excess property from fiscal years 2002 through 2004, including property with demilitarization restrictions,[3] such as chemical and biological protective suits, body armor, and guided missile warheads. Some of the missing restricted items had been improperly sold to the public. Further, our May 2005 report noted that during fiscal years 2002 and 2003, the military services needlessly spent at least $400 million to purchase new items instead of reusing identical excess items in new and unused condition (A-condition). As a result, the new, unused excess items were sold for pennies on the dollar while the military services paid

[1] GAO, *DOD Excess Property: Management Control Breakdowns Result in Substantial Waste and Inefficiency*, GAO-05-277 (Washington, D.C.: May 13, 2005) and GAO-05-723T (Washington, D.C.: June 8, 2005); *DOD Excess Property: Risk Assessment Needed on Public Sales of Equipment That Could Be Used to Make Biological Agents*, GAO-04-81TNI (Washington, D.C.: Oct. 7, 2003) and GAO-04-15NI (Washington, D.C.: Nov. 19, 2003); and *DOD Management: Examples of Inefficient and Ineffective Business Processes*, GAO-02-873T (Washington, D.C.: June 25, 2002).

[2] JSLIST is a universal, lightweight, two-piece garment (coat and trousers) that when combined with footwear, gloves, and a protective mask and breathing device, forms the warfighter's protective ensemble. The ensemble is to provide maximum protection to the warfighter against chemical and biological contaminants without negatively affecting the ability to perform mission tasks. JSLIST is the current model protective suit used by the military services.

[3] DOD-4160.21-M-1, *Defense Demilitarization Manual* (1995), contains DOD policy related to controls over items with significant military technology application.

the full acquisition price to order these items from Defense Logistics Agency (DLA) supply depots.

Our recent investigative tests of controls over sensitive excess military equipment and technology items that require demilitarization focused on determining whether (1) DOD was improperly selling these items to the public[4] and (2) excess property warehouse facilities had adequate security to prevent unauthorized parties from obtaining excess military items with demilitarization restrictions. Our investigative tests of controls for preventing liquidation sales of new, unused excess items that DOD is continuing to buy or that are in demand by the military services focused on whether these items were continuing to be sold to the public. We used publicly available information to develop undercover identities and techniques used in our investigations. We conducted our investigations from November 2005 through June 2006 in accordance with quality standards for investigators as set forth by the President's Council on Integrity and Efficiency.

Today, we will summarize the results of our recent work with respect to whether (1) unauthorized parties could obtain sensitive excess military equipment that requires demilitarization when no longer needed by DOD and (2) systems and process improvements are adequate to prevent liquidation sales of A-condition items that DOD is continuing to buy or that are in demand by the military services. In addition, we will highlight the status of DOD corrective actions on the recommendations in our May 2005 report. The details of our work are included in our investigative report, which the Subcommittee is releasing today.[5]

Summary

Posing as private citizens to disguise our identity, our investigators identified and purchased numerous sensitive excess DOD military technology items that should have been demilitarized instead of being sold to the public. Sensitive excess military equipment we purchased at DOD excess property liquidation sales auctions included ceramic body armor

[4] In concert with the federal government's E-government policy to use information technology (IT) investments to deliver services and information to citizens electronically, DOD's excess property liquidation sales are conducted over the Internet. OMB, *Implementation Guidance for the E-Government Act of 2002*, M-03-18, at att. A, ¶ B, 1 (Aug. 1, 2003).

[5] GAO, *DOD Excess Property: Control Breakdowns Present Significant Security Risk and Continuing Waste and Inefficiency*, GAO-06-943 (Washington, D.C.: July 25, 2006).

inserts currently used by deployed troops, a time selector unit used to ensure the accuracy of computer-based equipment, such as global positioning systems and system-level clocks, a universal frequency counter used to ensure that the frequency of communication gear is running at the expected rate, two guided missile radar test sets, at least 12 digital microcircuits used in F-14 *Tomcat* fighter aircraft, and numerous other sensitive electronic parts. We were able to purchase these items because controls broke down at virtually every step in the excess property turn-in and disposal process. Also, in instances where DOD required an End-Use Certificate (EUC)[6] as a condition of sale, our undercover investigator was able to successfully defeat the screening process by submitting bogus documentation and providing plausible explanations for discrepancies in his documentation.

In addition, posing as DOD contractor employees[7] our undercover investigators were able to easily penetrate security at two separate locations in June 2006 and obtain at no cost directly from excess inventory warehouses, numerous sensitive military equipment items valued at about $1.1 million that should not have been released outside of DOD. The items we obtained included two launcher mounts for shoulder-fired guided missiles, several types of body armor, a digital signal converter used in naval electronic surveillance, an all-band antenna used to track aircraft, six circuit cards used in computerized Navy systems, and several other items in use by the military services. The body armor could be used in terrorist or other criminal activity. Many of the other military items have weapons applications that also would be useful to terrorists. Our undercover investigators were able to obtain these items because Defense Reutilization and Marketing Office (DRMO)[8] personnel did not confirm their identity and authorization to requisition excess DOD property items. The DRMO personnel even helped our undercover investigators load the items into our van.

[6] An EUC is a form used by DOD to document the intended destination and disposition of sensitive, controlled items released from the department.

[7] Under DOD's excess property reutilization program, DOD contractors are treated the same as DOD units and are not charged for excess property items they requisition for reuse.

[8] DRMOs are excess property warehouses operated by the Defense Reutilization and Marketing Service (DRMS), which is the agency within DLA charged with managing DOD's excess property disposal system.

We also made several undercover purchases of new, unused A-condition excess DOD items, including wet-weather parkas, cold-weather desert camouflage parkas, a portable field x-ray processing enclosure, high-security locks used to secure the back bay of logistics trucks, a gasoline engine, and a refrigerant recovery system used for servicing automotive vehicles. The items we purchased at DOD liquidation sales were being ordered from supply inventory by military units at or near the time of our purchases and for one supply depot stocked item—the portable x-ray enclosure—no items were in stock when we made our purchase. At the time of our purchase, DOD's liquidation contractor sold 40 of these x-ray enclosures with a total reported acquisition cost of $289,400 for a liquidation sales price of $2,914—about a penny on the dollar. In another example, we purchased a gasoline engine in March 2006 for $355. The Marine Corps ordered 4 of these gas engines from DLA supply inventory in June 2006 and paid $3,119 each for them. At the time of our undercover purchase, 20 identical gasoline engines with a reported acquisition cost of $62,380 were sold to the public for a total liquidation sales price of $6,221. Our investigation demonstrated that the problems we reported on in May 2005 have not been fully resolved and there is continuing waste and inefficiency in DOD's excess property reutilization program.

We provided a detailed corrective action briefing to DOD on June 28, 2006. DOD managers told us they shared our concern about the breakdowns in security controls that allowed sensitive military items requiring demilitarization to be sold to the public. They asked us for pertinent documentation obtained during our investigations to support their follow-up inquiries and corrective action plans. We provided this information on June 30, 2006, along with documentation to show that the military services were still ordering and using the excess A-condition items that we purchased. In addition, we provided a draft of our investigative report to DOD for comment on July 10, 2006. In commenting on our draft report, DOD stated that given the time allotted to comment,the department was not able to perform a detailed review and has no comments at this time. DOD also stated that it continues to implement changes to procedures based on our May 2005 report.[9]

[9] GAO-05-277.

Undercover Acquisitions of Sensitive Excess Military Items Identifies National Security Risk

Posing as private citizens, our undercover investigators purchased several sensitive excess military equipment items that were improperly sold to the public at DOD liquidation sales. These items included three ceramic body armor inserts identified as small arms protective inserts (SAPI), which are the ceramic inserts currently in demand by soldiers in Iraq and Afghanistan; a time selector unit used to ensure the accuracy of computer-based equipment, such as global positioning systems and system-level clocks; 12 digital microcircuits used in F-14 *Tomcat* fighter aircraft; guided missile radar test sets used to check the operation of the data link antenna on the Navy's *Walleye* (AGM-62) air-to-ground guided missile; and numerous other electronic items. In instances where DOD required an EUC as a condition of sale, our undercover investigator was able to successfully defeat the screening process by submitting bogus documentation and providing plausible explanations for discrepancies in his documentation. In addition, we identified at least 79 buyers for 216 sales transactions involving 2,669 sensitive military items that DOD's liquidation contractor sold to the public between November 2005 and June 2006. We are referring information on these sales to the appropriate federal law enforcement agencies for further investigation.

Our investigators also posed as DOD contractor employees, entered DRMOs in two east coast states, and obtained several other items that are currently in use by the military services. DRMO personnel even helped us load the items into our van. These items included two launcher mounts for shoulder-fired guided missiles, an all-band antenna used to track aircraft, 16 body armor vests, body armor throat and groin protectors, six circuit card assemblies used in computerized Navy systems, and two Palm V personal data assistant (PDA) organizers.

Sensitive Excess Military Items Purchased at DOD Excess Property Liquidation Sales

Using a fictitious identity as a private citizen, our undercover investigator applied for and received an account with DOD's liquidation sales contractor. Our investigator was then able to purchase several sensitive excess military items noted above that were being improperly sold to the public. During our undercover purchases, our investigator engaged in numerous conversations with liquidation sales contractor staff during warehouse inspections of items advertised for sale and with DRMS and DLA's Criminal Investigative Activity (DCIA) staff during the processing of our EUCs. On one occasion our undercover investigator was told by a DCIA official that information provided on his EUC application had no match to official data and that he had no credit history. Our investigator responded with a plausible story and submitted a bogus utility bill to confirm his mailing address. Following these screening procedures, the

EUC was approved by DCIA and our undercover investigator was able to purchase our targeted excess military items. Once our initial EUC was approved, our subsequent EUC applications were approved based on the information on file. Although the sensitive military items that we purchased had a reported acquisition cost of $461,427, we paid a liquidation sales price of $914 for them—less than a penny on the dollar.

We observed numerous sales of additional excess sensitive military items that were improperly advertised for sale or sold to the public, including fire control components for weapon systems, body armor, and weapon system components. The demilitarization codes for these items required either key point or total destruction rather than disposal through public sale. Although we placed bids to purchase some of these items, we lost to higher bidders. We identified at least 79 buyers for 216 public liquidation sales transactions involving 2,669 sensitive military items. On July 13, 2006, we briefed federal law enforcement and intelligence officials on the details of our investigation. We are referring public sales of sensitive military equipment items to the federal law enforcement agencies for further investigation and recovery of the sensitive military equipment.

During our undercover operations, we also noted 13 advertised sales events, including 179 items that were subject to demilitarization controls, where the items were not sold. In 5 of these sales involving 113 sensitive military parts, it appears that DOD or its liquidation sales contractor caught the error in demilitarization codes and pulled the items from sale. One of these instances involved an F-14 fin panel assembly that we had targeted for an undercover purchase. During our undercover inspection of this item prior to sale, a contractor official told our investigator that the government was in the process of changing demilitarization codes on all F-14 parts and it was likely that the fin panel assembly would be removed from sale. Of the remaining 8 sales lots containing 66 sensitive military parts, we could not determine whether the items were not sold because DOD or its contractor caught the demilitarization coding errors or because minimum bids were not received during the respective sales events.

Sensitive Military Items Obtained through Inside Penetrations of DRMO Security

Our investigators used publicly available information to develop fictitious identities as DOD contractor personnel and enter DRMO warehouses (referred to as DRMO A and DRMO B) in two east coast states on separate occasions in June 2006, to requisition excess sensitive military parts and equipment valued at about $1.1 million. Our investigators were able to search for and identify excess items without supervision. In addition, DRMO personnel assisted our investigators in locating other targeted items in the warehouse and loading these items into our van. At no point

during either visit, did DRMO personnel attempt to verify with the actual contractor that our investigators were, in fact, contractor employees.

During the undercover penetration at DRMO A, our investigators obtained numerous sensitive military items that were required to be destroyed when no longer needed by DOD to prevent them from falling into the wrong hands. These items included two guided missile launcher mounts for shoulder-fired missiles, six Kevlar body armor fragmentation vests, a digital signal converter used in naval electronic surveillance, and an all-band antenna used to track aircraft.

Posing as employees for the same DOD contractor identity used during our June 2006 penetration at DRMO A, our investigators entered DRMO B a day later for the purpose of testing security controls at that location. DRMO officials appeared to be unaware of our security penetration at DRMO A the previous day. During the DRMO B undercover penetration, our investigators obtained 10 older technology body armor fragmentation vests, throat and groin protection armor, six circuit card assemblies used in Navy computerized systems, and two Palm V personal digital assistants (PDA) that were certified as having their hard drives removed. Because PDAs do not have hard drives, after successfully requisitioning them, we asked our Information Technology (IT) security expert to test them and our expert confirmed that all sensitive information had been properly removed.[18]

Shortly after leaving the second DRMO, our investigators received a call from a contractor official whose employees they had impersonated. The official had been monitoring his company's requisitions of excess DOD property and noticed transactions that did not appear to represent activity by his company. He contacted personnel at DRMO A, obtained the phone number on our bogus excess property screening letter, and called us. Upon receiving the call from the contractor official, our lead investigative agent explained that he was with GAO, and we had performed a government test.

[18] Our IT expert used National Institute of Standards and Technology (NIST) utilities recommended for forensic analysis to run the tests. See NIST Pub. 800-72, *Guidelines on PDA Forensics* (November 2004).

Waste Associated with Sales of A-Condition Excess Items that Military Services Are Continuing to Use in Operations

Because significant numbers of new, unused A-condition excess items still being purchased or in use by the military services are being disposed of through liquidation sales, it was easy for our undercover investigator to pose as a liquidation sales customer and purchase several of these items for a fraction of what the military services are paying to obtain these same items from DLA supply depots. For example, we paid $1,146 for several wet-weather and cold-weather parkas, a portable field x-ray enclosure, high-security locks, a gasoline engine that can be used as part of a generator system or as a compressor, and a refrigerant recovery system used to service air conditioning systems on automobiles. The military services would have paid a total acquisition cost of $16,300 for these items if ordered from supply inventory, plus a charge for processing their order.[11]

Several of the items we purchased at liquidation sales events were being ordered from supply inventory by military units at or near the time of our purchase, and for one supply depot stocked item—the portable field x-ray enclosure—no items were in stock at the time we made our undercover purchase. At the time of our purchase, DOD's liquidation contractor sold 40 of these x-ray enclosures with a total reported acquisition cost of $289,400 for a liquidation sales price of $2,914—about a penny on the dollar. We paid a liquidation sales price of $87 for the x-ray enclosure which had a reported acquisition cost of $7,235. In another example, we purchased a gasoline engine in March 2006 for $355. The Marine Corps ordered 4 of these gas engines from DLA supply inventory in June 2006 and paid $3,119 each for them. At the time of our undercover purchase, 20 identical gasoline engines with a reported acquisition cost of $62,380 were sold to the public for a total liquidation sales price of $6,221, also about a penny on the dollar.

Status of DOD Corrective Actions

In response to recommendations in our May 2005 report,[12] DOD has taken a number of actions to improve systems, processes, and controls over excess property. Most of these efforts have focused on improving the economy and efficiency of DOD's excess property reutilization program. However, as demonstrated by our tests of security controls over sensitive excess military equipment, DOD does not yet have effective controls in place to prevent unauthorized parties from obtaining these items. For

[11] As noted in our May 2005 report, the weighted average cost for warehousing and shipping all supply items was 20.7 percent in fiscal year 2003.

[12] GAO-05-277.

example, although DLA and DRMS have emphasized policies that prohibit batch lotting[13] of sensitive military equipment items, we observed many of these items being sold in batch lots during our investigation and we were able to purchase several of them. In addition, DLA and DRMS have not ensured that DRMO personnel and DOD's liquidation sales contractor are verifying demilitarization codes on excess property turn-in documentation to assure appropriate disposal actions for items requiring demilitarization.

Further, although DLA and DRMS implemented several initiatives to improve the overall reutilization rate for excess A-condition items, our analysis of DRMS data found that the reported reutilization rate as of June 30, 2006, remained the same as we had previously reported—about 12 percent.[14] This is primarily because DLA reutilization initiatives are limited to using available excess A-condition items to fill customer orders and to maintain established supply inventory retention levels. As a result, excess A-condition items that are not needed to fill existing orders or replenish supply inventory are disposed of outside of DOD through transfers, donations, and public sales, which made it easy for us to purchase excess new, unused DOD items.

Despite the limited reutilization supply systems approach for reutilization of A-condition excess items, DLA and DRMS data show that overall system and process improvements since the Subcommittee's June 2005 hearing have saved $38.1 million through June 2006. According to DLA data, interim supply system initiatives using the Automated Asset Recoupment Program, which is part of an old DOD legacy system, achieved reutilization savings of nearly $2.3 million since July 2005 and Business System Modernization supply system initiatives implemented in January 2006 as promised at the Subcommittee's June 2005 hearing, have resulted in reutilization savings of nearly $1.1 million. In addition, DRMS reported that excess property marketing initiatives implemented in late March 2006 have resulted in reutilization savings of a little over $34.8 million through June 2006. These initiatives include marketing techniques using Web photographs of high-dollar items and e-mail notices to repeat customers about the availability of A-condition items that they had previously selected for reutilization.

[13] Batch lotting refers to combining one or more items, or a mixed group of items, on the same turn-in document or sales lot.

[14] GAO-05-277 and GAO-05-729T.

Concluding Remarks

Our most recent work shows that sensitive military equipment items are still being improperly released by DOD and sold to the public, posing a significant national security risk. The sensitive nature of these items requires particularly stringent internal security controls. Our tests, which were performed over a short duration, were limited to our observations, meaning that the problem may likely be more significant than what we identified. Although we have referred the sales of items identified during our investigation to federal law enforcement agencies for follow-up, the solution to this problem is to enforce controls for preventing improper release of these items outside DOD. Further, liquidation sales of items that military units are continuing to purchase at full cost from supply inventory demonstrates continuing waste to the taxpayer and inefficiency in DOD's excess property reutilization program.

Mr. Chairman and Members of the Committee, this concludes my statement. I would be pleased to answer any questions that you or other members of the committee may have at this time.

Contacts and Staff Acknowledgments

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Mr. SHAYS. Could you just make reference to where in your statement you make reference to homeland security and Iran? Which page is that in your statement?

Mr. KUTZ. I don't know if it is in our statement. We had a subsequent meeting to our field work ending, and so it is subsequent to the actual——

Mr. SHAYS. So that is in addition to what you submitted to us?

Mr. KUTZ. Yes, it is. They asked to meet with us and we met with them several weeks ago.

Mr. SHAYS. Thank you.

Mr. Estevez.

STATEMENT OF ALAN F. ESTEVEZ

Mr. ESTEVEZ. Chairman Shays, Congressman Kucinich, members of the subcommittee, thank you for the opportunity to appear before you and discuss the Department's excess property programs. I am Alan Estevez, Assistant Deputy Under Secretary of Defense for Supply Chain Integration, and I appreciate the opportunity to provide an update on improvements we have made since the last hearing in June 2005 and to address the challenges highlighted by the recent GAO draft report on this topic.

I am proud to be joined today by Major General Bennie Williams, DLA's Director of Logistics Operations, and Mr. Paul Peters, a member of the Senior Executive Service and the Director of the Defense Reutilization and Marketing Service.

The fact that we have now placed executive-level leadership at DRMS is an indication of our commitment to the reengineering of our reutilization and disposal process. Before we discuss our efforts to improve reutilization and disposal, I would like to place it within the context of the broader logistics enterprise.

Over the past year, our uniformed and civilian logistics professionals have continued to successfully support complex military operations, including ongoing operations in Iraq and Afghanistan, as well as relief efforts for the Pakistan earthquake and along our own Gulf Coast in support of Hurricane Katrina.

Returns and reutilization are an important part of the DOD supply chain, and the Military Services Defense Logistics Agency and Defense Reutilization and Marketing Service are charged with implementing and executing DOD's policy. We have three main goals for processing or disposing of material which has reached the end of its useful life or is in excess of a military unit's requirements.

First, we want the reutilization process to be a source of reusable material for the war fighter, provided this material can be used without detriment to the mission.

Second, we want to ensure that materiel with potential military application is properly demilitarized or destroyed. Let me be clear: it is our policy and our goal that no materiel requiring destruction will be offered for sale or be available under any circumstances to unauthorized persons.

Finally, we want to get the best value for the DOD material by selling materiel that has no DOD or other authorized user requirement and has been completely demilitarized. DRMS strives to balance these sometimes conflicting objectives.

Independent of but reinforced by the GAO efforts in this area, we have been reengineering the return portion in the supply enterprise. Mr. Peters will discuss DRMS' transformational improvements in detail. Even as DOD makes major changes to the DRMS processes, we have worked diligently to address GAO recommendations. GAO itself has praised DOD's responsiveness and progress in addressing the 13 recommendations in the May 2005, report. We will continue both to address GAO's recommendations and to complete our own review and process improvements.

Let me focus on the most significant area requiring improvement in the recent GAO report, which is the sale of items with military only applications to unauthorized parties. We take this matter extremely seriously and have already implemented procedures to fix that process. Major General Williams and Mr. Peters will provide further details.

GAO has highlighted several other areas in which we believe our practices are sound, and I would like to take a moment to discuss those.

In the last hearing, the focus was largely on concurrent buying of materiel from the commercial sector when such material was available from DRMS. The Department worked diligently to reduce simultaneous buying and disposal, and the July 2006, report provides no examples of concurrent buying.

In its July 10th report, GAO repeatedly highlights the difference between historic cost of an item and the amounts received via public sale. The items that are offered for resale are material in excess of the DOD's requirement, and the prices that the July 10th report references have been set by public auction, an extremely efficient pricing mechanism and thus a far better indicator of a pre-owned item's value than its original acquisition cost.

In closing, Mr. Chairman, thank you for the opportunity to testify before this subcommittee. The DOD has worked diligently and will continue to transform DRMS' processes to increase its effectiveness and improve internal controls.

I would be happy to answer questions you or any member of the committee may have.

[The prepared statement of Mr. Estevez follows:]

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TESTIMONY OF

ALAN F. ESTEVEZ

ASSISTANT DEPUTY UNDER SECRETARY OF DEFENSE

(SUPPLY CHAIN INTEGRATION)

BEFORE THE UNITED STATES HOUSE

COMMITTEE ON GOVERNMENT REFORM

NATIONAL SECURITY, EMERGING THREATS, AND

INTERNATIONAL RELATIONS SUBCOMMITTEE

July 25, 2006

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Overview of the Department of Defense
Excess Property Systems

Mr. Alan F. Estevez
Assistant Deputy Under Secretary of Defense
Supply Chain Integration

Chairman Shays, Congressman Kucinich, and Members of the Committee:

Thank you for the opportunity to appear before you again and discuss the Department's Excess Property Programs. I am Alan Estevez, Assistant Deputy Under Secretary of Defense for Supply Chain Integration. In my position, I am responsible for developing Supply Chain Materiel Management Policy in the Department of Defense (DoD), which covers how the Department keeps our fighting soldiers, sailors, marines and airmen supplied with the materiel they need to fulfill their missions. Returns and reutilization are part of that supply chain, and the Defense Reutilization and Marketing Service (DRMS), a field command of the Defense Logistics Agency (DLA), and the Military Services are charged with implementing and executing our policy.

I appreciate the opportunity to provide an update on improvements we have made since the last hearing in June 2005 and to address the challenges highlighted by the Government Accountability Office (GAO) in their draft report, *DoD Excess Property: Control Breakdowns Present Significant Security Risk and Continuing Waste and Inefficiency*, dated July 10, 2006. I will discuss the solutions we are implementing to improve the return supply chain as it applies to reutilization and disposal.

I am proud to be joined today by Major General (MG) Bennie Williams, the DLA's Director of Logistics Operations, and Mr. Paul Peters, a new member of the Senior Executive Service (SES) and director of DRMS. The fact that we now have SES level leadership at DRMS is an indication of the resources we are devoting to the reengineering of our reutilization and disposal supply chain.

Before we discuss our efforts to improve the reutilization and disposal process, it would be useful to place it within the context of the broader DoD logistics enterprise, a $151 billion operation. We support weapons systems engaged in air, land, sea, space and cyberspace programs around the world and feed and clothe over one million fighting men and women daily. The DoD logistics enterprise would be 9th on the Fortune 500 list if it were a separate company. DLA alone would be in or near the Fortune 50, or roughly the same size as companies such as Intel, Lockheed Martin and Microsoft.

The primary mission of the DoD supply chain is to ensure that the warfighter has the materiel required for his or her mission. I would like to take just a few moments to recognize the efforts of our DoD logisticians in supporting not only the warfighter, but a host of other missions as well. With the help of this Congress, the nation has crafted a world-class military logistics system. Over the past year, our uniformed and civilian logistics professionals have continued to successfully support complex military operations, including the ongoing operations in Iraq and Afghanistan, as well as humanitarian relief associated with the Pakistan earthquake, and the humanitarian relief along our own Gulf Coast. This group of dedicated and knowledgeable logisticians is the only group in the world that could have successfully undertaken these efforts. DLA

logisticians have played a critical role in all these support efforts, including providing over 5.1 million meal kits and bottled water to hurricane victims while simultaneously providing ongoing support to our forces deployed in Iraq and Afghanistan. In fact, a recent Joint Staff assessment rated DLA's support of our warfighters as excellent.

Even as we provide the levels of support at the scale referenced above, we are engaged in a massive effort Departmentwide to transform the operations of our supply chain. This transformation effort includes a comprehensive re-engineering of all of the processes which support logistics, increasing the skills of, and tools available to, our logisticians, and developing the information systems to support our improved processes and people. The results can be seen in such major achievements as:

1) $400 million in cost avoidance through the efforts of DLA, working with the United States Transportation Command, the Distribution Process Owner, and U.S. Central Command to establish a supply depot in Kuwait;

2) a decrease of 33% between 2004 and 2006 in customer wait time, a key performance measure of the logistics system, which measures how long it takes the logistics system to deliver an item to the end user from the time he or she orders an item until it is received.

While we have more work ahead of us, we are proud of what we have achieved to date.

Reutilization and the DoD Supply Chain

An important part of the DoD supply chain is the 3.5 million lines of excess material the DoD processes each year for reutilization or disposal, but it is a relatively

small piece of our total logistics operation. Reutilization is a supporting function, and, as we'll discuss later, reutilization and disposal can help the warfighter fulfill the mission by relieving the burden of unneeded materiel, or by helping the warfighter obtain needed materiel. However, programs that more directly support the warfighters' mission remain the primary focus of the Department's logistics efforts.

The mission of the reutilization and disposal function is to ensure that our troops, whether in garrison or forward deployed, have an efficient and user friendly process for disposing of materiel which has reached the end of its useful life or is in excess of that unit's requirements. If the warfighter doesn't need it, the process for turning it in should be as streamlined as possible.

Once materiel has been inducted into our DRMS process, we have three main goals. First, we want the reutilization process to be a source of reusable material for the warfighter provided this materiel can be used without detriment to the mission. If the warfighter cannot use the materiel, it is made available to other DoD components, and then to federal government components, a variety of state and local agencies, disaster relief agencies, and many others. For example, the DRMS was a significant source of no cost materiel provided during the Hurricane Katrina relief efforts, including generators, shelters, and other items.

Second, we want to ensure that materiel with potential military application is properly demilitarized or destroyed. The challenge is finding the right balance between ensuring maximum reuse of materiel by organizations authorized to do so, while ensuring that no unauthorized individuals gain access to militarized materiel. Let me be clear – it

is our policy and our goal that no materiel requiring destruction or demilitarization ("demil") will be offered for sale or be available under any circumstances to unauthorized persons. Finally, we want to get the best value for the DoD by selling materiel that has no DoD or other authorized user requirement, and that has been completely demilitarized.

The DRMS organization strives to balance these sometimes conflicting objectives. They have shown great responsiveness to the warfighter's needs by working with our forces to streamline the turn in process while monitoring compliance, balancing the need for accurate turn in data with the warfighter's need to focus on the mission. They have tried to balance access to excess materiel, in order to increase utilization, with the risks inherent in allowing authorized outsiders to walk through our warehouses. The DRMS staff is dedicated professionals, performing a mission that only gets recognition when something goes wrong, and are to be commended for their service to the Department and the country.

The reutilization and disposal supply chain is a microcosm of the overall DoD supply chain, and mirrors the transformation efforts going on in the overall logistics enterprise. Independent of, but reinforced by, the GAO efforts in this area, DRMS has been reengineering the return portion of the supply enterprise by engaging commercial resources where appropriate, comparing itself to analogous operations in the commercial sector, and initiating a complete systemic review of risk and its mitigation. DRMS is taking a people/process/technology approach to transformation, and Mr. Peters will discuss such improvements as the linking of disposal and materiel procurement systems, the training done both for DRMS and turn in generators in the Military Services, and the

reviews of internal controls at DRMS locations. Full transformation of the DRMS business, however, will require significant rethinking of the way we do business, just as we are doing in the larger supply chain. I urge the GAO and the Committee to give these professionals the time required to complete this transformation.

Even as DoD makes major changes to the DRMS processes, the Department has worked diligently to address the GAO recommendations. In many cases, the recommendations reflected actions already underway, such as linking the supply and disposal systems under DLA's modernization program, and my DLA colleagues will share the excellent results of this effort which was implemented as we promised this Committee in June 2005. GAO itself has praised the responsiveness and progress in addressing the 13 recommendations in the May 2005 report. In fact, as a result of what seemed to a strong working relationship, we have gained valuable insight from the GAO. I appreciate any assistance that helps us improve support to our forces and strengthens our management controls.

Just as we are continuing to reassess our processes and results in all areas of the supply chain, we will continue our efforts in reutilization. Any Fortune 10 size enterprise will have inherent risks, and one engaged in supporting the greatest warfighting force in a changing world will have increased risk. We will continue to both work with the GAO's recommendations and complete our own review and process improvement efforts.

Let me focus on the most significant area that required improvement in the most recent GAO report, which is the sale of items with military-only applications ("demil-required" items) to unauthorized parties, including items which are accessible to the

broader public. All of us at the Department take this matter extremely seriously. We have begun an assessment of our internal controls and procedures to assess how this happened, have already implemented procedures to fix the process, and continue to identify and fix the root causes of the problem. My DLA colleagues will provide further detail, but I know we can count on the support of all the Military Services and Defense agencies to ensure that the problem is fixed. Clearly, we need to follow the policy and procedures we have in place, and constantly review those procedures for vulnerabilities to human error.

There are no new recommendations in the July 10, 2006 report, and we have had concurrence from GAO that we have made significant progress in addressing the 13 recommendations in the May 2005 report. However, GAO indicates in the July 10 report that there are several areas that still need to be addressed. We are reviewing these areas, including process reengineering and tightening of internal controls to ensure proper handling of disposal materiel and the development of processes to ensure appropriate access to DRMS facilities. There are, however, several areas mentioned in the July 10 report in which our current policy and execution is sound, and which are unlikely to change as we reengineer the DRMS process.

Concurrent Buying and Simultaneous Usage

In the last hearing addressing the excess property program, the focus was largely on concurrent buying of materiel from the commercial sector when such materiel was available from DRMS. The Department and the entire reutilization organization have worked diligently to reduce simultaneous buying and disposal. We were pleased to see

that the July 2006 report provides no further examples of concurrent buying, and my colleagues from DLA will describe the progress we have made in linking systems to prevent such concurrent buying, leading to measurable decreases in this practice, and an increase in reutilization of A-coded items considered ready for use.

However, in the most recent report the GAO seems to have broadened the definition of concurrent buying to include items which are requisitioned by units from the supply system while the same item is available on the DRMS Contractor's (Government Liquidation) site. If the item has made it through the various levels of reutilization screening and into the public sale system, it has been determined to be in excess of our retention requirements. In some cases, there still may be requirements for the item – but we have sufficient items in the inventory to meet expected demand. Under these conditions, good business practice dictates that we do not restock the item but attempt to recover whatever value we can for it, even as we continue to issue our remaining stock. There is a cost to inspecting, transporting, restocking and holding materiel that has already been sold from our national inventory.

Further, it would also be counterproductive to our primary mission to mandate in policy that the warfighter must requisition previously owned materiel from the reutilization system. We have built economic incentives to encourage our warfighters to use this materiel, but it must be at the warfighter's discretion where previously used materiel can be utilized safely, and where it poses unacceptable risk to deployed troops. We have policy and process which encourages the reuse of all materiel where feasible.

Materiel Resale Pricing

In its July 10 report, the GAO repeatedly points out the huge difference between the historic cost of acquisition, and the amounts received via the public resale site. While the GAO makes no specific recommendation about how to increase resale revenues, I'd like to explain the reasons for this apparent disparity.

1) The items that are offered for resale are materiel in excess of DoD's requirement, and not needed by any of the state and local government agencies, relief organizations or cultural groups which have preferential access to DRMS items. The market for these items will clear at a low price compared to the original purchase precisely because there was no demand in the screening process.

2) Original purchase price can be an amount which was paid many years before, for an item, such as electronics in which historic cost of acquisition bears little relationship to its current value.

3) The government does not set prices for these items, nor does the DRMS sales support contractor. The prices that the July 10 report references have been set by public auction, an extremely efficient pricing mechanism which reflects the clearing price for the item. The amounts the GAO references as revenues are determined by the market, and thus are a far better indicator of an item's value than its cost of acquisition in the distant past.

Amount of Excess Materiel

The GAO implies that the DoD is ordering more materiel than it needs, and that is why so many new and unused items are available for resale through the disposal system. Balancing overage (too much materiel) and underage (shortages) is the fundamental challenge of any inventory management system, and this is no different at DoD, Target, Wal-Mart or any other organization with inventory. Like any organization, the DoD would like to minimize the amount of excess and obsolete stock it has, and continues to make significant investments in systems, training and new processes to order the right amount of materiel and minimize excess.

However, there is no organization in the world that handles product that does not have excess and obsolete inventory, and does not sell it at a reduced cost. If inventory planning were an exact science, there would be no outlet malls or end of summer sales. As I pointed out in my prior testimony, the cost of a stockout in weapons system parts is far greater than a stock out at Wal-Mart, and we will always plan our inventory levels accordingly.

We Can Still do Better

Since the GAO issued their report in May 2005, the DoD has worked diligently to address many of the specifics of what DRMS is doing to increase its effectiveness. However, I will focus on some of the actions which we believe can lead to better results in our reutilization supply chain without burdening our warfighter with excessive procedural steps. Whatever steps we taking in addressing GAO concerns must not further hinder the work of our warfighters.

1. We will work to improve internal controls in such areas as access to demil-required materiel and to enhance inventory control and accuracy. This is a major area for continued improvement. In doing so, we will use best practices in evaluating risk/reward and cost/benefit tradeoffs for any changes in internal controls, thus balancing our requirement for a user-friendly turn in process with the need for management control of sensitive materiel.
2. We will continue to work to decrease the amount of excess materiel by improving our forecasting, supply base management and logistics processes. We believe that such initiatives as regional inventory management, Radio Frequency Identification (RFID), commodity management and others can lead to greatly improved warfighter support at equal or lower costs to the taxpayer, and that is our primary mission. At the same time, we will use inventory judiciously as a necessary enabling investment in warfighter support.
3. We will fully collaborate with GAO to define a set of performance metrics and internal control reviews focused on the role of disposal and reutilization in relieving the warfighter of the burden of unneeded materiel, assuring public safety, and ensuring reutilization by our forces, other agencies, or the public.

In closing Mr. Chairman, thank you for the opportunity to testify before the Committee about our plans for improving operations and addressing risks in all aspects of DoD logistics, in particular in our excess property program. I would be happy to answer any questions you and the Members of the Committee may have.

Mr. SHAYS. Thank you, Mr. Estevez.
General Williams.

STATEMENT OF MAJOR GENERAL BENNIE E. WILLIAMS

General WILLIAMS. Good afternoon, Mr. Chairman, Mr. Kucinich, and distinguished members of the subcommittee. I am Major General Bennie Williams, Director of Logistics Operations at the Defense Logistics Agency.

I am responsible for the procurement, management, storage, and distribution of some 5 million line items at an annual volume of 25 million receipts and issues and over $30 billion in sales. As part of this worldwide mission, the Defense Reutilization and Marketing Service, DRMS, provides reutilization, marketing, and disposal services at offices in 37 States and 14 countries, including Iraq and Afghanistan. DRMS handles a complex yearly workload that totaled over 3 million line items at over $20 million in original acquisition cost.

With me today is Mr. Paul Peters, a member of the Senior Executive Service, who assumed leadership of DRMS as its director in February 2006.

Our No. 1 priority is logistics support to the war fighter. DLA works closely with Mr. Estevez and his staff and the military services to resolve related issues.

Ongoing reviews by the GAO and this subcommittee's oversight of our efforts have also helped us to find areas warranting attention in our excess property program. In recent years we have taken many steps to resolve vulnerabilities and inefficiencies in our program. We increased our leadership focus by restructuring our alignment of DLA Senior Executive Service Corps to provide the position Mr. Peters assumed in February. We enhanced reutilization condition code A items through several initiatives, including implementing an update to our modernized software through business systems modernization release 2.2 on schedule in January 2006.

We also took action to improve control over key items received in batch lots, worked with the military services to promote appreciate disposal guidance, increased our oversight of inventory accuracy processes, and we added further controls over further high-risk items. However, we agree more must be done. Previous corrective actions have reduced vulnerabilities but not eliminated them. This was further evidenced by GAO's recent findings. A more thorough compliance validation is required.

It is thus apparent that our current excess property business model must be fundamentally changed to meet the challenges and risk of today's world environment. Our new business model requires a fine balance between maximizing reuse of property, controls over potential vulnerabilities, and the cost versus benefits of related improvements. We need to take a more complete programmatic approach to reengineering and enhancing our excess property program and accelerate progress, as well.

To address the primary focus areas that have emerged from our own and GAO's assessment, we are immediately implementing significant changes in how we account for and process excess property. These include greatly enhanced and consolidated review of items in

batch lots or with local stock numbers prior to any sale to the public. We have immediately typed in procedures for verifying the identity and authority of those seeking to obtain material from DRMS sites and are capitalizing our results of the DRMS A–76 private/public competition.

DRMS also has an in-depth review on the way of the complete range of vulnerabilities and risk mitigation options to define and implement additional improvements, and we continue to develop information technology solutions that will give us greater availability to meet DOD's disposal needs, with the key component being the reutilization modernization program scheduled for implementation in fiscal year 2010.

What I have described is a complete transformation of the DOD reutilization and excess property program. This requires a long-term commitment and focus on all aspects of the program, including human capital, process improvements, and technology-based solutions. We know that revolving issues identified by ourselves, the GAO, and this committee will further mitigate risks to national security, better serve the men and women in the military services, and ensure taxpayer dollars are more effectively utilized. We are committed to providing the leadership and resources required to successfully transform the DOD reutilization and excess property program.

I would be happy to answer any questions you and members of the committee may have.

[The prepared statement of General Williams follows:]

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STATEMENT OF

MAJOR GENERAL BENNIE WILLIAMS

DIRECTOR, LOGISTICS OPERATIONS

DEFENSE LOGISTICS AGENCY

HEARING BEFORE THE

NATIONAL SECURITY, EMERGING THREATS AND INTERNATIONAL

RELATIONS SUBCOMMITTEE

OF THE

HOUSE GOVERNMENT REFORM COMMITTEE

JULY 25, 2006

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NATIONAL SECURITY, EMERGING THREATS AND INTERNATIONAL
RELATIONS SUBCOMMITTEE

Good afternoon, Mr. Chairman, Mr. Kucinich, and distinguished members of the Subcommittee. I am Major General Bennie Williams, Director of Logistics Operations at the Defense Logistics Agency (DLA). I appreciate the opportunity to discuss DLA's and the Defense Reutilization and Marketing Service's (DRMS) on-going and more recent efforts to improve the performance of the DoD excess property Reutilization, Marketing and Disposal program, including addressing National Security concerns the committee may have and the related actions we are taking to ensure that our program resolves such concerns.

As DLA's Director of Logistics Operations, I am responsible for the procurement, management, storage, and distribution of some five million line items, at an annual volume of twenty five million receipts and issues and over thirty billion dollars in sales, for our Military customers, various federal agencies, and allied forces. As part of this worldwide mission, DRMS, a DLA field activity headquartered in Battle Creek, Michigan, provides reutilization, marketing and disposal services at Defense Reutilization and Marketing Offices (DRMOs) in 37 states and 14 countries, including Iraq and Afghanistan. DRMS handles a complex and varied workload involving hundreds of thousands of different products and material. DRMS processed 3.4 million line items, with an original acquisition value of over 20 billion dollars, in Fiscal Year (FY) 2005. This was material that was excess to specific users' needs, but could potentially be reutilized within the department or otherwise sold or disposed of as appropriate. DRMS' roles include extensive efforts to support warfighters in Iraq and humanitarian efforts such as Katrina relief. With me today is Mr. Paul Peters, a member of the Senior Executive Service, who assumed leadership of DRMS as its Director on February 16, 2006.

DLA's number one priority is to provide best value integrated logistics support to the warfighters to help them ensure national security objectives are met. Our demonstrated ability to provide virtually every consumable item imaginable - food, fuel, medical supplies, clothing, weapon systems repair parts,

and construction material - to our forces in Afghanistan and Iraq, and to all our customers worldwide, is a continuing testament to our talented and dedicated workforce.

DRMS plays a vital role in DLA's support to the warfighter by providing essential hazardous and surplus property disposal services to the Military Services at home and where deployed, and by facilitating maximum utilization of these assets elsewhere within the department, or by other authorized customers, at little or no cost to the user. We are also responsible to ensure effective control measures are in place to prevent excess DoD property from falling into the wrong hands.

For many years our DRMS business model was to incorporate accepted commercial best practices and focus on increasing reutilization while reducing costs. In the post-September 11, 2001 era and in support of the Global War on Terror, we have been increasingly emphasizing the identification and mitigation of related risks, while sustaining the overall effectiveness and efficiency of the excess property program and supporting increased requirements in theater with the warfighters. DLA is working closely with the Office of the Secretary of Defense (OSD) and the Military Services to resolve related issues Department-wide and ensure positive results from these efforts. On-going reviews by the Government Accountability Office (GAO) and this committee's oversight have also helped us define focus areas and contributed to improving this important program.

Most recently, four primary areas have emerged from our own and GAO's assessments. They are processing controls for batch lot items and the related impact on controls over material requiring demilitarization, processing of items received at DRMS coded with Local Stock Numbers, improved controls regarding access to DRMS assets, and reducing concurrent procurements of items available at DRMS. We have made progress on all four, but it was apparent from

our own programmatic review this spring, and confirmed by the most recent GAO assessment, that more work remains, especially with regard to the first three areas. The fourth, concurrent procurement, can best be resolved by on-going systemic enhancements described later in this statement.

Accordingly, we are immediately implementing significant changes in how we account for and process certain excess property, while also continuing to ensure we obtain the best value for the taxpayer. As discussed in more detail later in this statement, these changes include implementing enhanced and consolidated processes for items received in batch lots and/or with Local Stock Numbers, as these are elements of our excess property functions that have been at the greatest risk. In addition, we have immediately tightened procedures for verifying the identity and authority of those seeking to obtain material from DRMS sites, while continuing those enhancements that reduce the potential for the Military Services or DLA to simultaneously procure items from the commercial sector that are available in A condition at DRMS.

Before I address in detail our current programmatic improvement actions, I want to note the many actions we have taken to resolve those vulnerabilities and inefficiencies identified in past hearings and reports, including progress to date on current focus areas. I will then discuss how we are proceeding today, including highlighting the aggressive new program that will significantly improve our processing for batch lot and Local Stock Number items. In all of these actions, our ultimate goals for DRMS are to enhance its ability to continue to provide quality support to the warfighter, mitigate risks to national security by strengthening the disposal process and inventory accountability, and ensure taxpayer dollars are spent appropriately.

PROCESS ENHANCEMENTS

Leadership focus and performance assessment: DLA's commitment to improving our stewardship of the excess property program is reflected by the DLA Director's decision in late 2005 to restructure the alignment of DLA's Senior Executive Service (SES) corps to provide an SES position at DRMS. Mr. Peters was selected and, as already noted, took over at DRMS on February 16, 2006. He is the first SES Director of DRMS, and is also the first flag-level or equivalent military or civilian to lead DRMS since 1989. He brings a broad logistics background and has wide ranging experience in auditing and program management across the Department. In the relatively short time he has been at DRMS he has instituted important process, management oversight and programmatic changes which I will address later in this statement. In addition, expanded DRMS performance metrics are included in monthly DLA-wide performance management reviews with the DLA Director, myself and the Agency's corporate leadership, and the Director and I are briefed at least quarterly on the actions DRMS is taking regarding improving property reutilization and disposal processes.

Reducing concurrent procurement: In recent years a principal DLA focus has been on improvements in the excess property reutilization program. Of particular concern was the issue of concurrent procurement and disposal of items that were in excess yet were in serviceable condition (e.g., Condition Code A property). This issue required coordinated action by OSD, the Military services and DLA.

We initially chose internal DLA processes and procedures as a key target, since DLA manages over 70% of the Condition Code A line items received by DRMS. DRMS personnel work with the three DLA Inventory Control Points (ICPs), who are the primary DLA procuring activities, to use existing systems

such as the Automated Asset Reutilization Program (AARP) to help increase reutilization.

Until recently, DLA's own inventory procurement and disposal systems were not integrated, and this had been identified as a significant part of the concurrent procurement problem. As stated during last year's hearing, DLA addressed this factor with implementation of an update to its Enterprise Resource Planning (ERP) software, Business Systems Modernization (BSM) Release 2.2, which became operational on schedule in January 2006. Release 2.2 successfully integrated the AARP functionality for NSN items in the BSM inventory. It maximizes use of DRMS' Condition Code A excess property by systematically ensuring recoupment of those assets up to the amount authorized by DLA inventory retention levels. BSM currently is used at our ICPs in managing about half of DLA's items. Within a year it will be used to manage all of DLA's items, so we expect this means of avoiding concurrent procurement will bring additional benefits in the near future.

In the past year, our DLA ICPs have reutilized over 8,600 line items with an acquisition value of 5.7 million dollars. This is an increase of 24 percent in line items and 77 percent in acquisition value. Specifically, AARP requisitions with the DLA ICPs were 4,841 line items from July 2005 - June 2006, with a combined acquisition value of 2.2 million dollars, while from January through June 2006, DRMS filled 1,201 BSM orders with an acquisition value of 1.2 million dollars.

DRMS also addressed this issue with the Military Services' procuring activities, who do not have direct links to DRMS excess property, by enabling increased use of Automated Want Lists. These lists are created by customers to identify needed items that may be received by DRMS. Begun in June 2004, this initiative enables customers to create a list of up to 10,000 separate items they need. When DRMS receives any of the needed items in its inventory, the

customer is automatically notified via email. DRMS has received 5,663 requisitions as a result of Want Lists since October 2005, with a combined acquisition value of 53 million dollars.

In total, these efforts are showing positive results. To date our overall reutilization rate for Condition Code A property has risen from approximately 18 percent in FYs 04 and 05 to approximately 21 percent in FY 06. For DoD customers alone, excluding mandated programs such as Foreign Military Sales and Law Enforcement Support, the overall reutilization rates are 11 percent for FY 04, 12 percent for FY 05, and 14 percent for FY 06 to date, and this is saving the Department approximately 224 million dollars in original acquisition cost for Condition Code A items.

In the longer-term, DLA continues to implement information technology solutions that will give us greater ability to meet DoD's disposal needs, resulting in further system collaboration and enhanced inventory visibility. The key component of this effort is the DRMS systems initiative known as the Reutilization Modernization Program (RMP). RMP will increase asset visibility and integrate the redistribution of excess property into the Military Services' and DLA supply chains for maximum effectiveness, while increasing the Agency's ability to identify items not currently associated with an NSN. RMP implementation is scheduled in FY10.

Asset coding: In a 2005 audit, GAO raised concerns regarding the Military Services turning in serviceable property as unserviceable. In our efforts to correct this, we discovered that a key problem was that property was being coded as unserviceable because it was obsolete for its current user and was being replaced by newer and better technology. This prevented other Military Service organizations from considering it for use. DLA is part of a joint group that is working DoD-wide options to resolve this issue

In 2005 the Department also had directed the Military Services and DLA to review their excess property procedures, turn-in documentation and accountability mechanisms. DLA and DRMS worked with the Military Services to ensure appropriate disposal guidance is included in their training doctrines, policies, and directives. We are submitting draft disposal language for inclusion in Joint and Military Service publications at their next publication review cycle.

A recurring theme from our customer engagements is that current internal Military Service regulations are adequate, but assigning precise Condition Codes on their turn-ins of excess property to DRMS is a challenge for personnel who already face a demanding workload to support their direct operational commitments. DRMS senior leaders have met with senior Military Service logistics officials, emphasizing the importance of assigning proper Condition Codes, and supporting development of a disposal curriculum to be used by DRMS employees to train those who dispose of property at the installation level.

Batch lot processing and demilitarization ("demil") coding: Batch lots are the physical grouping of individual receipts of low dollar value property under a consolidated turn-in document. In response to prior DLA and GAO findings, DRMS further restricted the kinds of property that could be batch-lotted, as Items in batch lots lose their specific identity. As a result, we broke apart and individually reviewed all batch lots potentially containing the high risk property identified in a 2003 GAO report, required increased review and certification of documentation on all property going into a batch lot, and helped set up a new program specifically to process chemical/biological suits to prevent further releases to the public. As noted later in this statement, we are establishing additional highly focused processes for batch lot and Local Stock Number processing at DRMS that will reduce our reliance on customer coding of turn ins to identify demil-required items.

Inventory accuracy: The 2005 GAO report questioned the accuracy of DRMS' inventory. In September 2005 DRMS began an assessment of existing inventory accuracy issues, including potential problems with property inventory records. Relevant data is reviewed weekly by DRMS field and headquarters personnel. We established eleven account monitor positions to help improve inventory management and data integrity, and improved the visibility of internal DRMS shipments. The initial results are positive - DRMS' net inventory loss rates have declined, from 0.17 percent in FY 04 to 0.06 percent in FY05 and 0.05 percent to date in FY06.

Security: DRMS increased its emphasis on risk management. This included identifying and funding physical security improvements at key sites and tightening controls over release or sale of property. DRMS screens property for laboratory equipment that could conceivably be used by terrorists. We also increased our computer-supported ability to view excess assets held by our sales contractor, Government Liquidation (GL), and are now using it to ensure only appropriate items are available for potential sale, including revalidating an item's demil code prior to sale by GL. As discussed further in this statement, DRMS recently initiated a complete review by DRMS HQ and field personnel of literally every step in the property disposal process, to identify the risks and vulnerabilities within each step, and the actions necessary to address those risks.

PROGRAMMATIC CHANGES

As I just discussed, we have initiated various process enhancements to address concurrent procurement of available assets, to improve control of items received at DRMS and to reduce risks in other specific areas. Today's post-9/11 environment and the DoD excess property business model call for increased emphasis on preventing inappropriate property from falling into the hands of the wrong people, and requires a finer balance between maximizing the re-use of

property, controls over potential vulnerabilities and the costs vs. benefits of related improvements. We have made progress, but our actions must be accelerated and more changes are needed.

Accordingly, DRMS and DLA have realigned our processes to further prevent the release of potentially harmful property to the public, even if this may result in reduced revenue and some increased costs to the taxpayer. This requires further changes to the DRMS business model. Our current efforts to address related risks and achieve overall improved performance at DRMS are focused on five specific areas: Improving handling of batch lots (especially with respect to items requiring demilitarization), better management of items we receive with Local Stock Numbers (LSNs), enhanced security, immediate additional issue-focused process enhancements, and capitalizing on the results of the DRMS A-76 public-private competition. We are also aggressively pursuing broader DRMS-wide programmatic improvements, and will continue the systemic enhancements that will further limit incidents of concurrent procurement. I will now summarize our progress in each area:

Batch Lots and demil items: The most recent GAO investigation indicated continued problems in the areas of release of demil-required property inadvertently placed in batch lots, and the potential for unauthorized persons to obtain such excess or surplus property via fraudulent means. GAO's recent findings confirmed that despite the challenges and costs involved with more stringent review of low value batch lot items, increased compliance validation was required for these items, which were 44 percent of the line items processed by DRMS in FY 05.

DRMS immediately froze the processing of all batch lots currently in the possession of DRMS and its sales contractor, Government Liquidation (GL), and took them apart to ensure the property contained within was appropriate for release. DRMS is now implementing an aggressive new approach to more fully

control batch lot material. This fundamental change in the business model will centralize batch lot physical verification and implement a 100% physical inspection of all such items prior to sale. This approach, and our ability to devote experienced disposal subject matter experts to this consolidated batch processing and provide multiple reviews of the property involved, will be more effective than our current decentralized batch lot process in preventing inappropriate release of property.

Local Stock Numbers (LSNs): Another major focus area is the use of Local Stock Numbers (LSNs). LSN items are an especially challenging element of the DoD property disposal program, in that they represent approximately 40% of the items received in DRMS, often as part of batch lots. In many cases, LSNs reflect items purchased from the commercial sector, often procured with IMPAC cards used Government-wide to reduce unnecessary and expensive procurements, or via Prime Vendor support contracts. These items are not turned in with a National Stock Number (NSN) that is fully coordinated across the department. Other items that have a valid NSN are sometimes turned in under LSNs. Without an NSN readily available, LSN items lack a detailed item description and cannot be automatically screened to determine their demil code. GAO identified use of LSNs as a deterrent to reutilization in their earlier report. After considering various alternatives, we have concluded that LSN items, except for low risk categories such as furniture, commercial vehicles and appliances, will be processed in the same consolidated and focused manner described above for batch lots---with 100% physical inspection at the same sites we will use for batch lot processing before consideration of public sale.

Security: Despite improved procedures, DRMS was also recently made aware of vulnerabilities in the release of property via reutilization to unauthorized persons. GAO personnel, using forged documents and posing as contractors working for an Army activity, removed demil-required property from at least two DRMOs. Until this occurred, the reutilization of military equipment by DoD

activities had been considered a lower risk for unauthorized property release than was the sale of property to the public. DRMS took immediate action to significantly minimize the risk of unauthorized release by tightening its procedures to be enforced on all walk-in removals of DRMO property. These procedures require, among other things, that all authorization letters be on file at the DRMO before the arrival of the screener, and that before property is released, the DRMO must contact the point of contact for the authorization letter and obtain verification authorizing release of the property. DRMS and DLA are also reviewing policies and procedures to determine if ending walk-in reutilization is a long-term solution. This change, if adopted, could have negative effects on the program's benefit to the warfighter, by making reutilization overly burdensome.

Another concern raised by the GAO was their ability to obtain a clearance from DLA to purchase export controlled material from DRMS' sales partner, GL. A GAO agent was able to obtain a favorable Trade Security Control (TSC) assessment using an assumed identity, by providing copies of a forged driver's license and utility bill and a Social Security card issued in the name of the assumed identity. Despite these efforts, the TSC assessment process identified problems in GAO's application, but an error still occurred when the undercover GAO agent was able to explain away the noted problems. In an effort to address these issues, additional training will be provided to TSC assessment office personnel to ensure no buyer is favorably assessed without first resolving all discrepancies that cast doubt on the buyer's identity.

GAO's purchase of export controlled material clearly should not have happened, but we do not consider it representative of the overall quality of our aggressive TSC efforts. In a post-9/11 environment, DLA has focused the TSC program on both overseas and domestic sales. DLA's TSC program is accomplished through a three-pronged approach. First, TSC assessments are conducted to evaluate the integrity and reliability of all prospective purchasers

of controlled property requiring Trade Security Controls to reduce the likelihood of unlawful exports or diversion to unauthorized buyers. Second, DLA uses proactive Post Sale Investigations of selected buyers of the property to detect and prevent illegal exports or diversion. Finally, purchasers of controlled property are educated regarding export licensing requirements through written notice provided to all assessed buyers before the sale, and through written and in-person notices provided to those buyers who are contacted during Post Sale Investigations. DLA has applied due diligence in this area and provides a level of scrutiny that goes beyond regulatory requirements to include domestic sales.

In a further effort to strengthen this process, DLA is currently preparing a procedure for public comment that will allow us to exclude questionable buyers from purchasing Munitions List and Commerce Control List items (demil codes B and Q property). We anticipate this procedure will be ready for implementation by December 2006.

Additional near-term process enhancements: Institution of more quality control checks and validations in the day-to-day processes of DRMS are another step forward. DRMS uses internal Self-Assessments and Compliance Assistance Visits (CAV) to monitor compliance with existing written policies and procedures. DRMS has conducted four quarterly Self Assessments at each DRMO and 50 CAVs since June 2005. Effective this month, DRMS is strengthening these compliance activities through use of operational effectiveness reviews. These review teams will be comprised of senior disposal experts from within DRMS. Their purpose is to determine compliance with established procedures, assess business processes to identify vulnerabilities, determine effective risk mitigation actions and test those corrective actions. Inspection protocols will also be enhanced to ensure they cover vulnerabilities being identified in the ongoing DRMS risk assessment process.

A-76 results: Another major focus area is for DRMS to fully implement a fundamental change in the way it does business through the A-76 Most Efficient Organization (MEO) for DRMS warehousing operations in the continental United States. The MEO is the result of a competition that began in 2001, and the transition period is concluding this month. As stated previously before this Subcommittee, the stand up of the MEO will result in a reduced organizational and physical structure (18 fully staffed DRMO warehousing operations compared to 68 last year), improved command, control and communication and more efficient use of facilities.

Broad-based Programmatic Enhancements across DRMS: To ensure we have been as comprehensive as possible, DRMS has undertaken a major program review to identify further improvements that may be needed throughout the DoD disposal system. The first wave of process improvements was primarily aimed at outside influences on the system, and the results of these efforts have been discussed earlier in this statement. The second wave of this effort was to identify all risks and vulnerabilities in the DRMS internal processes and define the risk mitigation actions. The initial payoff from this wave is the program we are now implementing to improve the processing of batch lot and LSN items that I described earlier, as well as enhanced controls over property release to individuals. We expect significant reduction in the problems cited in the GAO's most recent findings as a result of our new batch lot and LSN processing approaches, but other challenges and vulnerabilities remain. Full in-depth review and execution of other vulnerability and risk mitigation options are expected to take a year or more to complete.

In addition to these initiatives, we continue to address systemic enhancements to reduce concurrent procurements, which will come to fruition with expansion of BSM use across all DLA-managed items over the next year, and RMP's implementation in FY10.

In closing, Mr. Chairman, DLA's highest priority remains top quality direct support to the warfighter. We know that resolving issues identified by ourselves, the GAO and this committee will further mitigate risks to National Security, better serve the men and women in the Military Services, and ensure taxpayers' dollars are more effectively utilized. The challenges we face require a sustained cost-effective effort, and we believe we have taken significant steps toward resolving the identified short- and longer-term problems, both in recent years and with the additional immediate steps concerning batch lots, LSNs and property release processes that I have outlined today. We remain committed to providing the leadership, modernized systems, process enhancements and resources needed to resolve these concerns, and to help ensure that America's fighting forces remain the best equipped in the World at the best value cost to the taxpayer.

Mr. SHAYS. Thank you.

Before I recognize Mr. Peters, General, I want to thank all of our witnesses for serving their country, but I particular want to thank you for your service in support of Operation Desert Shield, Storm, Saudi Arabia, Operation Restore Hope, Somalian Operation Joint Endeavor, Boznia Herzogovinia. We appreciate your service to your country.

General WILLIAMS. Thank you, sir.

Mr. SHAYS. You are welcome. Thank you.

Mr. Peters.

STATEMENT OF PAUL PETERS

Mr. PETERS. Mr. Chairman and distinguished members of the subcommittee, I am Paul Peters, Director of the Defense Reutilization and Marketing Service.

DRMS is a field activity of the Defense Logistics Agency responsible for the execution of DOD policy on the processing of DOD excess property. Specifically, DRMS provides reutilization, marketing, and disposal services worldwide, including serving side-by-side with our military forces in Iraq, Kuwait, and Afghanistan, and handled last year over 300 million line items valued at approximately $20 billion in original acquisition cost.

Although actions have been implemented to address the excess property concerns raised in prior hearings, the most recent GAO findings and our own internal analyses have demonstrated that more work remains. My appointment as the first SES Director of DRMS on February 16, 2006, shows that DLA is committed to a long-range, consistent effort to fix these problems. We must continue to balance the maximum reuse of property, controls over potential vulnerabilities, and the costs and benefits of improvement.

Current pressing issues include the proper disposal of demil-required property in batch lots, proper disposal of local stock number items, and mitigation of unauthorized access to obtain property. To resolve these issues, we immediately froze the processing of all batch lots and took them apart to ensure the property was appropriate for release. We are now implementing a reengineered approach to control batch lot material by establishing consolidated, centralized sites where batch lots will be verified and all items will be 100 percent physically inspected prior to sale.

Items turned in to DRMS with a local stock number lack a detailed item description and cannot be automatically screened to determine the right demil code.

Higher-risk local stock number items will be processed in the same manner as described for batch lots, with 100 percent physical inspection before public sale.

GAO personnel posing as DOD contractors working for the U.S. Army used forged documents to remove demil-required property. Immediate action was taken to tighten the walk-in procedures for excess property removal and ensure that authorization letters and potential screeners are independently verified before property release.

The GAO was also able to get a clearance from DLA to purchase export-controlled material by using an assumed identity and forged documentation. Additional training is being given to ensure that no

buyer is favorably assessed without resolving discrepancies in that buyer's identity.

DLA is also preparing a procedure for public comment that would exclude questionable buyers from purchasing such property.

The transition to the most efficient organization in the continental United States will further reduce the number of fully functioning DRMS warehousing operations from 68 to 18, thereby improving command control and communication regarding the processes such as those I have just discussed and enabling more efficient use of resources, in addition to actions to leverage existing DLA systems and the plan for their transformation by providing improved capability to DLA activities to match excess property assets against inventory retention levels.

The overall reutilization rate for condition code A property was approximately 18 percent in fiscal years 2004 and 2005 and is currently 21 percent year to date in fiscal year 2006 and is saving the Department approximately $224 million in original acquisition cost.

Finally, we are conducting a major outcome-based review to identify additional vulnerabilities and gaps in DRMS processes, to define and test the appropriate corrective actions, and to continue the efforts to improve condition code and demil code accuracy.

The re-engineered batch lot and local stock number processes noted earlier are an important initial result of this review.

Mr. Chairman and distinguished committee members, we are taking both the short-and the long-term actions necessary to ensure these problems are resolved and to enable DRMS to provide the best possible support to the war fighter while conserving taxpayer resources.

Thank you.

Mr. SHAYS. Thank you all very much.

We will start with Mr. Marchant. We are going to do 10 minute rounds of questions.

Mr. MARCHANT. Thank you for your testimony today.

Major General, in your statement you talked about a new business model. How long has the concept of a new business model been in the works as far as this process goes?

General WILLIAMS. Sir, we started a new business model when I assumed responsibilities in my current position and when Mr. Peters came onboard. The focus is really to concentrate on how we can improve upon those improvements that have been made, the seams and gaps that we detected, and work that needs to be done, and there is more work that needs to be done. So we just want to pile on what has already been done and then improve upon what has been done and then really do some reengineering because we need more work done and done faster, sir.

Mr. MARCHANT. What would you say would be the major difference in the resale or disposal of excess items versus 10 years ago that exist today? What would be the major difference in how you disposed of these items 10 years ago or during the Bosnian War or Desert Storm as opposed to now? Are there new complexities involved? Are there new business strategies, or is there just more stuff to get rid of?

General WILLIAMS. No, sir. In terms of items to get rid of with our Army, I won't put a quantity on that; however, what I will tell

you is that the key to success is identifying that which need not fall into the hands of a third party. If there is a demil required, then it is our responsibility to, No. 1, correctly identify, to accept accountability, and to ensure that throughout the process that item does not transition over to GL or is eligible to be bought by a third party, sir.

Mr. MARCHANT. Thank you.

Mr. Peters, is there a penalty, is there a civil penalty, is there a crime that is committed if someone falsifies bidding information, besides the GAO, to obtain sensitive material? Do we have a prosecutorial system to go after someone that obtains something fraudulently?

Mr. PETERS. Congressman, the process that is in place right now when a prospective buyer fills out an end use certificate is designed to verify their identity and the stated intention and purpose of the item that they are purchasing. What happened with the GAO was those alarms went off. There were discrepancies in the identity information that was provided.

The assessor, unfortunately, made a favorable assessment for that buyer without resolving the discrepancies in that identity. If a public citizen were to do the same thing that GAO did, our job is to try to verify that those discrepancies exist and determine that individual is not authorized for that. I am not aware of a prosecutorial position that DLA or DRMS would take, but clearly our job is to properly execute that process and ensure that those individuals are identified and we don't favorably resolve their assessment while there are still discrepancies.

Mr. MARCHANT. Is there some kind of a notification process that you would refer to the Justice Department when someone tried to fraudulently obtain excess material?

Mr. PETERS. If we were aware of an individual trying to make that attempt, we certainly would inform DLA and the Department. At this point I haven't been here long enough to——

Mr. MARCHANT. Mr. Ryan seems to have an answer.

Mr. RYAN. Congressman, in situations where someone is lying to the Government, there is violation to Title 18, 1001, false statement to the Government. The method in which they are making application, either by wire or mail, is also a violation of the crime. In this particular case they shouldn't be referring these things. Once a red flag comes up, they should be passing this on to agents who have experience in interviewing people and can get the information and the intelligence that they need from the field to make value decisions.

But to answer your question, there are violations that they can pursue and they should work that out with Justice and determine if Justice is going to pursue these type of crimes.

Mr. MARCHANT. I guess my question, rhetorical question, is if there aren't any referrals going on and there is, in de facto, no penalty, nothing, no down side to having this happen, you know, maybe people aren't being discouraged from doing this.

Mr. PETERS. Congressman, if I may, the Defense Criminal Investigation Agency and DLA is involved in the assessment process, and so their involvement would automatically trigger that type of notification internally to our Agency.

Mr. MARCHANT. I would suggest that maybe occasionally one of those cases be made public so that the public, in general, understands that there is some consequence to this kind of behavior.

The last thing I will ask of Mr. Kutz or Mr. Peters, either one, has there been an analysis made of the cost of the Agencies that implement the sale of the property, and does the value of the sale of the property even cover the cost of the agencies that are charged with selling the property? I mean, do we have this whole elaborate system of disposal of materials that costs more than we recoup from the sale of the material? Has there been any kind of a cost analysis done of that?

Mr. PETERS. Congressman, when you just look at condition code A, reutilization of property, in fiscal year 2006 year to date we have reutilized approximately $224 million just in condition code A property. That exceeds the cost of operations of the DRMS. If you look at the total reutilization of all property for the Department, it is well over $1.5 billion. Again, that far exceeds the operating cost of the DRMS.

Mr. MARCHANT. OK.

Mr. KUTZ. There are two savings. There is the issue of how much you bring in from the public sales, but the reutilization within the Department of Defense and Government agencies there is a bigger savings to the Government there.

Mr. MARCHANT. OK. Thank you.

Mr. SHAYS. I wonder if the gentleman would yield the remainder of his time?

Mr. MARCHANT. Yes.

Mr. SHAYS. Thank you. I think Republicans and Democrats are on the same page in terms of what we are seeing at this hearing. I would just like to start by asking about the all-band antenna. Is this all-band antenna new or is it used, Mr. Kutz?

Mr. KUTZ. I believe it is new and unused.

Mr. SHAYS. Mr. Ryan, that is correct?

Mr. RYAN. Yes, that is true.

Mr. SHAYS. Are we still purchasing these antennas or are they antennas that we are no longer purchasing?

Mr. KUTZ. According to the manufacturer, they are still producing them for the Department of Defense.

Mr. SHAYS. OK. Were we incorrect when we stated it cost $120,000?

Mr. KUTZ. According to DOD records, that is a $120,000 purchase.

Mr. SHAYS. And this was given free to you, to our inspectors? That is correct, Mr. Ryan?

Mr. RYAN. Yes. When we went to the DRMO we walked in and requisitioned it and we walked out with it.

Mr. SHAYS. I mean, the bottom line to this is, Mr. Kutz, what I find most surprising is your statement that you are saying that the Department of Homeland Security is saying they are looking for this equipment that is being sold by the Department of Defense, that it is getting into the wrong hands; is that correct?

Mr. KUTZ. Particularly of interest to them were the aircraft parts, and F–14 was the major part. As you know, Iran is the only country that is currently flying F–14s.

Mr. SHAYS. Iran has the old F–14s.

Mr. KUTZ. Correct.

Mr. SHAYS. We have refused to provide parts for them, so they are going really on the black market.

Mr. KUTZ. Yes.

Mr. SHAYS. And so these were bought for nothing or for something?

Mr. KUTZ. For something. I mean, the ones that were the F–14 micro circuits, we actually bought those on the internet.

Mr. SHAYS. But to Iran they are worth a fortune, correct?

Mr. KUTZ. Correct.

Mr. SHAYS. Thank you.

I recognize Mr. Kucinich. Mr. Kucinich has pointed to you, so I recognize you, Mr. Waxman.

Mr. WAXMAN. Thank you very much.

Mr. Peters, as I understood your answer to the question a minute ago, there are procedures that alert you when someone is pretending to be someone else in order to buy equipment; is that correct? You said there was a red light that went off?

Mr. PETERS. Yes, sir.

Mr. WAXMAN. In effect?

Mr. PETERS. Yes.

Mr. WAXMAN. Gee, I was pretending to be a Defense contractor; is that right?

Mr. PETERS. Yes.

Mr. WAXMAN. And you were alerted to that fact, yet they were able to walk off with $1 million worth of equipment. What happened? Why didn't somebody at Defense say wait a minute, we are starting to get suspicious you are not who you say you are? Why did the sale proceed?

Mr. PETERS. For clarification, Congressman, the trade security control process that I was describing was different than the process of allowing an authorized screener to walk onto a military installation into a DRMO and directly remove property. The direct removal capability is something that exists for the convenience of the military services to acquire the items that they need to support their mission. The issue——

Mr. WAXMAN. But if there was some suspicion that somebody—it turned out to be GAO—was passing themselves off as a legitimate purchaser, a Defense contractor, and you had some idea that was happening, why was the sale culminated?

Mr. PETERS. For the direct removal process where the GAO was able to use letters of authorization and identification to have physical access to the receiving area and remove items, the breakdown in the procedure there is that the letter of authorization, the identity of that individual, and the confirmation of the items that they wish to remove need to be independently verified to offset and mitigate that risk. That process did not happen at the point in time at the two DRMO warehouses on the east coast where the GAO was able to conduct the direct removal investigation.

We have tightened those procedures by ensuring that there is an independent verification of the letter of authorization from the home organization and the identification of that individual with the

home organization and a confirmation of the items that individual would wish to remove.

Mr. WAXMAN. So you think that the problem will be corrected?

Mr. PETERS. Yes. The actions that we have already taken in response to what the GAO was able to do will significantly mitigate the risk of that type of operation again.

Mr. WAXMAN. Well, Mr. Kutz, you were here before. This isn't the first time that we have been able to fool the people at the Defense Department into selling your undercover agents military equipment. Some of that military equipment jeopardizes our national security; isn't that right?

Mr. KUTZ. Yes. This is items that could be used against us or other countries.

Mr. WAXMAN. Now, one of the examples that you used was dozens of classified digital micro circuits, including those for F–14 fighter aircraft. Your report states these are classified items that require protection in the interest of national security. What was supposed to have happened to these micro circuits?

Mr. KUTZ. They should have been destroyed. They should not have gone out in a public sale.

Mr. WAXMAN. And who would want these micro circuits? Are there any foreign countries or U.S. adversaries that would want to get their hands on these items?

Mr. KUTZ. Well, we are aware that the only country flying F–14s right now is Iran, and the investigators that came over and met with us several weeks ago had said that they had serious concerns about F–14 parts leaving DOD and going to Iran. So yes.

Mr. WAXMAN. Well, my colleague on the other side of the aisle said perhaps we ought to make some of this public so that the American people would know it is a crime to do what you did, in effect, by representing yourself as eligible to buy this equipment. Instead we have a hearing this year, as we had in previous years, indicating that it is not that hard to fool these people at Defense. Why was it so easy for you to be able to buy equipment that could jeopardize our national security?

Mr. KUTZ. Well, with respect to the end use certificate, I want to clarify those are two separate incidents.

Mr. WAXMAN. OK.

Mr. KUTZ. When we posed as contractors they did not have suspicion that we weren't contractors. When we got our end use certificate they actually called us and said the person that applied for this end use certificate doesn't exist, doesn't have the credit history, doesn't have any other history. The answer to the question we gave them is that it was identity theft, and they bought it.

And we basically then counterfeited—we said we will send you a copy of a utility bill. They said that would be fine. We sent them a copy of the utility bill, which we forged basically, and, based upon that, they accepted our application. And that end use certificate allowed us to purchase several of the items that you are talking about now.

Mr. WAXMAN. You are pretty smart. Do you think some of our adversaries could be just as smart and get away with purchasing this equipment?

Mr. KUTZ. I suspect they are much smarter than we are, certainly.

Mr. WAXMAN. I mean, this is really incredible because we are talking about national security of the United States of America. Wouldn't it be better to—well, they are supposed to be destroyed. Why weren't they destroyed?

Mr. KUTZ. I think it was a combination of the batch lots that were mentioned. I think they covered in their opening statement some of the reasons. I think they have gone back and taken a look at some of the reasons these have gone out. There are issues with errors in coding, items getting into these batch lots, and other types of errors that have occurred in the system why these were able to get out. I think they know what the problem is. They need to demonstrate that they can fix it or it really raises questions about whether we should be selling things to the public.

Mr. WAXMAN. Are you satisfied that what Mr. Peters told us is going to be a fix for the future, is going to stop this from happening in the future?

Mr. KUTZ. Well, from a standpoint of what he said it sounds good. I mean, I think we would have to look at more of the details of actually what they are going to plan to implement and how they can do it, because the issues relate to people, processes, and systems, as I think the general said, and so they have to address all of those areas to be successful in what they are doing.

Mr. WAXMAN. Mr. Estevez, you are the Deputy Under Secretary for the supply chain integration, and General Williams, you are the Director of the Logistics of Operation, Defense Logistics Agency, and Mr. Peters, you are the Director of the Defense Reutilization Marketing Service. Who is responsible for what we are hearing about these breaches of our national security and what we have heard in the past were also breaches of our national security? Who is responsible?

Mr. ESTEVEZ. Let me answer that, Congressman Waxman. In my job I write the policy that we are executing for not just the disposal process but overall supply management in the Department of Defense. Our policy remains sound in this regard. Items that should be destroyed we need to destroy.

I also provide oversight of the process, and I will go back to the point that over the course of time, in answer to some of GAO's previous findings, we have been marching forward also on our own, changing the structure of the DRMS organization, changing the leadership to making it Executive level leadership, are all things that the Department has been doing because we recognize the issues here.

Again, let me be clear that we do not want anything that should be destroyed out for sale to the public.

Mr. WAXMAN. Well, you shouldn't have wanted it the first time it was revealed to us that this sort of thing was happening. Now, GAO says this is a significant security breach. Do you disagree?

Mr. ESTEVEZ. No, I do not, but I want to point out that GAO, in its investigation, in their ability to access a DRMS facility posing as not a DOD contractor, as contract support for the U.S. Army—so they were representing themselves as a valid Army agency with the ability to take any of this material. We have put checks in proc-

ess, and I agree we need to do those checks in process, but GAO has a lot of information that a private citizen would not have in order to perform that false identification.

Mr. WAXMAN. Now, do you know how many agents have been assigned to investigate examples of this kind of transaction where either security is being breached by equipment that should have been destroyed has been sold or what we have also heard about, equipment that shouldn't have been sold, been sold for pennies on the dollar? How much manpower are we spending to investigate these sales after the fact?

Mr. ESTEVEZ. Sales after the fact would be referred to Defense Criminal Investigation Service, and after that I would have to take the question for the record on how many people they may be expending or how many people GAO may be expending through law enforcement to address that issue, sir.

Mr. WAXMAN. Mr. Kutz, is this really a money-making venture for the Department, or do the risks of these kinds of security breaches outweigh any monetary benefit that might arise? Perhaps the best way to settle this problem is not to let them sell what they call excess equipment. What is your thought on this issue?

Mr. KUTZ. I think in the long term if they are unable to demonstrate that they can prevent military technology from going out in the excess system to the public, then that is a very serious question that they would need to answer, and maybe Congress would need to take action. If they can't show that they can prevent it from going out, the $30 or $40 million that they net from the public sales is possibly not worth it.

Mr. WAXMAN. My time is over, but I do want to say, Mr. Chairman, you said Democrats and Republicans both are outraged by this behavior, but Republicans are in charge. They are in charge of the Congress and they are in charge of the executive branch, and someone should be held accountable.

If we are not going to have the people at DOD held accountable, we ought to have the elected officials held accountable who are supposed to be sure that these kinds of things do not take place. They claim to be fiscal conservatives, they claim to care about national security, and we see this gross incompetence which jeopardizes every American, Democrat and Republican.

Thank you.

Mr. RYAN. Mr. Waxman, I would like to respond to the statement about—I would like to comment on Mr. Estevez' statement about having a great amount of knowledge to be able to accomplish this. This was done with information that you can get off the internet. This information that we used, we have a policy that we don't use inside information, so we didn't use it.

As a matter of fact, when we called the contractor or we called DRMO to find out how to prepare the forms, they were gracious enough to tell us what to put on the forms. So it is a matter of they are accepting—this idea of challenging isn't part of the process. It is an accepting. They accept what you tell them so they can fill a blank in, and then they go ahead and they allow you to get what you need.

So I just want the Congress to know that we didn't use inside information; that the agents that did this used publicly available

information to be able to accomplish this, with a little bit of guts to walk in, and that is all it was.

Mr. SHAYS. Before I recognize Mr. Kucinich I just want to point out that the Department of Defense has been unauditable since 1947, starting with President Truman. This has been an issue that both Republicans and Democrats have been trying to deal with for years. This is a problem that exited pre this administration. I do agree we need to deal with it, but I want that on the record.

Mr. Kucinich, you have the floor.

Mr. KUCINICH. Thank you very much.

Mr. Kutz, is it possible that private contractors are buying sensitive equipment at a discount and then turning around and reselling it back to the Pentagon at market prices?

Mr. KUTZ. Yes. In fact, I think it has been documented that has happened in the past, but that is possible.

Mr. KUCINICH. And are you continuing to look at that, that we pay twice for something?

Mr. KUTZ. We have not looked at that, no.

Mr. KUCINICH. Mr. Chairman, I think it would be useful, in the context of looking at surplus equipment——

Mr. SHAYS. Don't give away our next hearing.

Mr. KUCINICH. All right. But I think it would be useful. We are looking at a whole system here. How is something declared surplus? Who declares it surplus? Do they have any business interest connected?

Once something is declared surplus, how long is it sitting around as surplus? Who purchases it? What do they do with it and how fast do they move it? Who do they resell it to? How much was it first purchased for by the taxpayers? How much did the secondary purchaser pay for it? How much was it resold for? It is like a whole system here we are looking at.

Now, there was an allusion made by Mr. Shays earlier. We had a little side conversation about an issue about a black market. I mean, is it possible that Army "surplus" is a substantial part of a black market in Defense material?

Mr. KUTZ. I don't know about substantial. It certainly is possible, and I think that the investigators have told us that it is. I think that the other market is a legitimate market. There is a lot of industries that have cropped up around the country of people who live off of the DOD excess property system, and there is various associations and surplus stores, etc., that buy these items legitimately and resell them to the public, and presumably they are making a profit on it.

Mr. KUCINICH. OK. We are saying these items.

Mr. KUTZ. Not the military sensitive items. I am talking two things: the sensitive items on the black market you are talking about, versus legitimate.

Mr. KUCINICH. Are you aware of everything that is sold Army surplus? Do you have a list of every single thing that has been sold on surplus?

Mr. KUTZ. We wouldn't have a list, no.

Mr. KUCINICH. Who does? Who knows? Who has the list of everything that is being sold Army surplus? I mean, you showed missile launchers. Are missiles being sold Army surplus? You showed parts

for an F–14. Are planes being sold Army surplus? You showed radar guidance.

Who has the list of what is being sold Army surplus? We don't really know what we are talking about here if we don't—I mean, we have to define what we are talking about. What is for sale? Does anyone know? Does anyone have a list? It is unbelievable.

Mr. ESTEVEZ. Congressman, we could tell you what processes through the excess system, through DRMS. There are other types of material.

Mr. KUCINICH. That is the Defense——

Mr. ESTEVEZ. That is the Defense Reutilization and Marketing Service.

Mr. KUCINICH. Just may have tuned in. It is Defense——

Mr. ESTEVEZ. Defense Reutilization and Market Service.

Mr. KUCINICH [continuing]. Reutilization and Market Service, and that is pronounced "dermes?"

Mr. ESTEVEZ. "DRMS" is the way we would pronounce that acronym.

Mr. KUCINICH. "Dermes?"

Mr. ESTEVEZ. Close enough.

Mr. KUCINICH. OK. Go ahead.

Mr. ESTEVEZ. We would be able to tell you what we process through that pipeline, whether it goes in for destruction or whether it goes out through donation to first responders, the other needy hospitals and the like that are eligible for that type of material through special——

Mr. KUCINICH. Could you make available, Mr. Chairman, Mr. Estevez, to this committee the list of what is Army surplus?

Mr. ESTEVEZ. I am going to have to turn to Mr. Peters, but I believe we could tell you what was processed through the system.

Mr. KUCINICH. Mr. Peters.

Mr. PETERS. Yes, sir, we can make available for the record items that have been sold, transferred, and donated and reutilized.

[NOTE.—The information referred to may be found in subcommittee files.]

Mr. KUCINICH. Well, what is Army surplus? What constitutes Army surplus, Mr. Kutz, is it anything the Army says is surplus, correct?

Mr. KUTZ. If they've declared it surplus and it goes through their system, yes.

Mr. KUCINICH. So it could be anything?

Mr. ESTEVEZ. But that does not include things like munitions that would be destroyed. We would not sell munitions. We would not excess munitions. Munitions that have reached their end of useful life would be destroyed. Weapons platforms, tanks, planes, etc., certain types of those might end up, after they are demilled, after the military capability is removed, given to museums or certain associations, but only under certain conditions. For the most part they——

Mr. KUCINICH. You are talking about weapons. Are weapons Army surplus?

Mr. ESTEVEZ. Again, they would not go through this process, but certain types of those items could end up being given—not fighter planes, but planes could be given to first responders, and there are

certain old planes that could end up in museums with the military capabilities for those weapons platforms, tanks, planes, etc., removed from them before they would be allowed out, many of those at congressional behest.

Mr. KUCINICH. You know, I want to say that the gentleman representing various aspects of handling the surplus, it is comforting to hear you speak with such certitude. On the other hand, when GAO does its investigations the certitude with which you speak meets a little bit of reality. There is reality testing right next to you.

We need a list to know exactly what is declared surplus.

The other thing that I am interested in is the relationship between what our taxpayers pay for it and the creation of a black market. I am very interested in that. I mean, if you are talking about these—you were able to essentially fake some documentation to get an end use certificate. Have there ever been audits done of end use certificates to see how many other end use certificates, since it was so easy for you to fake it, are there other end use certificates that might similarly be faked that have resulted in people getting goods that they shouldn't have?

Mr. RYAN. I am not aware of an audit that was done, but I can tell you that when we held the conference with DHS investigators and the DOD investigators, they had some real major concerns about the credibility of those end use certificates, because they are supposed to be an identification of people who get a hold of items that aren't supposed to ship it out of the country. If that material in those applications are false and there is no credibility to them, where do we go to identify these people that aren't supposed to ship the items?

So if you are talking about your black market, a black market is created when someone lies and disguises their identity and they have an opportunity to make money.

Mr. KUCINICH. That is exactly the point of my question. So what I am asking you, Mr. Chairman, you know, as this subcommittee's work seems to be growing here in leaps and bounds before our very eyes, maybe it is appropriate for this committee to ask for an audit of the end use certificates to see who has been applying for the ability to purchase Army surplus and to see if, in fact, they are legitimate and to see what has happened with what they have purchased. It may be very instructive.

And I think that certainly where the GAO report reads, "In instances where DOD required an end use certificate as a condition of sale, our undercover investigator was able to successfully defeat the screening process by submitting bogus documentation and providing plausible explanations for discrepancies and documentation." That, to me, is an open door to the black market, folks, and we need an audit on that.

Mr. Chairman, I guess my time is up at this point, but——

Mr. RYAN. Mr. Kucinich, in response to that, also at that meeting we had with law enforcement——

Mr. KUCINICH. We had what?

Mr. RYAN. In regards to the meeting we had with law enforcement with the DHS and the DOD, they indicated that they were going to try to reach out and try to get some data and try to do

some credibility checks to determine whether or not they are credible. So the intelligence group of DHS, Department of Homeland Security, was aware of the situation. We briefed them and they said they were going to try to do it, but I know that is not going to be a full audit like you are talking about. But the intelligence people at DHS were thinking on the same lines you were.

Mr. KUCINICH. Well, it is nice that they are thinking about it.

Mr. RYAN. Yes, sir.

Mr. KUCINICH. Mr. Chairman, thank you.

Mr. SHAYS. I am not usually at a loss for words, but I am getting close to it, because this is like, where do you begin. One of the thoughts that I was thinking is I wouldn't want your job, Mr. Estevez, for all the money in the world, or Mr. Peters. I wouldn't want it, because I have this sense that if it was easily solvable it would have been solved. And I have this sense that, because it is not easily solvable, we are not even trying to solve it. That may be unfair, but this is now the 4th year we have been at it.

I don't want to be unkind to any of you, but there is an outrage here and I don't feel the outrage. I feel, just in terms of looking at this equipment and thinking that if the all-band antenna is something we keep buying and we basically gave it away for $120,000, something really, really, really, really is serious. Then I think that if the F–14, I was thinking, well, there are some F–14s around somewhere. Someone may want it. And then I thought maybe you can convert the circuit board. And then I think, well, you have it.

Our enemy—they are our enemy. I hate to say it, but they are our enemy, and that is Iran. We don't have diplomatic relations with them. They have helped fund Hezbollah. They've helped train them. Their fingerprints are all over what has happened in the Middle East. And we have an embargo with F–14s, but they can come and get it for free. Well, maybe they have to pay the person who is buying it a tidy sum, but at least they, from their standpoint, get it.

I am smiling through my tears.

I guess the way I will begin is by asking you about the two reports. I mean, your report last year of May 2005, which we had the June hearing, there are 13 recommendations. Now, this report that you are doing, DOD Excess Property Control Breakdowns, there are not recommendations here, so, Mr. Kutz, tell me why.

Mr. KUTZ. Well, that was more of an investigation.

Mr. SHAYS. OK.

Mr. KUTZ. So it wasn't a full scope audit. We gave what we call a corrective action briefing after we had done the various operations, and we gave them our input at that point in time.

Mr. SHAYS. I am going to come back to the 13 recommendations, so this hearing is going to be a little longer than I would like and it is going to be a little tedius, because I am going to ask you about each of the recommendations. I am going to ask about where we are in those recommendations.

Should I make an assumption, Mr. Kutz, that we need to add to these 13 recommendations, or are these 13 recommendations probably still pretty operative?

Ms. Fischer, I am going to ask you. You are nodding your head. I am getting a little more life out of you than some others here.

Ms. FISCHER. Those recommendations are still operative. They have taken action on many of them, but the ones we are still concerned about are the ones that related to identifying systemic weaknesses that resulted in loss, theft, missing, sensitive military items, and the recommendation that they take a look at DRMO security and fix weaknesses there.

And then, with regard to their corrective action on their system so that they pull these A-condition, new, unused items back into the process instead of continuing to buy the same items, we think they haven't gone quite far enough in the action they took.

They met with us. They told us how they implemented the system fix in January and the interim fix prior to that, which they started last July, but we just haven't seen the money coming back.

When you look at the process, the screening process for——

Mr. SHAYS. Let me just interrupt you here. When you say the fix, what is this? Does this mean there are other things that should be added to your recommendations? This does not describe a fix to me.

Ms. FISCHER. What I meant was the recommendations on the systemic weaknesses for the stuff getting out and the DRMO security, those have not been addressed. Those recommendations are still open, they still stand. And as far as the reuse of new, unused items, they are treating those things the same in the process as they are items that need repair or junk. They have the same 14-day screening period and then they are out the door.

Mr. SHAYS. Let me just tell you, unfortunately, your knowledge, you are losing me right now.

Ms. FISCHER. I am sorry.

Mr. SHAYS. I am at baby steps here. You are taking big leaps and I am not there and neither is DOD there. I am going to just come back to this all-band antenna. If they paid $120,000 for it, Mr. Kutz, should they have been able to buy it outside?

Mr. KUTZ. We didn't buy that. That was something that we used our undercover operation.

Mr. SHAYS. So it was given?

Ms. FISCHER. That is a DRMO security issue.

Mr. SHAYS. Right. But it is a secure item that should not have been sold to the general public, correct?

Mr. KUTZ. Right. And it was in the excess property system.

Mr. SHAYS. Right. So we can have a question as to why it was excess when we are still buying it. We can have questions why it was free when it cost $120,000. And we can have a question about how the heck could anyone get it when this was military equipment that shouldn't have been sold to anyone.

Now, Mr. Estevez, do you agree that this should never have gotten in the hands of our investigators?

Mr. ESTEVEZ. Congressman Shays, it should not have gotten in the hands of your investigators, but let me be clear. This item was in a DRMS. They came into that DRMS.

Mr. SHAYS. Slow down. You are going to have as much time. Slower. This item was what?

Mr. ESTEVEZ. This item was in the excess property system. That means that it was not needed by the unit that held that item nor by that service to issue to any other unit when it was excessed into

the reutilization system. The GAO investigators, impersonating an Army user—let's be clear.

Mr. SHAYS. Right.

Mr. ESTEVEZ. They were not impersonating a private citizen or a Defense contractor. They were impersonating a valid Army user. They came in and requisitioned this item as a valid member of the military service, the contract support through that military service. Any item in the reutilization system is available to members of the military service. That is the point of having the system, so that we can reutilize that material across that service.

Mr. SHAYS. OK. So the story is terrible, but you are saying it is not as terrible.

Mr. ESTEVEZ. It is terrible that they were able to access the system and forge documents. We should have had a cross check on that. But once you accepted that validity, they were entitled to that item.

Mr. SHAYS. Mr. Estevez, we had at one time the Secretary of HEW under the previous administration, and they didn't move forward with what they were required to do with the safety of the blood supply when I was chairman of the Health Committee. She wouldn't have thought to come in here and in any way justify anything. She said we screwed up, this is what we are going to do, and this is when we are going to get it done. You know what? There were no stones thrown at her because she did it.

I need to be very clear about just this one item as a for example. Is it your testimony under oath before this subcommittee that this equipment was never to be sold outside the military, even as marked? Is it your testimony that this was viewed as excess throughout the military or just excess within that unit?

Mr. ESTEVEZ. Before that item should have been put in DRMS—and I would have to go back through the reutilization system——

Mr. SHAYS. Well, did you know that this item was going to be one of the items that was brought? Were you told about this item?

Mr. ESTEVEZ. Yes, sir.

Mr. SHAYS. It would have been helpful for you to find out.

Mr. ESTEVEZ. Yes.

Mr. PETERS. Congressman Shays, if I may——

Mr. SHAYS. Yes.

Mr. PETERS. This item is required to be demilitarized and destroyed if it is not reutilized, and it should not ever be made available to go through the entire reutilization transfer and donation process and made available to a public sale. It is a demil-controlled item that is required to be destroyed if it is, in fact, not used by our military.

Mr. SHAYS. Well, I hope to God we wouldn't destroy it, though, because we are still buying them.

Mr. ESTEVEZ. Congressman, we were not buying these items. The fact that we may have these items in inventory is not an indication that we are continuing to buy this item. Now, I can't say that we wouldn't in the future.

Mr. SHAYS. You know what? I feel like we are straining at gnats and swallowing camels here. I mean, I want to be fair to you because I don't think we need to, from this standpoint, make the story worse than it is because it is really bad. From my standpoint,

if I were thinking if I were you in your place, Mr. Estevez or Mr. Peters, my comment would be this is a huge example of lots of breakdowns in the system, to which we are trying to correct.

What my feeling would be if I were on that side of the table is this is where we are having success and this is where we are having failure. I feel like you are trying to make it seem like somehow there is nothing—you know, it is a problem but it is really not a problem. We just don't get it up here. I don't think that is to your value. I really don't.

We are told that we have an inventory of about 1,000-plus different computer systems that can't talk to each other. Mr. Estevez, that was not your problem. You never caused that. General, you never caused it. That is a problem you have to deal with. So in dealing with it, what we know is—and we have known this for a while—you have one department within one branch, you have a unit that has excess, and even within the same branch they may need it, they just don't know it is somewhere else. But then it is compounded because it may be even another branch, and, and, and. I mean, that part I get.

What I am not getting, and it has to be corrected, and you aren't going to be correct it over night, nor was President Clinton able to correct it and his people overnight, but I would at least like to know we have made some progress.

What I want to know is, is this an item that we are actively using, and the answer is yes. Is this an item that may be needed somewhere else within the military? Probably yes. Is this an item we may buy in the future? Probably yes. Therefore, I can see your argument if you said well, we found someone within the military that wants it, and we are going to make sure we get it. That part I get now, so there is a little sanity to this conversation.

But what raises huge story here, and Mr. Kutz, he could just comment on this one item and it would be a huge story. We don't know who you are. You don't exist. Well, you don't understand. There was identity theft, dah, dah, dah. If that part of the dialog is true, that, alone, is huge.

My red light is on here, but let me just pursue this and we will keep at it here.

Mr. Kutz, is it your testimony—and maybe someone could speak more directly rather than secondhand. Was this you, Mr. Ryan, that had this experience?

Mr. RYAN. I think in the situation of this antenna we were able to secure the antenna by doing an intrusion into the DRMO and getting possession of it.

Mr. SHAYS. Now, you did it pretending you were the military?

Mr. RYAN. We did it by being a contractor hired by the military working for the military, so I was not posing as a military——

Mr. SHAYS. Well, that raises an interesting question. Are we in a position where we are having to have contractors help the Army find their own equipment?

Mr. RYAN. Well, it appears in this particular case yes, because we basically were not identified until the second day by the person who was contracted by the Army to search for the property. They called——

Mr. SHAYS. You are the contractor. They don't think you exist, correct? This is the one where you don't exist?

Mr. RYAN. Actually——

Mr. SHAYS. I don't want to mix them up.

Mr. RYAN. We are, because what we have to do is to think about the intrusion into the DRMO as us providing totally bogus information.

Mr. SHAYS. Right.

Mr. RYAN. No one challenging us.

Mr. SHAYS. And that is not because you were GAO. I could have done the same thing.

Mr. RYAN. If you had put together a plan to pose as a contractor.

Mr. SHAYS. OK. So you did that. Just finish it out and then I am going to yield to the gentleman from Maryland. Keep moving here.

Mr. RYAN. So once we got the property, they contacted us and we told them it was a test. What we are talking about——

Mr. SHAYS. You told who it was a test?

Mr. RYAN. We told the contractor that when they contacted us—DLA never contacted us. We told them at the end of our——

Mr. SHAYS. Who is we?

Mr. RYAN. GAO.

Mr. SHAYS. And you told who?

Mr. RYAN. We told DCIS, Defense Criminal Investigative Service, and DLA that we had successfully penetrated the DRMOs and we were able to take possession of excess property that was demil.

Mr. SHAYS. Right. But before that wasn't there a call raising questions?

Mr. RYAN. There was a call by the contractor who was working on behalf of the Army screening property who realized that their company was being—this property was being charged to them as us taking it, and realized that they didn't have any screeners.

Mr. SHAYS. So you used somebody else, contractor, who was legitimate?

Mr. RYAN. Yes.

Mr. SHAYS. And so you used a legitimate contractor and the contractor was wondering what the heck is going on here, and then you told that contractor, not the military——

Mr. RYAN. Yes.

Mr. SHAYS [continuing]. That, in fact, this was identity, and the issue dropped, and the contractor didn't notify the military?

Mr. RYAN. Wasn't the identity. Identity issue was the end use certificate situation. That is primarily a purchase over the internet. The end use——

Mr. SHAYS. Let's stay with this story.

Mr. RYAN. OK. But the identity issue doesn't come into play in regards to securing the penetration into the DRMO. We just falsified everything.

Mr. SHAYS. You falsified everything, used a legitimate contractor as the person?

Mr. RYAN. Yes.

Mr. SHAYS. Eventually that contractor did find out about it. By then you had the equipment?

Mr. RYAN. Yes, that is true.

Mr. SHAYS. So you could have just disappeared?

Mr. RYAN. Absolutely, and if we wouldn't have given a legitimate telephone number as a call-back so we could monitor the activities, they would never know who we were.

Mr. SHAYS. Yes. I get it now.

Mr. RYAN. OK.

Mr. SHAYS. And you could have been an operation, a front for anyone?

Mr. RYAN. You are absolutely correct.

Mr. SHAYS. And had you taught me how to do it, I could have done it?

Mr. RYAN. Absolutely.

Mr. SHAYS. And when you went to DOD, they helped you load that on to——

Mr. RYAN. The agents that did the penetration, they got assistance from the people inside the DRMO to load the property on their truck.

Mr. SHAYS. And you were a contractor picking this up, so you didn't have military uniforms on or anything like that?

Mr. RYAN. No.

Mr. SHAYS. Nothing?

Mr. RYAN. Used a driver's license to get on the base.

Mr. SHAYS. OK. Well, I mean, it is astonishing. I mean, that is astonishing. That, alone, is an astonishing story. It is astonishing.

I thank the gentleman from Maryland. You have the floor.

Mr. VAN HOLLEN. Thank you, Mr. Chairman, for holding this hearing. As you and others have said, I am sure this subcommittee looks forward to the day that we get a report that the recommendations have been adopted and things have changed and, in fact, we are saving the taxpayer some money.

Mr. Kutz, I was just looking at your testimony from about a year ago in front of the subcommittee on some of the same issues. In your testimony then you found that there was about $3.5 billion in money essentially wasted from the taxpayers' perspective. Do you recall that testimony?

Mr. KUTZ. Yes.

Mr. VAN HOLLEN. OK. And, as I understand your testimony today, in this round you sort of tested the system and you have concluded that the 13 recommendations you have made have not been adopted; is that right?

Mr. KUTZ. No, there has been some progress, and I have mentioned in my opening statement they have reportedly saved $38 million through June of this year. But we believe that the potential is there for hundreds of millions of more savings.

Mr. VAN HOLLEN. OK. Do you have any reason to believe that, with the exception of the approximately $24 million——

Mr. KUTZ. That was $38 million.

Mr. VAN HOLLEN. The $38 million, that we are not continuing to lose $3.5 billion?

Mr. KUTZ. The $3.5 billion wasn't related necessarily just to the excess property system. The actual amount for the excess property system last year I believe was several hundred million dollars. And so the $3.5 billion related to items that were purchased and that were never used, but that was not really related directly to the ex-

cess property system, so that gets into the broader logistics issue at the Department of Defense.

Mr. VAN HOLLEN. OK. But as I understand the testimony from last year, you are talking about $4 billion related to items in new, unused, and excellent condition——

Mr. KUTZ. Yes.

Mr. VAN HOLLEN [continuing]. That were sold, and you say we determined that $3.5 billion, or 88 percent, included substantial waste and inefficiency because new, unused, and excellent condition items were being transferred or donated outside of DOD, sold on the internet for pennies on the dollar, or destroyed, rather than being reutilized.

Mr. KUTZ. Yes.

Mr. VAN HOLLEN. Do you recall that testimony?

Mr. KUTZ. Yes, that is correct.

Mr. VAN HOLLEN. And do you have any reason to believe there has been a significant change in the practices to avoid that?

Mr. KUTZ. Yes. Like Mr. Estevez, I think there has been some progress, but there is a lot more issues that need to be resolved.

Mr. VAN HOLLEN. All right. We can get into that in a moment, but, as Mr. Kucinich mentioned, I think that people following this are going to be just amazed to hear that, rather than take the principle I think most people were taught by their financial advisors or parents, which is you buy low and you sell high, DOD has just reversed it and done the opposite and they are selling low and buying high. The consequence is great losses it seems to me to the taxpayer.

I would point out that just last Friday the Army came out with a statement, the Army bearing most of the cost for the war in Iraq and Afghanistan, saying that its money crunch has gotten so bad it is clamping down on spending for travel, civilian hiring, and other expenses. We have to wonder, given the crunch that the Army is facing, whether or not we can't find savings through the kind of efficiencies that we are talking about here.

Let me just make sure I understand and get this straight in my mind. I do think specific examples are important to make it clear what is at stake here.

On page 31 of your current report you talked about a gasoline engine, and you say that GAO was able to buy the gasoline engine for $355. Do you recall that?

Mr. KUTZ. Yes, that is correct.

Mr. VAN HOLLEN. Now, it seems like a pretty simple item, a gasoline engine, but, of course, there are large quantities of gasoline engines being sold. As I understand, the same time you were buying these engines for a few hundred dollars, the military, in particular the Marine Corps, was buying these identical gasoline engines for $3,119; is that correct?

Mr. KUTZ. Yes, they got four of them from DLA in June 2006, is my understanding.

Mr. VAN HOLLEN. So the Marines are paying 10 times for the equipment what you were purchasing the equipment for; is that true?

Mr. KUTZ. That is correct.

Mr. VAN HOLLEN. And you also looked at purchases, I understand, of 20 more gasoline engines from the Internet?

Mr. KUTZ. At the same time we bought ours, there were another 20 or so available. We just picked one and bought it for about $350.

Mr. VAN HOLLEN. OK. And so on the internet, and the original acquisition cost, if you sort of add all that up, was $62,000, and the price on the internet was the same discount that you got, so it was approximately $6,221; is that right?

Mr. KUTZ. Yes.

Mr. VAN HOLLEN. So a tenth of the price, essentially.

Let me ask you, Mr. Estevez, I mean, these are concrete examples. I guess most people would ask the question all of us would ask: how come we can't seem to get a handle on this? And the reason I focus on a specific example is that it is there, they went out and did it. It was on the internet. What do we have to say?

Mr. ESTEVEZ. Congressman, we have put a number of fixes in place from the time of the last hearing, so that if we are going out to the commercial sector to buy material from a commercial vendor and that material has been put into the excess property system, we will offset the buy from the commercial sector against material that is in the excess property system so long as that material is in brand new contract. You know, there is a training factor in the process of turning in material from a unit that owns that material to ensure that they code it properly. We have reinforced that training. That remains an issue because it is a rotational assignment that is generally a junior grade.

Using that in the last year we have offset buys by $224 million, so we are, in fact, reusing material to the benefit of the American taxpayer and to the benefit of our military forces.

Items that go back into the excess property system that have been screened against the requirements of the military service, that have been sitting in that system for, I believe, 45 days, and then another period of time, and there is no requirement from the military service while that item is sitting in that system, depending on the condition code of that item, on whether they believe that is an item that they can use, you know, we would not—they have the opportunity to reuse that item.

That does not preclude them from ordering that item from the national inventory where we would stock that item and where we have the networks, in fact, set up so we can distribute that item to them in a cost effective, timely manner so that they can use that item to make a weapons system operate, which is the true cost savings for the Department of Defense, getting the return on the dollar investment in weapons platforms.

That is standard supply chain management practice. In that regard we do the same as a Wal-Mart or a Target or any industrial operation would do. Most of those folks would not take any item back into the inventory and put it back in their national stock system.

We continually do retention analysis, when we should be re-buying an item. We buy millions of buys a year. As our s yes, sirs become more sophisticated, as our ERP systems come online, and as the system that we manage the realization system gets modernized, we will probably have the ability to do better retention analy-

sis. But those are tough calculations. It is an ongoing process and in that regard I believe we are doing sound supply chain management.

Mr. VAN HOLLEN. Well, let me ask you. I am not sure I understood the full answer, but you are saying that you put some changes in place that would address the issue we just talked about, which I understand was within the last year, I understand.

Mr. ESTEVEZ. The beginning of this year we put a system fix in place so that if there is an item coded in brand new condition that is in the reutilization process at the time we are going out to the commercial sector to buy that same material, we will offset the buy by inducting the material that is in the reutilization process back into the national inventory and only buy the difference of those items.

Mr. VAN HOLLEN. All right. So, as I understand it, based on that testimony, this particular scenario we talked about with the gasoline engines should not have happened with the new system in place, assuming that the Marines were asking to purchase these engines at the same time the same engine was up for sale on the Internet?

Mr. ESTEVEZ. The Marines, in that scenario, we were not buying it from the commercial sector. The Marines were ordering it from items already in the existing inventory, so really they are paying a working capital fund, a transfer of dollars within the DOD. The DOD has already expended the true cost of that item out to the commercial sector to buy it, so it is not a matter of an O&M dollar into a working capital fund to repay the working capital fund.

Mr. VAN HOLLEN. Sure, but I guess the problem is—I mean, I understand what you are saying about inventory management, but obviously a gasoline engine is something that is a pretty common item. That is something I think you would expect to restock your inventory, and so, you know, just because they are buying it off the inventory shelf doesn't mean that is not a loss to the taxpayer because you can expect that you are going to have to buy it back from the original contractor for the same $3,000 level from the original supplier.

And so it would seem to me that, especially for items that are in common use and where you have a pretty reasonable expectation that there is going to be a need for them in the future, we wouldn't put them up and sell them, as GAO said in its report last year, for pennies on the dollar when we know we are going to have to buy that some time down the road. I really hope that when we have this hearing next year there won't be any more examples like the kind we heard about here.

Mr. ESTEVEZ. I would like to say that. We want to make full use of our inventory, and at that point it goes down to how much inventory do we want to hold. So if it is in brand new condition and we believe there is a use case for it, we need to determine what inventory we should be inducting back into the national system, which is not the norm, based on the retention rate of that item and what the use case of that item is, the demand against that item. We continually have to do that.

It goes back to Congressman Shays' point about our systems not being fully interconnected. But as our systems mature, we modern-

ize the RP systems that we are putting in place, and as the system that we are upgrading our reutilization process comes into place, we should be able to do that better than we are doing that today, Congressman.

Mr. KUTZ. Congressman, the waste there goes back to the beginning of the process when someone actually decided in the 1990's to buy all these engines and, as it turns out, nobody was going to use them, which is a different problem than what Mr. Estevez is dealing with here.

Mr. VAN HOLLEN. Right. And I don't know, based on this testimony, how many engines were in the inventory, but I——

Mr. KUTZ. I am told 1,500.

Mr. VAN HOLLEN. So 1,500 was the total, but, I mean, I would suspect that you are right, the problem of over-buying up front, but especially with an item that is likely to be needed some day in the future, even though there is no an immediate demand for it, it seems to me it probably makes more sense to retain it in the inventory, if there is an expectation you are going to use it, then to sell it really literally pennies on the dollar, 10 percent, and then go back and have to order another one at taxpayer expense.

Thank you, Mr. Chairman. Thank you for the testimony.

Mr. SHAYS. I thank the gentleman.

We still have a number of questions we need to ask. I just need you to know that.

I want to start by asking each of our three folks from DOD which of these items is most discomforting to you that it is out there as an example that people, our investigators, could get. Which one? Take your pick. Which is the one, Mr. Peters, that you find the most disconcerting up there?

Mr. PETERS. Congressman Shays, it is disturbing that any of these items would ever go through the reutilization, transfer, and donation cycle and then be made available to public sale. They reflected a breakdown in the procedures. They also reflect some inherent risks in the disposal process. Changing or reengineering the process to control batch lotting and local stock number items which represent 44 percent of the annual workload that DRMS handles, that is a tremendous amount of the annual workload that we really need to close the gaps and the vulnerabilities inherent with that batch lotting process.

Many of items that are in front of us that the GAO bought were observed or obtained, came out of batch lots. Many of these other items were——

Mr. SHAYS. Now let me just speak about batch lots. I was going to get to it. In our hearing last year, in June 7, 2005, Mr. O'Donnell, who was your predecessor—is that correct, Mr. Peters?

Mr. PETERS. Yes.

Mr. SHAYS. OK. He said, "We no longer accept batch lots. All of the items that are now turned in in J-list are reviewed at those sites. They make the determination if they are serviceable for reutilization." Was that a correct statement?

Mr. PETERS. Congressman, I believe that Colonel O'Donnell was referring to biological and chemical items when he made that statement.

Mr. SHAYS. Right.

Mr. PETERS. When I talk about batch lotting, I am talking about the total volume of items that entered the disposal system through the batch lot process, which is much broader, and we need to re-engineer and transform that process, and we can do that by establishing multiple check points.

Mr. SHAYS. Why don't you talk about batch lots. Explain what batch lots are.

Mr. PETERS. Batch lots is a methodology that exists in the disposal system whereby DRMS tries to minimize the handling, the cost, and the administrative time to process an excess item through the disposal system. Because it includes 44 percent of the annual workload, that is over 1.2 million line items——

Mr. SHAYS. So you combine a lot of things together?

Mr. PETERS. You combine a lot of things together.

Mr. SHAYS. And someone buys this batch, and they may like some of the items and they may not like some of the items, but in the end, for a relatively small amount of money, someone is able to purchase a batch of items; is that correct?

Mr. PETERS. If a batch goes through the entire process, it would be available for public sale, and the risk of the batch lotting, sir, is that once an item goes into a batch we lose the identity and the visibility of that individual item, which is why we need to change the process dramatically and——

Mr. SHAYS. We will come to that.

Mr. Kutz, did you buy or did your investigators buy any of these in a batch lot?

Mr. KUTZ. Yes. Several of them were batch lots, several of them weren't on that side.

Mr. SHAYS. OK. And does everything on this side to my right, your left, represent military sensitive?

Mr. KUTZ. Yes, everything on this half of the room. Some of it we got in that operation where we were posing as contractors, the other we bought on the internet.

Mr. SHAYS. OK. And not posing as military?

Mr. KUTZ. Correct, posing as a private citizen with a credit card.

Mr. SHAYS. So what did you get as a private citizen as opposed to—and if someone else needs to answer, that is fine, but what did you get here not posing as military connected?

Mr. KUTZ. Well, like the ceramic body armor, which is current issue. That was in a batch lot.

Mr. SHAYS. OK. Any other item?

Mr. RYAN. The F–14 parts.

Mr. SHAYS. The F–14 parts?

Mr. RYAN. The F–14 parts.

Mr. SHAYS. So that was in a batch lot?

Mr. RYAN. Yes. I think it is important also to recognize that in the batch lots some of these batch lots were prepared by the contractor that DOD has actually hired for these sales.

Mr. SHAYS. Say that one more time.

Mr. RYAN. DOD has a contract with Government Liquidators to provide assistance of the sale of——

Mr. SHAYS. And so they assemble the batches?

Mr. RYAN. It appears that, based on talking to some GL people, yes, they do assemble batches for sale.

Mr. SHAYS. So let me ask you this, Mr. Peters or Mr. Estevez or the General, whoever can answer this. It is my understanding that you have taken away leave for some of our personnel to go through batches to determine whether or not there is military sensitive equipment in various batches; is that correct?

Mr. PETERS. Congressman, once we became aware of the operation by the investigation by the GAO, we immediately froze all the batch lots that were in the inventory and we began to recertify each individual item and its demil code. There were 9,000 batch lots that were in the system that we froze and have been in the process, over the last 6 weeks, of recertifying each item.

The principle of inspecting each item in the batch lot is a sound action that needs to take, and that is part of the reengineering of the batch lotting process in the future. If we centralize and consolidate all of the batch lots into four sites, for example, here in the United States, we can take the more experienced subject matter experts in the disposal system, physically inspect each of those items, verify their demil code, and verify those items that are appropriate to move on through to the sale phase of the disposal system.

We can do that at the time we break down the batch and we can do that again prior to the sale of the item, and that will significantly reduce the kinds of items that we see in front of us of progressing through the system inappropriately.

Mr. SHAYS. And so in the process of doing this have you been finding any military sensitive equipment in those batches?

Mr. PETERS. Yes, sir, we have.

Mr. SHAYS. Good. So that is a positive step?

Mr. PETERS. I believe it is the right step in the short term, and I believe that is the basis of a sound reengineering of the batch lots process for the long term.

Mr. SHAYS. Well, Mr. Peters, you gave me a general answer, and that is probably a good one, but I am asking for you to tell me which is the one you find most awkward in all of these. Is it seeing something transferred for nothing that cost $120,000, or is it seeing potentially a hand-held missile launcher? Is that the thing that you find most unsettling? Which one is the one that you find most unsettling here?

Mr. PETERS. Sir, DRMS has a responsibility to execute this——

Mr. SHAYS. I am asking you a question. I want to know which one you found most disconcerting here.

Mr. PETERS. And my discomfort is that any of these items——

Mr. SHAYS. I know that, but now take your pick, boss. Which one?

Mr. PETERS. Any item that is demilitarized and should be controlled——

Mr. SHAYS. Mr. Peters, that is not what I asked. Which one of these do you find most unsettling?

Mr. PETERS. Congressman, all of these items I find disturbing that they've gone through the system——

Mr. SHAYS. So you would equate one of these small items to one of the bigger? Are they all the same to you? They are all the same?

Mr. PETERS. Any of these items that have been determined that should not be made available to——

Mr. SHAYS. Mr. Peters, I am going to say it again and I want you to listen to the question. You can go on record, but I want to make sure that I understand. There are some items here that strike me as not as significant as others. Which do you think is the most significant item that never, ever should have gotten out of military hands?

Mr. PETERS. Any item that is directly related to a weapons system——

Mr. SHAYS. Mr. Peters, forget it.

Mr. PETERS [continuing]. Is most disturbing.

Mr. SHAYS. That is a very uncooperative response. I can't believe that you would equate them all together, and if that is the way you want it to be you are on record that way, but all that says to me is you choose not to be cooperative.

General, which is the one you found most unsettling?

General WILLIAMS. Sir, I found the SAPI to be the most unsettling.

Mr. SHAYS. Which one?

General WILLIAMS. The Small Arms Protective Inserts.

Mr. SHAYS. OK. Thank you, sir.

Mr. Estevez.

Mr. ESTEVEZ. Congressman, I also find the small arms protective insert extremely unsettling because they are easily identifiable for what they are.

Mr. SHAYS. Thank you, sir.

Mr. Kutz, what would you find?

Mr. KUTZ. In addition to those, the micro circuits that are part of the F–14.

Mr. SHAYS. Thank you.

Ms. Fischer.

Ms. FISCHER. I think the F–14 weapons system parts.

Mr. SHAYS. Thank you.

Mr. Ryan.

Mr. RYAN. I also agree the F–14s. The parts that the law enforcement officers on the street are chasing all the time, there is no reason that they should be out there. We have law enforcement, DOD, and DHS chasing down people that have possession of those. We could be using their manpower in other ways.

Mr. SHAYS. Mr. Peters, do you want another crack?

Mr. PETERS. Sir, I agree that the F–14 parts, because of the one Nation in the world that continues to fly that and the SAPI armor plats which clearly should never have gone through the process, those are obvious examples of things that are disturbing, but all of——

Mr. SHAYS. Thank you. I understand. I understand. Thank you.

I am going to have you ask a few. I am going to ask professional staff to ask a few questions.

Mr. CHASE. Mr. Kutz, during your opening oral statement you did make reference to social engineering techniques. Could you just for the record define what you mean by that?

Mr. KUTZ. Yes. It is really a ruse or a trick or a con is kind of the way you would describe it, where you exploit people who are trusting and you utilize that to either penetrate systems or get them to do something that they wouldn't normally do. I think the

end use certificate example is one where we told them it was identity theft and they believed it, and, using the contractor identifications we looked like contractors, we talked like contractors, we had a few pieces of paper that made us appear to be contractors, and we were able to get items out of the DRMS location.

Mr. CHASE. OK. As a followup to that then could you please tell us what the end use certificate is?

Mr. KUTZ. It is a certificate that is supposed to provide some legitimacy to who is actually buying items that are trade security controlled, and so, to the extent that we were able to get that using a person that doesn't exist—and they did have red flags. They said you don't exist and, again, I think someone should have probably asked the next question about we said it was identity theft, well, why do you still not exist. I mean, if it is identity theft you would still exist probably. So I think that is something like what Mr. Ryan said, possibly a more experienced person asking those questions would be useful.

Mr. CHASE. So then I think the first time you were able to break the end use certificate was in 2003.

Mr. KUTZ. Yes.

Mr. CHASE. And you were able to do it again in 2006?

Mr. KUTZ. Yes. I think it was harder this time because I think they actually checked our background. The first time I don't believe that they checked our background. So they have enhanced their procedures, and I think that, again, we were able to beat those procedures with, again, social engineering this time, so they had the right information in front of them, they just didn't effectively utilize it.

Mr. SHAYS. OK. Then to any of our DOD witnesses, what change have you made any changes to the procedure for identifying end use certificates between 2003 and 2006, or is that an ongoing process?

Mr. PETERS. Sir, it is an ongoing process; however, we access additional data bases now than we did in the earlier years. The trade security control process to verify an end use certificate is designed to verify the identity and the stated purpose of the acquisition. It does not eliminate the risk; it is a risk mitigation procedure.

Mr. SHAYS. I am just going to interrupt a second to make sure, while the staff is asking these questions, Mr. Kutz, do you have your 13 recommendations? Do we need to give them? Do you have someone here who has the 13 recommendations?

Mr. KUTZ. Yes, we have them here.

Mr. SHAYS. Yes. I want to make sure. What I will be asking you—I want to give you a little time—give me the ones you think are the most important, not whether you think they have done them or not but what you think. Pick out of the 13, I am going to ask you to pick out half that you think are very important.

I just want to ask if Mr. Estevez, Mr. Peters, or the General, you have those recommendations and would be able to respond to them. Do you have that, Mr. Estevez? Do you have those 13 recommendations? I have a copy up here if we need one in writing.

Ms. Fischer, do you have those?

Ms. FISCHER. Yes.

Mr. SHAYS. Do you have an extra copy that we could make sure—anybody else have them?

Mr. KUTZ. We have one.

Mr. SHAYS. Could I just ask staff to bring those down. I would mark them, and we will give them to all of you.

The purpose is to just get a sense of where we are from last time around. I am not going to ask them right now. I am going to go back and ask professional staff to ask some questions.

Ms. Fischer, why don't you mark them in case Mr. Kutz is asked questions. Who do you want to direct your questions to? General Williams, we are going to be asking you some questions.

Mr. CHASE. General, in your written testimony—I may have missed it if you mentioned it in your oral testimony—you have the term the DEMIL challenge program.

General WILLIAMS. DEMIL what, sir?

Mr. CHASE. Challenge program.

General WILLIAMS. Roger.

Mr. CHASE. OK. Can you tell me, if we have this program, why is the program failing to catch items that are miscoded?

General WILLIAMS. Well, sir, when you view current processes and procedures there are seams and gaps that have been clearly identified by GAO, and I agree with GAO findings. So the next step is to accept accountability, to make sure that you understand the problem, and then to implement fundamental changes.

For example, the SAPI plate that I referred to, the SAPI plate is clearly a demil item, No. 1. We all agree to that. No. 2, the problem was that it was inadvertently, through human error, or classified as a mistake, placed in a batch lot. We have gone through that particular process.

That batch lot was eventually transferred over to GAO, therefore you have a demil item now available for sale to the general public in a batch lot.

So when we take a holistic view of current processes and procedures—and I will have to say that there has been tremendous progress to date but not enough—when you look at that, the question is how do you prevent that from happening.

First of all, leadership, accountability, then ensuring, through centralizing this program process at some localized level, that we take one final look at batch lots before we hand the particular batch lots over to GL.

So what I am saying is we accept the accountability and the responsibility; therefore, when GL receives an item, that item clearly is not a demil item.

By the way, if something changes and all of the sudden it becomes a demil item, then GL turns the item back. But I will tell you again another fundamental change are the weekly and monthly review of everything that GL has in its inventory to make sure that through some change or some mistake demil items don't exist.

Mr. CHASE. OK. You check it at your end to ensure that demil items aren't going out. Shouldn't the contractor also be checking? You indicated the contractor was checking. If you have two systems checking, why do we still have this problem?

General WILLIAMS. Again, sir, if you will, check, check, check. What we are having here, if I go back to the SAPI plate again,

clearly in a batch lot and it shouldn't have been. At that particular point in time, when we implement our new system of centralized control and a final check, we break apart those batch lots, and then the intent is that we will mitigate the intent by catching this particular item before we transfer it over to GL.

Mr. CHASE. OK. One last question. Why doesn't DOD set a minimum price for items that legitimately can go out for sale to the public? Looking at the Web site, it appears that there is a minimum constantly set at $35, or have I misinterpreted the Web site? Why doesn't DOD—as an example, I think someone mentioned the gasoline engine. Why don't you set a minimum price of $500? I mean, why is everything set at a minimum price of $35?

General WILLIAMS. Sir, good question, but I will have to defer that because I am not knowledgeable enough to answer that particular question.

Mr. CHASE. OK. Could you get back to the committee with that?

General WILLIAMS. Yes, sir, I absolutely can.

[The information referred to follows:]

Hearing Date: July 25, 2006

Committee: House Government Reform
Member: Mr. Kucinich
Question #1

DOD EXCESS PROPERTY: Inventory Control Breakdowns Present a Security Risk

Question: Who has the list of everything that is being sold army surplus? I mean, you showed missile launchers. Are missiles being sold army surplus? You showed parts from an F-14. Are planes being sold army surplus? You showed radar guidance. Who has the list of what is being sold army surplus? We don't really know what we're talking about here if we don't -- I mean, we have to define what we're talking about. What's for sale? Does anyone know? Does anyone have a list?

Answer:
DRMS has visibility of all excess property turned in by the Military Services that flows through its system as an item.

As agreed to during the hearing, we are providing the list of items that have been sold, transferred, donated and reutilized through the excess property system managed by DRMS.

Due to the large volume of items DRMS processes annually, we are providing a CD and not a printed list. The enclosed CD contains items that were issued through the Reutilization, Transfer, Donation or Sales programs. The following is a brief definition of those programs:

- Reutilization – items offered for reuse to agencies within the Department of Defense and other authorized programs. Examples of other authorized programs include the Law Enforcement Support Organization (LESO) and service museums.

- Transfer – items offered for reuse by Federal agencies (all Federal agencies are considered transfer customers).

- Donation – items offered for reuse through the State Agencies for Surplus Property (SASPs). Examples of organizations eligible to receive property under this program include hospitals, schools and clinics.

- Sale – Property that cannot be Reutilized, Transferred, or Donated, that is eligible for release to the public, is offered for sale either directly to the public or through a DRMS Commercial Venture partner (currently Government Liquidation, LLC). Property not authorized for release is destroyed.

The time period of the data on the CD is the last ten months (Oct-Jul) of Fiscal Year 2006.

Hearing Date: July 25, 2006

Committee: House Government Reform
Professional Staff Member: Mr. Chase
Question #2

DOD EXCESS PROPERTY: Inventory Control Breakdowns Present a Security Risk

Question: Why doesn't DOD set a minimum price for items that legitimately can go up for sale to the public? Looking at the Web site, it appears that there is a minimum price constantly set at $35. Or have I misinterpreted the Web site? ...why is everything set at a minimum price of $35?

Answer:

DOD Response: Property no longer needed by DOD and not desired by another Federal Agency or a donation customer is sold to the DOD's Commercial Venture Partner – Government Liquidation (GL). At this point it is no longer DOD property and saves the Government the costs of warehousing unneeded inventory. GL uses on-line auctions with a $50.00 minimum bid requirement which they have determined is the best business practice for reselling this type of property. The minimum bid requirement is set to cover expenses to receive, process, and resell property and was changed from $35 to $50 about a year ago. GL anticipates that each item offered is valued no lower than their minimum bid requirement, therefore, bids begin at that price. Their property is sold via an auction, not as a retail sale with a specific price tag attached. The minimum bid in and of itself doesn't establish the market value – the bidding process does. Setting a minimum bid higher than the market value will result in some items not being sold. Items which are not sold will continue to incur storage costs and will incur further cost to re-offer. GL could also choose to scrap the property rather than continue to incur those additional costs on property whose value as deemed by the market is not sufficient to place the minimum bid.

Mr. CHASE. And, finally, what procedures does DOD have in place to recover items that have been inadvertently sold to the general public?

General WILLIAMS. Sir, once we find out that items have been inadvertently sold to the general public, the contractor agreement is that we will make all efforts to regain those particular items, going back to the buyer, saying that this is a demil item that should not be in their control, and we need to recover that particular item from you.

Mr. RYAN. I would like to add to the General's situation. In talking to law enforcement, there seems to be some legislative help that is needed in the law enforcement community because once the ownership of the property is transferred on a sale, it is hard for the Government to actually go back and request that item back. There has been at least three or four attempts to try to get some legislative help to change to try to recover those items from a law enforcement perspective.

Mr. CHASE. When was this legislation offered?

Mr. RYAN. I can get the specifics on it, but that was at the briefing that law enforcement gave us a few weeks back. I can get you the history on that.

Mr. CHASE. OK. Thank you.

[The information referred to follows:]

Attempts were made in the National Defense Authorization Acts for Fiscal Years 2001, 2002, and 2004 to amend title 10 of the U.S. Code by inserting a new section authorizing the return of significant military equipment (e.g., equipment designated by the Department of Defense as requiring demilitarization) to the United States government. In this regard, Section 361 of the Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001 (H.R. 4205 RH) provided the following language to be inserted: "*When the Secretary of Defense requires the return of significant military equipment for demilitarization by the Government, the Secretary shall bear all costs to transport and demilitarize the equipment. If the person in possession of the significant military equipment obtained the property in the manner authorized by law or regulation and the Secretary determines that the cost to demilitarize and return the property to the person is prohibitive, the Secretary shall reimburse the person for the purchase cost of the property and for the reasonable transportation costs incurred by the person to purchase the equipment.*" Similar language was included in bills (section 921 of S.1155 IS and section 921 of H.R. 2586 IH) that were introduced in the Senate and House in the 107th Congress. In addition, similar language was included in bills (section 1047 of S. 747 IS and section 1044 of H.R. 1588 IH) that were introduced in the 108th Congress. Based on our review and information obtained from the Defense Logistics Agency, title 10 of the United States Code was not amended to include such language regarding the return of sensitive equipment.

Mr. SHAYS. I am going to say something I have said before, but I do want to say it again. I know this problem wasn't caused by any of you. I know this problem has existed for decades. But it is still stunning to see what we still fail to deal with, and, you know, Mr. Kutz kind of took my breath away when he said the Department of Homeland Security is saying we are trying to track some of the stuff that DOD has sold.

Could I appreciate, Mr. Kutz, that besides the Department of Homeland Security that FBI would be involved in this process? Mr. Ryan.

Mr. RYAN. In the briefing that we had with law enforcement, law enforcement across the board is looking at this issue.

Mr. SHAYS. So not just Homeland Security?

Mr. RYAN. Not just Homeland. We know that the jurisdiction over the exporting and importing of particular items goes to Homeland Security ICE, so they have been taking the lead with DOD.

Mr. SHAYS. OK. Now, have you told the subcommittee this before or are you sharing this today as you realized it might be of interest to us?

Mr. KUTZ. Well, it was a meeting just several weeks ago, so it is new. We have coordinated with them before. We actually coordinated with people after we had the hearing on the biological equipment. You may recall we did investigations and saw that was being shipped out of the country, so we had a number of case studies we followed then, and we did a referral then to some of the same people for those items.

Mr. SHAYS. I am going to ask our subcommittee to have the same kind of dialog that you had, and if you would supply the folks that were in contact with you, and we will invite you, Mr. Estevez or Mr. Peters, to participate in that so we kind of share this information.

Mr. KUTZ. And we do a referral, too. With respect to the cases here, I mentioned the other buyers and the over 2,600 items. We are referring those to the same group, and we have already sent those letters several days ago.

Mr. SHAYS. You know, I was thinking that, as you mentioned, Mr. Estevez, I think you did, you mentioned that auctions give you a pretty good market price, but auctions do, provided everyone knows about the auctions, and I am struck with the fact that if the general public were involved, there may be a lot more people who would be in the market to buy. I am not talking about the military sensitive equipment, I am talking in concept about price.

I guess having it on the Internet, there is logic to that. More people get involved. The key is on the Internet you want to make sure there is no military sensitive equipment, and there was testimony, Mr. Kutz, that you got some of military sensitive equipment from the internet, but that was batched items; is that correct?

Mr. KUTZ. No, not always. No. There were other items that went out.

Mr. SHAYS. So items that were pretty obvious then as military sensitive were not kind of stuck in between something that wasn't so obvious?

Mr. KUTZ. Correct.

Mr. SHAYS. OK. So that is pretty disappointing.

Let's take what you think, Mr. Kutz, are your key recommendations of the 13. I can't emphasize enough this is to understand where we are at along this process.

Mr. KUTZ. I am going to let Ms. Fischer answer that, but there are two parts. We want to first of all tell you which ones have been implemented, and then of the ones that remain there are several——

Mr. SHAYS. No. Let me just tell you this. No. I want to know which ones you think are the most important.

Mr. KUTZ. OK. The ones that are unimplemented.

Mr. SHAYS. Not the ones that haven't or the ones that have, which are the most important. And let's just see, of the ones that are most important, let's just get a sense of where they are at. I know you will be very fair as to your assessment of whether you think they are part of the way there, all of the way there, or not there at all.

Mr. KUTZ. OK.

Mr. SHAYS. OK, Ms. Fischer, you have the floor.

Ms. FISCHER. Recommendation No. 7 was to direct DLA and DRMS to review daily supply depot and DRMO excess property loss reports and identify systemic weaknesses and take immediate and appropriate corrective actions to resolve it.

Mr. SHAYS. OK. That is the most important. Now, why don't you—is anyone, Mr. Estevez or Mr. Peters or General—Mr. Estevez, I understand you have worked for the Department now for 6 months in this position? Mr. Peters.

Mr. PETERS. Yes. I have been in this position since February.

Mr. SHAYS. OK. And is this a recommendation that is new to you or have you seen these recommendations before?

Mr. PETERS. I have seen these recommendations before.

Mr. SHAYS. OK. Which one or who wants to respond to that?

Mr. PETERS. Sir, I will respond.

Mr. SHAYS. OK. Thank you, Mr. Peters.

Mr. PETERS. OK. For recommendation seven, since I have arrived I can tell you that we have initiated an internal review to identify the vulnerabilities and gaps in the DRMS processes. Prior to my arrival, over the last couple of responses to the hearings, DRMS and DLA were engaged with looking at weaknesses in the controls associated with biological and chemical items and laboratory equipment.

Even though those were responses to specific findings, if you will, it provided an important foundation for us to be able to look at the entire process from the moment that the DRMS receives an item to the disposition of that item, to really understand what are the vulnerabilities of gaps and receiving and issuance and processing through the sales process.

We have begun that review and we are assessing corrective actions to those vulnerabilities and gaps, and over the future months we will begin to implement those.

Mr. SHAYS. How far along do you think you are in that process? Are you at the point of identifying them, not necessarily stopping them?

Mr. PETERS. That is correct, sir.

Mr. SHAYS. OK. So that would explain what we are seeing here, in part.

Mr. PETERS. The vulnerabilities, the gaps that have been identified are certainly contributors to a breakdown in the procedures and the inherent risks in that process.

Mr. SHAYS. General, would you want to speak to that, or Mr. Estevez?

General WILLIAMS. Sir, again, I emphasize a holistic view of the current processes and procedures——

Mr. SHAYS. We are talking about recommendation No. 7.

General WILLIAMS. Yes, sir. And the seams and gaps where the vulnerabilities lie, which create the problem that is in front of us right now.

Mr. SHAYS. Mr. Estevez.

Mr. ESTEVEZ. Congressman, the other thing we have done to address that is we have significantly changed the structure of the reutilization and marketing process. We replaced a military officer, a colonel, with a career Senior Executive at the leadership level of that in order to drive this change, and we have significantly changed the structure of the organization, so we have moved down from 68 sites to 18 sites, where we are better able to implement internal controls and to monitor those.

Mr. SHAYS. So we have gone from 68 to 18 during a period of what time? I mean, are we at 18 now?

Mr. PETERS. Yes, sir, we are at 18 now. We just finished that.

Mr. SHAYS. Six months ago how many did we have?

Mr. PETERS. Six months ago there were 68 operating warehousing sites around the country.

Mr. SHAYS. OK.

Mr. PETERS. During the course of March through July, we began the transition to the 18 fully operational warehouses.

Mr. SHAYS. Is this that aspect where the claim is that $34 million has been saved, or is that another issue?

Mr. PETERS. I can't address that, sir.

Mr. SHAYS. OK. Mr. Kutz or any of your staff, what is your response to what you are hearing about this?

Mr. KUTZ. I think fewer locations will be conducive to stronger internal controls, and sustained leadership has been an issue here before, and I think that the sustained career leadership of a Senior Executive is important.

Mr. SHAYS. With no disrespect to our uniformed military, is the concept that someone who is in the private sector might have been involved in this type of work for 10 or 20 years, whereas a career military—I mean, General, you have had lots of different responsibilities, so you have to have lots of skills. Is the concept that you are looking for someone who may have dedicated their lives, someone from Wal-Mart, someone from K-Mart or somewhere else who has inventory experience? Is that the logic of saying non-military?

General WILLIAMS. No, sir.

Mr. SHAYS. OK.

General WILLIAMS. If we had the GO billets available easily we could have placed a GO in that particular billet because of the leadership that individual brings to that particular job.

Mr. SHAYS. Right.

General WILLIAMS. Mr. Peters, by trade, is not a DRMS trained individual.

Mr. SHAYS. Right.

General WILLIAMS. What he brings, though, is the savvy, the leadership skills, the ability to identify, to do the analysis, and then quickly come to a conclusion and execute the standard. So it is the leadership that we want, and what we have done in DLA——

Mr. SHAYS. But don't you want experience, as well?

General WILLIAMS. Yes, sir.

Mr. SHAYS. OK.

General WILLIAMS. But, sir, you know, leaders have that experience once you identify the problem. And so we made the choice to reengineer within the Agency, to place an SES position there because of what that position brings to bear. So we have the leadership in place now that we want, and I consider this a significant move.

Mr. SHAYS. I am just going to react. It seems to me if someone is trained in artillery and that is their basic, training, where if someone has gone to business school to learn how to control inventory, I will take the inventory over someone who has necessarily been trained on artillery when we are taking about inventory control. I mean, intuitively it strikes me that there is logic to that.

I am not saying that you don't want a command officer heading the Department, but it seems to me you need those skills in the unit.

General WILLIAMS. Yes, sir, I concur, but I will tell you—and I will have Mr. Peters speak for himself—we looked at his skill sets prior to hiring him to elevating him to the position of SES. He is a trained auditor. In terms of business acumen, he is right where he need to be. Already, sir, his leadership there has been a definite impact to that particular mission.

Mr. SHAYS. Thank you.

Mr. Estevez, any comment about recommendation seven? If you don't have a comment, that is all right.

Mr. ESTEVEZ. Again, I raise the issue that we significantly changed the organization in terms of leadership.

Mr. SHAYS. I am sorry, you did. I apologize, Mr. Estevez.

Ms. Fischer, what would be another item?

Ms. FISCHER. Recommendation No. 8: direct DRMS to take immediate appropriate action to resolve identified, uncorrected DRMO security weaknesses. DRMO security weaknesses are what allowed us to do the penetration at the two east coast DRMOs.

Mr. SHAYS. So we have really spoken to this, correct, or not, Mr. Peters?

Mr. PETERS. We have spoken the it from a process view, and there were also physical security recommendations made in prior hearings, and we have allocated moneys to address those physical weaknesses.

Mr. SHAYS. Your comment, Mr. Kutz? Do you think there is progress? Are you hopeful? Or is the jury still out?

Mr. KUTZ. Well, I think, again, there has been some progress. We haven't tested the entire area in that.

Mr. SHAYS. OK.

Mr. KUTZ. I mean, this was more of a limited investigation. The only real physical penetration test we did, that was what we got.

Ms. FISCHER. They focused on the structural weaknesses and some of the capacity weaknesses last year, stuff being stored outside that got weather damaged. I believe they corrected that problem. The leaky roof at one of the DRMOs that let items inside become wet and unusable, that has been addressed. But the things we are talking about that allowed us to do the DRMO penetration are new and those have not been addressed.

Mr. SHAYS. OK. Fair enough.

I make an assumption, as you reduce the number of facilities you have improved the facilities that exist, the ones that remain?

Mr. PETERS. Yes, sir, and we have also identified site improvements that need to be made at those facilities. We have prioritized them in accordance with our fiscal year 2006 and through the outyear POM dollars.

Mr. SHAYS. Let me do this. Let me just go through one more recommendation, then let me go to Mr. Platts, who on the full committee specializes on the whole issue of management controls and so on.

So what would be the third item that you would raise as an important item, not one that they have missed or failed to deal with, but that you just think it is important.

Ms. FISCHER. Yes. It would be the waste and inefficiency.

Mr. SHAYS. Which one?

Ms. FISCHER. Primarily recommendation 13, and it deals with the system changes implemented in January 2006. The recommendation says: require that DLA's BSM system design include adequate controls that would reject the purchase transaction or generate an exception report when A-condition excess items are available but are not selected for reutilization at the time purchases are made.

They have implemented a change in the system that lets them pull in A-condition items from the excess inventory if somebody is placing an order with DLA at the time or they need to replenish inventory levels, but they are still working against that 2-week or 1-month period in the excess inventory pipeline before they move it to sale. That is why, with the gasoline engines, we paid $355 in March and the Marine Corps came along in June and paid more than $3,000 for those same gas engines. They are not holding the A-condition items for a longer period than they are the items needing repair or the items that are essentially junk.

Mr. SHAYS. I would like the professional staff to just followup with that.

Mr. CHASE. Would you have a recommendation on a longer wait time?

Ms. FISCHER. We have suggested that to them once we saw what the January system fix encompassed and that the dollar savings weren't what we expected to see. We went back and looked and we said, well, maybe you need to hold these A-condition items a little longer to assure that they are reutilized.

Mr. SHAYS. Just then, to have you respond to that item, I was trying to filibuster to give you guys time to think about it.

Mr. PETERS. Congressman, when BSM release 2.2 was implemented in January. The period between January and May, the amount of reutilized material was low. What we have done in the month of June was DLA increased the scan, if you will, of the BSM system of the disposal inventory, and the results during the month of June exceeded what we incurred in the legacy system prior to the release of BSM 2.2. In the last 5 months since that release, there have been about approximately $1.2 million of acquisition cost of reutilization through the BSM, and the bulk of that has come during the month of June when we changed the cycle.

Mr. SHAYS. OK.

Mr. PETERS. Now, that doesn't address the issue of extending the holding period for A-conditioned assets, but it was a good step forward to maximize reuse of the property within that time constraint.

Mr. SHAYS. Thank you.

I am going to go to Mr. Platts, but I just want to tell you, Ms. Fischer, I would like to know three other items, so we can tell DOD so they can look at them. Have you got those three items? Just give me the numbers. Did you only pick out three?

Ms. FISCHER. Well, I picked out three because those were of most concern to us.

Mr. SHAYS. Fair enough. OK. I am going to ask you three more. You can look at them, so you have time to look at them. If you want to pass them a note during Mr. Platts' conversation so they know, that is helpful.

I am going to ask you, Mr. Kutz, what were items that you weren't able to buy that other people bought, because you just got outbid, that you think would have been kind of surprising, as well, if you know what those items were. That will be my questions. I will try to wrap up after that.

Mr. Platts, you have the floor as long as you want it. Thank you for being here.

Mr. PLATTS. Thank you, Mr. Chairman. I apologize for the late arrival and being with you just for a few minutes. I am sure I will be a little repetitive, and I will try not to be, in my questions.

Mr. SHAYS. Let me just say, Mr. Platts, you ask whatever you want. If it is a little redundant, it will reinforce what I need to know. I need to hear it three times before it sinks in.

Mr. PLATTS. Sounds good, Mr. Chairman.

Mr. SHAYS. OK.

Mr. PLATTS. First, our subcommittee, Government Management Finance Accountability, a big focus—and, Mr. Kutz, you have been with us a good number of times—is in the area of internal controls. And what, to me, we are really talking about here is a breakdown in internal controls in some fashion, whether it be technological, personnel, the review process, but somehow we are letting items go, either at amazingly low prices that are appropriately being sold but not at a fair price, or they shouldn't be sold, or they are being given away. But somewhere there is a breakdown.

I guess I want to start with a broad question really to our officials both in uniform and civilian from the Departments. The OMB had issued internal control regulations this past year requiring every department and agency to do an internal control review of

their processes and kind of, if necessary, it would lead eventually to perhaps an audit of internal controls. Where in that process does DLA stand in regards to this OMB regulation?

Mr. PETERS. Congressman, if I may respond, we are actually in the process right now of finalizing that internal control review report for this year, and the internal operational review that I had talked about earlier during the hearing, we have reflected that in our written response this year to lay the foundation that there are internal control weaknesses and to lay the foundation that, as we move forward, that we can identify the corrective actions and then test the outcomes of those corrective actions to ensure that they are effective in closing those internal control weaknesses.

Mr. PLATTS. In where you are in that review that has gone on thus far, I am assuming that some of those breakdowns relate directly to what has happened here with GAO?

Mr. PETERS. Yes, sir, they do.

Mr. PLATTS. And, while that process—I guess the deadline I think is November 15th as part of the other reports coming forward. In the meantime, you have taken action based on what you have identified, even while you are not at that deadline for the reporting; is that correct?

Mr. PETERS. That is correct. We began the review process of those vulnerabilities and gaps before this period, and the documentation that is due this summer is reflecting that action. Specifically as it relates to these items in front of us, many of those items came from batch lots, which is a real risk, an inherently risked process that exists.

Mr. PLATTS. They came from—say that again?

Mr. PETERS. From batch lotting of items.

Mr. PLATTS. OK. Great.

Mr. PETERS. And it also came from a breakdown in procedures where items that the GAO found were not in batch lots but had line item visibility throughout the process, and so those are the weaknesses that we are attempting to address.

Mr. PLATTS. I am not sure if it is a weakness or just a lack of occurring as far as from a training standpoint, both with civilian officials or on the military side. With the antenna and Chairman Shays' reference in his opening statement, the antenna as a kind of a classic example of the problem here, is there training to all individuals, whatever the level in the personnel ranking, that if you see that item that is about to go out the gate, whether you are the one that signed off for it and said yeah, it is to be given away or sold, is there any training of all personnel that if you see something that seems like it is too good of a deal, too good to be true, or it is too sensitive to be thought of just driving out the gate, that there is a reporting system in place like an 800 number? If you believe there is something askew here, here's where you should go, is that in place today?

Mr. PETERS. It is not in place today. What I have directed since my arrival is that we look at what I would call a job proficiency training curriculum for each employee within the DRMS disposal system. Historically, your specific job would identify the types of training classes that you would obtain. Based on our internal review, one of the weaknesses I believe that we need to shore up is

that, even if you have been with DRMS for a long period of time, refresher training is important, just as it would be for new training for a new employee, and that is what we are in the process now of developing is that curriculum.

Mr. PLATTS. I think it seems—and, again, not hearing all the testimony—it has to be part of the breakdown, that there is not a buy-in by every person on the staff at all levels that in any way is involved with this reutilization program and the distribution or selling of it, that isn't kind of on guard to look for these breakdowns.

Mr. PETERS. Congressman, I concur completely, and when I directed the internal review of the vulnerabilities and gaps from the moment that DRMS would receive an item through the disposition of that item, I brought in the senior disposal experts from the field to ensure that we began the process of having them to help identify those weaknesses—they are the closest to the ground—and to ensure that they help identify the corrective actions.

Mr. ESTEVEZ. Congressman, if I could add a point.

Mr. PLATTS. Yes.

Mr. ESTEVEZ. Because the disposal process starts out at the unit that has excess material and codes it and turns it in. We issue Department-issued guidance to the military services to reemphasize the training requirements of disposal personnel. Those tend to be military people that rotate at a junior grade, so it has to be a continual process on this.

This may be one of the items that Ms. Fischer is going to raise in a moment. Those services have come back and committed what they are doing to reemphasize that training, and this whole process—I chair a group of the service logistics chiefs. This is a continual discussion topic within that group, so we are trying to emphasize do the right thing.

Mr. PLATTS. That focus on the internal control process and then the training to me are hand in hand. I know in our other efforts we found, not just in this case with property reallocation or distribution, that it is key to getting to that bedrock foundation of good management.

The chairman kind of touched on this a little bit. I don't know if it has been addressed earlier. But we certainly, in not having to reinvent the wheel any time is good, especially when we are talking about taxpayer funds being spent, and then also the sensitivity of the products here.

Is there any kind of ongoing dialog between the procurement and logistic officials at Wal-Mart or Home Depot or Lowe's? You go into one of these national chains today, and if there is a shelf with an empty spot somebody comes over with the computer, they scan the bar code, and they say, yes, we have one that is coming in in 3 days. It has been shipped, is being restocked. They are amazing in their logistical handling of goods, both in and out of their stores.

Is there any interaction that happens between the public, your agencies, and the private sector? And I don't mean in the sense of hiring a consultant, but just reaching out to these American corporations to say hey, we would like to pick your brains and maybe get your insights?

Mr. ESTEVEZ. Congressman, absolutely. I am fortunate to have a lot of interaction with the folks from Wal-Mart and Proctor and

Gamble, Toyota, a number of other leading companies that do supply chain management very well to see how they do it.

Our business is different. War fighting is a different model, different operation. We are going to have more inventory than they have because it is more important to have a weapon system operating and to have a little bit of excess because we don't know when, where, how much they tend to. But we do take their best ideas and see how best we can implement them within the Department of Defense.

Let me point out from the disposal standpoint almost every one of those companies completely outsources their returns process. So an item gets returned to a store, they give it to a third party to assess what to do with that item, and that item is likely to end up in an outlet mall, not back on the shelf at a Wal-Mart or a Target.

Mr. PLATTS. Right. I am glad to hear that interaction is going on where it applies. And I readily acknowledge there is a similarity in the time sensitive nature because they want their product on the shelf when I am there to buy it. They want to have it ready. And your military personnel, when they need that weapon, they need whatever that supply is, it is there so that they are in the best position in their war fighting efforts.

On the reutilization program, is there an annual budgetary goal that is set at the beginning of the year that is expected to be met or hoped to be met?

Mr. SHAYS. If the gentleman would just suspend for a second, have we passed on those three recommendations to DOD so they know what the other three recommendations are that we are going to be asking them about?

Ms. FISCHER. Not yet.

Mr. SHAYS. Do you have them?

Ms. FISCHER. Yes.

Mr. SHAYS. Why don't you share that with them. What are those numbers?

Ms. FISCHER. Recommendation——

Mr. SHAYS. Just tell me the numbers.

Ms. FISCHER. No. 4 and No. 5 and No. 6.

Mr. SHAYS. Four, five, and six. OK. You can just take a look at that, whoever is not answering the question. I am sorry to interrupt.

Mr. PLATTS. Thank you, Mr. Chairman.

Mr. PETERS. Congressman, the DRMS goal for reutilization of condition code A property is 30 percent of our dispositions. If you look at the last 12 months, that goal has not been reached each month, but it is a stretch goal, but there have been several months where that goal has been reached and that is the baseline goal that we strive for as we currently know the process.

If you look at overall reutilization, more than just condition code A, we have increased that to 14 percent of our dispositions, and that in original acquisition cost represents over $1.5 billion of acquisition cost that was not new acquisition.

Mr. PLATTS. The reason I am asking is just that I want to make sure that we are not having goals set that are encouraging the sale of equipment to meet an arbitrarily set goal, and that sounds like there are some numbers, expectations, but it is not in the sense

of—I will use the example where you will hear citizens talk about the police officer needs to meet his quota for tickets this month, so there is an incentive to go out. Here there is no quota that is expected, but just what we anticipate?

Mr. PETERS. Yes, sir. We do have the goal. If you were to annualize our fiscal year 2006 year to date it is running at a 21 percent. If you look at it each month, as we do, several months we have hit 30 and several months we have been lower than that. So 30 is a good stretch goal, and we monitor and measure it each month.

Mr. PLATTS. Thank you, Mr. Chairman, for your oversight, and I want to thank all of our witnesses for your service to our Nation and your respective roles. I think our common goal in this hearing—and Chairman Shays has been outstanding in the oversight efforts on this issue—is the bottom line is, one, especially in the area of war fighting and the military, that we are getting whatever our men and women out there who are courageous in their service need. We get it to them when they need it and they have it and we don't repeat the example of what some of chem-bio suits where there was a shortage that we are selling, that we never repeat those errors, and, two, that we are doing right by the American taxpayers.

So I appreciate your efforts and your service, and for all of you, and, General Williams, especially, your service in uniform, believing that, while we all are public servants, those who wear the uniform are the cream of the crop, and your dedication.

The fact that I am a Baltimore Orioles fan, I saw you are from Baltimore, you have to be an Orioles fan if you grew up in Baltimore, right?

General WILLIAMS. That is affirmative, sir.

Mr. SHAYS. That is a very important question. What was the answer to that question?

Mr. PLATTS. It is a little harder to be an Orioles fan nowadays than when I was growing up. Brooks Robinson and those great players of the past are gone. But I do sincerely thank all of you, because we are all after the same goal, and that is good Government and support for our men and women in uniform.

Chairman Shays, thanks again for your efforts on the oversight.

Mr. SHAYS. I thank the gentleman. Just remember the promise of America is the best generations are yet to come, so there is hope.

Four, five, and six. I would like you to read four, and I would like DOD to respond to four. Would you read it nice and loud, please?

Ms. FISCHER. OK. Direct DRMS to develop written guidance and formal training to assist DRMO personnel and military service turn-in generators in the proper assignment of condition codes to excess property turn-ins.

Mr. PETERS. Congressman, if I may respond?

Mr. SHAYS. Sure.

Mr. PETERS. In the past year DRMS has met with each of the four military services, including 30 major commands within those four services, to not only review the outcomes of the GAO reports in prior years, but also to discuss with them the importance of accurate condition coding. As the generator, they own the asset, they turn it in because they have declared it excess. The more they un-

derstand and appreciate the value of the reutilization program and the more accurate that supply condition code is, the greater confidence they will have to rely upon an item out of the disposition or out of the disposal inventory.

We have an ongoing dialog with them. We have now gone to the second round of meetings with the services where we are now looking at their data with them to identify if there are actions that either we can take or some facilitation that we can help them as they continue their effort to improve the accuracy of their condition code.

In addition to that, we are developing a training curriculum that they can insert into their military schools, so as their military members come into the logistics arena, disposal will not be an afterthought. It will be a pre-conscious event.

Mr. SHAYS. Is there one place where you train all the different personnel of the different branches on logistics and inventory chain?

Mr. PETERS. No, sir. At this point in time the actions that have been completed to date have been the discussions with the military services and those major commands and the development of the training curriculum. There is a 2-year cycle for us to work with the military services to insert that curriculum into their military schools.

We do provide, on a demand basis, disposal experts to come in at the appropriate windows in certain military school instructions to provide instruction on the disposal process.

Mr. SHAYS. But we are not training all military personnel, just the ones that need to know, correct?

Mr. PETERS. Just the ones that need to know, sir.

Mr. SHAYS. We sometimes obviously send folks to graduate school and so on. Do we send them to graduate schools where they can take specific courses in this inventory control type concern?

Mr. PETERS. For the DRMS personnel, yes. We participate in the training curriculum that DLA has. We put in nominees for those types of schools.

When I mentioned earlier to Congressman Platts the development of a job proficiency training curriculum is what we are in the process of establishing now, and those types of opportunities to use commercial schools will be part of the development of that curriculum.

Mr. SHAYS. Recommendation five? In each case it says the GAO recommended the Secretary of Defense, and then you read——

Ms. FISCHER. Direct the military services to provide accurate excess property turn-in documentation——

Mr. SHAYS. This is No. 5, correct?

Ms. FISCHER. That is No. 5.

Mr. SHAYS. OK. Direct the Secretary of the Army, Navy, and Air Force——

Ms. FISCHER. I am sorry. You wanted me to back up in the lead-in? We recommend that the Secretary of Defense direct the Director of DLA, the Commander of DRMS, and the Secretaries of the Army, Navy, and Air Force, as appropriate, to take the following 13 actions, and recommendation No. 5 was with respect to directing the military services to provide accurate excess property turn-in

documentation to DRMS, including proper assignment of condition codes and national stock numbers, based on available guidance. National stock numbers are key to identifying the demilitarization code.

Mr. SHAYS. What I am reading, though, it says the Secretary of Defense direct the Secretaries of the Army, Navy, and Air Force to direct the military services to provide accurate excess property turn-in documentations, and so on. What is the answer to this one?

Mr. ESTEVEZ. We issued guidance to the military staffs that operate their supply systems, their supply processes, my counterparts, essentially, to issue that kind of guidance and to come back to us for what they were doing for training to ensure that proper documentation and proper coding was issued, and also, frankly, for No. 6, which deals with the accountability of material.

Mr. SHAYS. Let me read No. 6. The GAO recommended the Secretary of Defense direct the Secretaries of the Army, Navy, and Air Force to require the military services to establish appropriate accountability mechanisms, including supervision and monitoring for ensuring reliability of turn-in documents.

Mr. ESTEVEZ. That is correct, sir. Each of the services, to your earlier question, does have training courses for the enlisted and noncommissioned officer personnel that actually would do the turn-in. This is part of the curriculum in those courses. They also emphasize this at the officer level that are operating their supply agencies. Each service does it slightly differently, so each service, based on their business operation process. An Army unit is going to be different from a Navy ship, for example. Each of the services at the two-start level came back explaining where that is in their curriculum, how that is covered in their curriculum, and what they are doing to ensure that this documentation is proper.

Mr. SHAYS. Thank you. I am going to ask GAO one last question as it regards to recommendation. I would like to know where you think, of the 13 recommendations, which one they have had the greatest success and which one, to date, they have had the biggest failure.

Mr. KUTZ. I think with respect to the people and process related ones, which are the front ones, that is where the most progress has been made, so that has been numbers one through——

Ms. FISCHER. One through six.

Mr. KUTZ [continuing]. One through six, and seven through ten. I think that the BSM, which is the new system that they are developing, and some of those are more long term. There has been some progress in those areas, but I think that the system, the integration type of fixes are ones, as you know from your prior hearings, are ones that aren't necessarily short-term and those aren't problems that these folks caused in the first place, I know.

Mr. SHAYS. Before I have the professional staff just ask the last question, before I ask you a very general question afterwards, Mr. Kucinich and I were talking about it. We are both hoping to come back. One of us may, one of us may not, maybe both of us don't come back, but likely one of us comes back. I don't know if it is a Republican Congress next year or a Democratic Congress next year, but Mr. Kucinich and I both agree there will be another hearing a year from now.

To me, the best report and the thing that would make me the happiest is, when we task GAO to break through the system to find weaknesses, they are going to try to do it and we are happy to tell you what my hope is they come back and say we tried this, we failed, we tried this, we failed, we tried this, we failed, we tried this, we failed. We will have a hearing with nothing on these tables. We will put all the tables up there.

You know what? That will be a good day for you in the Defense Department, it will be a good day for GAO, and we will say at the fifth hearing, congratulations. That would be, to me, what will happen. But whether it is me or Mr. Kucinich, that hearing will happen. I think it is important to think about it right now, and I think you have enough time to deal with it, frankly. I think you have started that process and that would be good for you to be able to come back, to be able to get applause rather than criticisms.

You have one last question?

First, we want to put on the record your report of July 2006, and we want to put on the record all 13 recommendations of your May 2005, report.

[The information referred to follows:]

GAO CODE 192105/GAO-05-277
"DOD EXCESS PROPERTY: MANAGEMENT CONTROL BREAKDOWNS RESULT IN SUBSTANTIAL WASTE AND INEFFICIENCY"

DEPARTMENT OF DEFENSE COMMENTS TO THE RECOMMENDATIONS

[redacted] The GAO recommended that the Secretary of Defense direct the Director of the Defense Logistics Agency (DLA) direct Defense Reutilization and Marketing Service (DRMS) to clarify and enforce the policy that permits the Defense Reutilization and Marketing Office (DRMO) management to waive the requirement to verify quantities on turn-ins under exempted conditions, [redacted] (p. 45/GAO Draft Report)

DoD RESPONSE: Concur. DRMS will review the guidance found at DoD 4160.21-M, Chapter 2, Section E (1)(d) and DRMS-I 4160.14, Vol. II, Chapter 2, Section 1(B)(6)(c), and clarify those situations where DRMS personnel are allowed to waive the quantity verification requirement. DRMS will also ensure its employees understand this guidance and DoD policy, and consider additional criteria to maintain appropriate property accountability through continuous education. In March 2004, DRMS initiated a risk assessment program to evaluate certain DRMS processes and develop appropriate risk mitigation strategies. DRMS will utilize this program in reviewing applicable segments of the receiving process to validate past practices and consider potential changes in light of further perceived risk.

Further, DRMS reviews property accountability as part of its internal Compliance Program (self assessment and organizationally independent compliance inspections), and will review its current audit protocols to ensure that accurate counting of items at receipt is a part of its Compliance Assessments. Result of this assessment will be available in November 2005.

[redacted] (p. 45/GAO Draft Report)

DoD RESPONSE: Partially concur. DRMS will use its staffing model to determine the staffing needs by receipt workload and adequately staff its DRMOs to ensure excess property receipts are verified and processed in accordance with appropriate policies. However, other management actions are also being considered to address this issue. For example, DRMS is currently using contract hires at its DRMOs, rather than hiring new Government employees, because DRMS is in the final stages of an OMB Circular A-76 competition for the receipt, storage, and issue functions of useable property at all of its CONUS DRMOs. This competition is to be completed later this year. Results of this assessment will be available in November 2005.

[redacted]

DoD RESPONSE: Partially Concur. DoD Directives require generators to provide a description of the item on the turn-in document when it is turned in to a DRMO under a Local Stock Number (LSN). DLA's Prime Vendor purchases provide commercial, non-stocked items to military customers direct from vendors. These items are consumable, meaning they are intended for immediate use by the military customer. Bringing these items back into depot stock would negate warehousing/distribution savings achieved as a result of relying on the commercial supply chain. The increased technical documentation requirements required to assign national stock numbers to these non-stocked, commercial items will drive up costs significantly. Also, requiring Prime Vendors to convert commercial marking systems to military systems would run counter to the 1994 Federal Acquisition Streamlining Act preference to buy commercial.

[redacted] (p. 46/GAO Draft Report)

DoD RESPONSE: Partially Concur. The generating activities are responsible for the assignment of supply condition codes (SCC). The Military Services generating these excess materials are in the better position to assign SCCs and understand the impacts of the factors like functional obsolescence, material aging, and previous storage and handling situations. Generators from each of the Services currently receive formal blocks of instruction, as well as appropriate on-the-job training, on specific disposal procedures as part of their logistics education.

The DRMS provides guidance and training material to DRMS personnel, the Military Services and Defense Agencies regarding condition codes, including the web-based information and guidance found on the DRMS Web Site. It provides a DoD Disposal Manual, DoD 4160.21-M, and guidance found in the DRMS-Instruction 4160.14. Additional efforts are being undertaken to highlight supply condition codes issues in training and web based resources. Additionally, DRMS will review current guidance and coordinate with Headquarters, Defense Logistics Agencies and the Military Services to ensure the appropriate assignment of responsibilities regarding the establishment and use of supply condition codes. Results of this assessment will be available in November 2005.

2

[redacted]

DoD RESPONSE: Concur with intent. Existing Military Service policies and procedures require all generators to file accurate property turn-in documentation, as defined by DRMS, and the Services recognize the importance and ramifications of assigning accurate supply condition codes and National Stock Numbers (NSNs) to all property turned-in to DRMS facilities. However, the Services have agreed to reexamine their current procedures to determine if they are adequately implementing those policies and procedures.

Service policy is to reuse materiel to the fullest extent possible regardless of the category of the supply item, while considering economy and safety. Generators of excess and surplus property are required to identify the condition of items excess to their needs prior to disposal through DRMO or return to the supply system. If the condition cannot be determined, certified supply inspectors assist in this process. Service personnel have taken steps to consult with supply personnel to ensure a basic understanding of the updated military instructions. All of the Services endeavor to provide required information to applicable turn-in activities electronically, per the instruction found in the disposal directives.

Current Military Service procedures allow the repair of all space parts and equipment when economically feasible. When repair actions are necessary, the custodian will properly identify the condition of the item on DD Form 1577-2 and attach the tag to the item. When the custodian is not sure of the condition of the item, another qualified maintenance technician or inspector will be asked to help determine the condition of the materiel. Condemned equipment items, beyond economical repair, require the signature of a qualified maintenance technician on DD Form 1577 or the repair cost estimate from the repair center. Either of these actions must take place before the turn-in process can be accomplished.

Not all DoD items have assigned NSNs, as indicated in our response to recommendation 3 above. However, as a minimum, all transfers to DRMO for non-NSN items are required to have a description of the materiel attached to or annotated on the disposal document.

We will direct the Services and DLA to assess their training in condition codes and accuracy of property turn-in documentation. Results of this assessment will be available in November 2005.

RECOMMENDATION 6: [redacted] (p. 46/GAO Draft Report)

3

DoD RESPONSE: Concur. The Services recognize that accountability, supervision, and monitoring are imperative to all logistics operations. The Services and DLA already have systems in place to capture the required data. At the wholesale level, we support this recommendation to establish appropriate accountability mechanisms, including supervision and monitoring, to assure reliability of turn-in documents. DOD policy for retail and wholesale supply requires customers to return excess serviceable or unserviceable materiel to the Service supply activity or appropriate maintenance activity or comply with appropriate disposition instructions. The Services monitor these activities and work with DRMS to ensure visibility of assets throughout the disposal process to ensure a closed loop with regard to transaction item reporting among all Services and Defense Agencies involved. We will direct the Services and DLA to assess the adequacy of their existing systems to capture reliable turn-in data and to generate exceptions reports. Results of this assessment will be available in November 2005.

[redacted] (P. 46/GAO Draft Report)

DoD RESPONSE: Concur. The Agency agrees with the importance of being able to identify and correct systemic weaknesses in property loss reporting. DLA, the Supply Depots and DRMS are already implementing actions to improve our ability to detect actual losses, determine their causes, and take future action to mitigate such risks.

DRMS issued interim guidance to its personnel affecting how losses and adjustments are reported in the DRMS Automated Information System (DAISY). The purpose of this guidance is to improve reason code accuracy and to be able to distinguish "bookkeeping adjustments" from actual physical losses of property.

In February 2005, DRMS issued a task order to the Defense Logistics Agency Office of Operations Research and Resource Analysis (DORRA) to study systemic weakness in DRMS property accounting, provide an assessment of what percentage of losses are attributable to actual physical losses of property rather than record keeping errors, and examine DRMS' records to determine the exact nature of these reported inventory adjustments. Preliminary findings indicate that approximately 67% of the "H" coded losses represent inventory adjustments and data errors rather than a true loss of inventory. Thus, as noted, many of the "losses" cited result from record adjustments and do not reflect actual losses of property indicative of security or property management lapses.

The Defense Distribution Center (DDC) has a long standing program called the "SWARM" Inventory Improvement Initiative. SWARM is a wide-ranging, site-by-site program designed to: 1) identify the root cause of balance errors; 2) train employees on a case-by-case basis; 3) hold all employees accountable for their process; 4) provide comprehensive formal training on policy, processes and systems and clean up the physical warehouse location balances; and 5) Correct the accountable transaction records.

4

The SWARM is reported to the DLA Director monthly and has already made significant progress in achieving its goals. Our goal is to meet the MILSTRAP performance standards, and the Military Services' expectations of accuracy. Results of this assessment will be available in November 2005.

[redacted] (p. 46/GAO Draft Report)

DoD RESPONSE: Concur. DRMS policy is to take immediate appropriate action to resolve identified security weaknesses. DRMS has done so with respect to previous situations that have come to its attention and has done or will do so with respect to issues raised in the draft Report. Results of this assessment will be available in November 2005.

[redacted]

DoD RESPONSE: Concur. The DLA supply depots provide DRMS a weekly property list detailing the amount and type of excess and surplus personal property to be disposed of through Reutilization, Transfer, Donation and Sales. From this information, DRMS develops a property list that will be delivered to the liquidation sales contractor after statutorily mandated screening is completed. The Agency has implemented system changes to provide the property list 42 days in advance of delivery to the contractor.

The DRMS and its sales contractor also review past monthly historical shipments of property. From this information, both the liquidation contractor and DRMS can determine whether current storage capacities and staffing are adequate. The review will conclude whether additional sites should be added or different shipping routes be considered on a one-time basis. This review process is ongoing. DRMS, in conjunction with its liquidation contractor, directs surge or "overflow" quantities of excess property to alternate sites. Additional agency personnel have been assigned to specifically help process property shipped from the supply depots. The liquidation contractor also improved the management team responsible for handling depot property. The results of any changes undertaken will also be reviewed and modifications implemented as appropriate. Results of this assessment will be available in November 2005.

5

[redacted] (p. 46/GAO Draft Report)

DoD RESPONSE: Partially Concur. Inspection of all liquidation contractor facilities has been completed and periodic inspections will continue. The only facility requiring immediate structural repair is the Norfolk facility. DRMS has issued a work order to fix minor structural issues. Actions are being taken to ensure property damage does not occur, which may include diverting property to other sites, if required. Additional storage options are being regularly evaluated by the contractor and DRMS. Facility condition and protection of stock is a key issue for DRMS and Government Liquidation (GL) as the contract provisions provide for increased revenue for both parties based on the selling price of the item. Results of this assessment will be available in November 2005.

[redacted] condition items that could be [redacted] (p. 46/GAO Draft Report)

DoD RESPONSE: Partially Concur. Actions have already been taken to respond to this recommendation. Since 2004, DRMS implemented several initiatives to improve the visibility of disposal assets to DOD. These initiatives include the deployment of Pre-receipt Want Lists, Automated Want List Match against current inventory, and expedited processing property visibility on the DRMS website. In February 2005, DRMS deployed a new web application that allows DOD customers to ask questions on-line about property in inventory, including the ability to request pictures of the item if the condition code is in question. Answers are added to the property description and are available for all customers to view.

In addition, DRMS will work with the Item Managers on the best methodology to provide visibility of "A" condition property. Listings can be tailored for each Item Manager to include only those items or commodities (Federal Stock Class (FSC) or NSN specific) for which they are responsible. Results of this assessment will be available in January 2006.

RECOMMENDATION 12: [redacted] for BSM and RMP. (p. 46/GAO Draft Report)

6

DoD RESPONSE: Concur. Reutilization of DRMS assets is part of the Release 2.2 functionality of DLA's BSM program scheduled for implementation in January 2006. DLA and DRMS developed an interface between the DAISY and BSM for A1 condition code (new, unused and excellent) to provide property visibility and to allow for asset recoupment. BSM Release 2.2 functionality seeks maximum use of DRMS excess material categorized as A1 condition. The Release 2.2 functionality will search DRMS records daily for assets in A1 condition, and if found, will systematically initiate action to recoup those assets in accordance with the items economic retention limits. The system (BSM) will automatically process this information against identified supply needs to locate matching property. When an item is identified, DLA's BSM initiative will generate a requisition request for the item to return it to DLA stock. The interface is in the build phase and testing is scheduled for June through December 2005. Implementation is scheduled for BSM Release 2.2 in January 2006. Additionally, DRMS will further integrate asset recoupment processes in the DRMS RMP.

The "Gap Analysis" process for the DRMS RMP is underway with the BSM application as a primary "target" for functionality requirements. Our initial update on the GAP Analysis will be provided in November 2005. Full Operational Capability (FOC) for the DRMS RMP will be realized in FY 2009.

[redacted] (p. 47/GAO Draft Report)

RESPONSE: Concur. BSM's Release 2.2 functionality seeks maximum use of DRMS excess categorized as A1 condition. The Release 2.2 functionality will search DRMS records daily for assets in A1 condition, and if found, will systemically initiate action to recoup those assets in accordance with the items' economic retention limits. By proactively seeking to identify and recoup assets based on economic limits, the DLA will ensure maximum utilization of assets at the DRMS and will preclude the need to procure items when excess assets are available to be reutilized. Results of this assessment will be available in March 2006.

Mr. CHASE. Either to Mr. Estevez or to the General, General Williams, GAO reported in the report that they released today that in a 3-month period the Department, DLA, saved $34.8 million in new marketing techniques. Could you tell us a little bit about that? What were these new marketing techniques? And have you projected out what the future savings might be for the next fiscal year?

Mr. PETERS. Congressman, if I may respond?

Mr. SHAYS. Mr. Peters.

Mr. PETERS. I believe that, unless I have misunderstood the question, I believe that the new marketing techniques, as it pertains to the enhancement of reutilization material, we have implemented the ability for item managers in the services to identify up to 10,000 line items of items that they would have an interest in acquiring. When that item shows up in the disposal inventory, that alone has generated over 5,600 requisitions, and actually $54 million up to this point.

We have also implemented the ability to notify a prior buyer, not a public buyer but a military service member, of items that they have previously reutilized out of the inventory system. We send an e-mail notification to them to say hey, that item is now in the inventory again. Since we have done that, we have had 600 requisitions with approximately $3.8 million of acquisition value.

And the last item is we have just recently added rotating photos to improve the visibility of an item. This helps to reinforce the accurate condition coding of that item. A picture is worth more than just trust the system. And in the course of that, we have had 140 requisitions since we have implemented those rotating photos. That has yielded approximately $32 million as a result of that.

Those are three enhancements to strengthen the reutilization program. They have been very successful. I believe that they are directly attributable to the improvement that has been made, particularly in fiscal year 2006, toward that $224 million of original acquisition cost through the reutilization of condition code property.

Mr. SHAYS. Mr. Kutz, I did forget that I was going to make sure you put on the record what you couldn't buy because you were outbid that needs to be on the record.

Mr. KUTZ. OK. Let me go through a couple of them. There were several of them that were more of the military technology items. One was a——

Mr. SHAYS. And military sensitive?

Mr. KUTZ. Yes. One was a universal frequency counter similar to the one on my left that we also later purchased, but some of the early purchases we were outbid. The other military sensitive one was an optical instrument lens for an M–901A anti-tank vehicle, and this is one that is, again, national security item. We bid $550 and it sold for $909, and so that is one we lost out on.

Mr. SHAYS. Could you have bid $900 if you wanted to?

Mr. KUTZ. Sure. Yes. We just didn't. It is kind of like eBay. You put an automatic bid in and if someone overbids you, you lose out.

Mr. SHAYS. So you are not able the know their bid and then bid a higher?

Mr. KUTZ. We could have. If we were there at the time we could have outbid, but we put an automatic bid in.

Mr. SHAYS. Gotcha.

Mr. KUTZ. But we didn't want to bid more than that on this one anyway.

Mr. SHAYS. I understand.

Mr. KUTZ. The other items related to cold weather parkas, and then there were some stainless steel pans that are similar to what you see at, like, a hotel that are used to serve food. We were outbid on a number of those that were new and unused.

Mr. SHAYS. OK. So you all have been very cooperative. Mr. Peters, I appreciate you being cooperative, as well. Thank you very much. We had a little more difficult exchange, but I appreciate you not wanting to be the first, but I appreciate you joining in afterwards.

Let me just ask you anything we should put on the record that we didn't put on the record, that we need to put on the record, anything that you had maybe stayed up last night thinking well, gosh, this should be something I should respond to? Is there any tough question that we didn't ask that we should have asked you? So whatever you want to say. We will start with you, Mr. Ryan.

Mr. RYAN. Mr. Congressman, I think I would ask DLA and the General—and I appreciate what the general is trying to do to make sure the items don't get out the door, but I think I would suspend all sales except for A demil items until they have gone through this process. The general talks about oversight and searching these batch lots and making sure that the proper demil codes are identified. I guess in order for this to take place I think I would suggest suspending all sales except for demil A.

Mr. SHAYS. OK.

Ms. Fischer.

Ms. FISCHER. Yes. I would agree with that, and I would add that the Federal logistics information system, which is the system that contains the master information on demilitarization codes, be used to always check the demil codes. There is a problem within the excess inventory system on the demil codes in that, and when they challenge a demil code that system sometimes is giving them the wrong answer. So I would say that they need to go use the DOD standard.

Mr. SHAYS. OK.

Mr. Kutz.

Mr. KUTZ. I would just say we all want to see the same thing here. We are all looking for progress and solution. I just want to commend you for the consistent oversight you have had on this, because you could have walked away after one or two hearings but you have stuck at it and I think it was worthwhile.

Mr. SHAYS. Thanks.

Mr. Estevez.

Mr. ESTEVEZ. Mr. Shays, thank you for the opportunity to testify. I believe we are making progress. I think we have a long way to go, and we are committed to making that progress. I also look forward to the day where we have this hearing with nothing in front of us. Hopefully that will be soon.

Mr. SHAYS. Let me just tell you we will have that hearing, because we want it to be clear that we have made that progress and we would be proud to see that progress.

Major General.

General WILLIAMS. Sir, my goal is to provide an aggressive oversight against a timeline that will get at fixing this particular problem. So we understand the problem, let's fix it. I, as you, don't want to see anything here. Now, if there are a couple of items I should be able to clearly defend that we did to the best of our ability to mitigate the risk but a couple items due to human error happened to get through the process. But the goal is 100 percent no demil item getting into the wrong hands, sir.

Mr. SHAYS. Thank you, sir.

Mr. Peters.

Mr. PETERS. Congressman, since I have taken over the DRMS director position in February it has been an exciting period of time.

Mr. SHAYS. Are you happy you did it?

Mr. PETERS. Yes, sir, I am.

Mr. SHAYS. OK.

Mr. PETERS. I think it is exciting to be part of fixing something, and these problems have existed for a long time. I think we are taking the right steps. We are taking this seriously. It is going to require a true re-engineering of that disposal system, not just point to point fixes, and that is going to take time.

So at the hearing next year I, too, would like to see no items, but I also, because I know that the amount of work that remains to be done and the time and effort that it is going to take to cause that to happen, I hope that my expectation next year is that the GAO will be able to report to this subcommittee that we have made significant progress and that we did what we said we would do here this day.

Mr. SHAYS. Thank you, sir.

With that, we will adjourn the hearing. We thank you all and appreciate your patience. It has been a long afternoon, but thank you very much. With that, this hearing is adjourned.

[Whereupon, at 5:02 p.m., the subcommittee was adjourned.]

[Additional information submitted for the hearing record follows:]

DEFENSE LOGISTICS AGENCY
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IN REPLY
REFER TO DL

SEP 11 2006

Mr. Vincent Chase
Chief Investigator
House Government Reform Committee
Subcommittee on National Security, Emerging
Threats and International Relations
Washington, D.C. 20515-6143

Dear ~~Mr.~~ Vince Chase:

This is in response to your August 3, 2006, request that the Defense Logistics Agency (DLA) review the draft transcript from the July 25, 2006, DOD Excess Property hearing before the Subcommittee. OSD/L&MR has also reviewed the transcript. Attached is the draft transcript with comments.

Also attached is the DLA response to the Questions for the Record (QFRs). Please let me know if you have any questions.

Sincerely,

Robert T. Wimple, Jr.
Colonel, USAF
Director, Legislative Affairs

Federal Recycling Program Printed on Recycled Paper

Hearing Date: July 25, 2006

Committee: House Government Reform
Member: Mr. Kucinich
Question #1

DOD EXCESS PROPERTY: Inventory Control Breakdowns Present a Security Risk

Question: Who has the list of everything that is being sold army surplus? I mean, you showed missile launchers. Are missiles being sold army surplus? You showed parts from an F-14. Are planes being sold army surplus? You showed radar guidance. Who has the list of what is being sold army surplus? We don't really know what we're talking about here if we don't -- I mean, we have to define what we're talking about. What's for sale? Does anyone know? Does anyone have a list?

Answer:
DRMS has visibility of all excess property turned in by the Military Services that flows through its system.

As agreed to during the hearing, we are providing a list of available items that have been sold, transferred, donated and reutilized through the DRMS excess property system managed by DRMS.

Due to the large volume of items DRMS processes annually, we are providing a CD and not a printed list. The enclosed CD contains items that were issued through the Reutilization, Transfer, Donation or Sales programs. The following is a brief definition of those programs:

- Reutilization – items offered for reuse to agencies within the Department of Defense and other authorized programs. Examples of other authorized programs include the Law enforcement Support Organization (LESO) and service museums.

- Transfer – items offered for reuse by Federal agencies (all Federal agencies are considered transfer customers).

- Donation – items offered for reuse by State Agencies for Surplus Property (SASPs). Examples of organizations eligible to receive property under this program include hospitals, schools and clinics.

- Sale – Property, not requiring demilitarization, that cannot be Reutilized, Transferred, or Donated that is eligible for release to the public, is offered for sale either directly to the public or through a DRMS Commercial Venture partner (currently Government Liquidation, LLC). Property not authorized for release is destroyed.

The time period of the data on the CD is the last ten months (Oct-Jul) of Fiscal Year 2006.

UNIT OF ISSUE LEGEND

BX – Box

EA – Each

GL – Gallon

FT – Foot

LB – Pound

PR – Pair

SQ Yard – Square Yard

QT – Quart

YD - Yard