

VOTE 36 - DEFENCE

34. Defence Forces' Consumable Stocks

Background

The Department of Defence budget for 1999 was £510m of which about £31m was for the replenishment of consumable stocks. The estimated value of the stocks at 31 December 1999 was £74m, which were held in 92 stores in 19 locations throughout the country.

The stocks have increased in value from an estimated £42m in 1995 to £74m in 1999 but this is attributed by the Department to being due to more accurate estimation of stock values rather than to an increase in the volume of stocks held.

Responsibility for the control of stores, including nearly all of the purchasing, rests with the Deputy Chief of Staff (Support) but the Secretary General of the Department of Defence is the Accounting Officer for the entire Defence Vote, which includes expenditure on and control of Defence Forces stocks.

Since 1996 the Department's Appropriation Account contains a note regarding the non-adherence to public accounting procedures regarding the valuation and recording of these stocks.

The following is an analysis of the Department's estimate of the value of the stocks as at 31 December 1999

	£
Air Corps	20,000,000
Naval Service	12,986,351
Clothing	10,155,850
Weapons & Ammunition Spares	7,533,009
Cavalry	5,859,011
Communications & Information Service	4,758,148
Barrack Services	3,989,767
Engineers	3,814,969
Transport Spares	3,650,263
Medical Supplies	914,312
Other	<u>382,217</u>
Total	<u>74,043,897</u>

Objectives and Extent of Audit

The objectives of the audit were to ascertain and evaluate:

- The controls in place to ensure that adequate security was being maintained over the stocks.

- The procedures in place to ensure that stocks were maintained at an appropriate level taking account of the costs of holding stocks on the one hand and ensuring security of supply on the other and that they were fairly and correctly valued.
- The efficiency with which the stores function was being operated.
- The policy and procedures being employed in relation to obsolete and surplus stocks.

During the course of the audit, four locations containing six stores were visited: Baldonnell - Air Corps; Haulbowline - Naval Stores; Clancy Barracks - Clothing and Transport; Curragh Camp - Cavalry and Engineers.

Discussions also took place with Department of Defence and Defence Forces personnel.

Audit Findings

Security of Stocks

The stocks are held in military locations and the buildings containing the stocks are patrolled on a 24 hour basis by military personnel, as is the case for all buildings in the locations.

The management of military stores is governed by Army Regulations in particular Army Order 2/87 and Defence Force Regulation S2. They provide for management supervision and accountancy procedures for all technical stores and workshops. The procedures were well documented and contained sufficient instruction for the safeguarding and management of stocks. They set out clearly the stores procedures in relation to management and accounting, purchasing, receipt and issue of goods, disposal of surplus items and stocktaking. The audit indicated that the procedures were being followed, except in relation to the disposal of surplus and obsolete items.

The stores area is subject to ongoing audit by the Department's Internal Audit team and regular physical checks on stocks are also carried out. My audit confirmed that discrepancies found on these checks are relatively minor and appropriate follow up action is taken by way of investigation and adjustment of book balances.

In relation to stores records, while detailed records are maintained in relation to goods received, issued and in stock, no stock control accounts, showing totals of goods received and issued, and overall balances which could be reconciled to the detailed listing of stores balances, are maintained. Such accounts would provide assurance on the accuracy of the detailed stock records. Furthermore, the total value of goods booked into stock is not agreed to the total amounts expended on stock items, which would provide assurance on the correctness of the amounts paid for stock items and the amounts booked into stock.

Stock Values

The Department's policy is to value all stocks at their most recent purchase price.

Surplus and obsolete stocks were therefore overvalued in the books relative to their true worth resulting in an overstatement of stock values in the Appropriation Accounts. This was most noticeable in the Air Corps and Naval Service stocks.

The Air Corps stock was valued at £20m as at 31 December 1999 and included some 21,000 item types of stock. In 1999 the Air Corps identified about 8,300 item types, which had not moved in the previous 5 years and which have been certified as being surplus to requirements. They have been segregated and are awaiting a decision on disposal. (No value was available for these items many of which were between 10 and 20 years old).

The Naval Service stocks were valued at £13m as at 31 December 1999. Tests carried out during the audit identified about 10,000 item types, showing a value estimated at £3.1m, which had not moved in the last 7 years. As a result of the audit findings, the stores personnel have commenced an exercise to ascertain the items which are surplus to requirements.

In the case of Air Corps stocks it was acknowledged by the military authorities that the stock value of £20m as at 31 December 1999 was not computed on the basis of quantities held at the most recent purchase price, but was their best estimate because of pricing inaccuracies and anomalies found on the system.

Audit tests carried out on Naval Service stocks revealed stock overvaluations estimated to be in the order of £2.2m. These overvaluations centred on the incorrect treatment of foreign currency conversion, notwithstanding the fact that the stock system had a facility to automatically convert such amounts.

Stock Levels

The principal reason the Department of Defence holds stocks is to avoid shortages which might make it impossible to carry out functions critical to the success of military missions. Other reasons relate to:

- Holding insurance spares for equipment or machinery which are no longer being manufactured.
- Gaining quantity discounts from buying in bulk.
- Reducing administration costs by reducing the number of orders placed.

It was noted that the ratio of stocks held to annual throughput was quite high. The ratio overall for 1999 was 2.3 which varied from 0.05 for provisions to 12.72 for engineering stocks. The figures indicate that for some categories, the level of stocks is higher than is appropriate taking into account the costs associated with carrying excess stocks such as storage and financial costs as well as the likelihood of stocks becoming obsolete or redundant.

The audit indicated that the high level of stocks was due to a build up of stocks in past years arising from a policy of buying on the basis of predetermined budgets and in large quantities so as to maximise quantity discounts, rather than on the basis of need. However, the Defence Forces have in recent years moved to a policy of buying on the basis of previous year's usage and where feasible on a "just in time" basis, which should in time lead to lower and more appropriate stock levels being maintained when the surplus stocks have been disposed of.

Operational Costs

A Report by the Efficiency Audit Group in 1993 recommended that a rationalisation of the stores area was needed with the ultimate goal of having one multi-purpose store per location. The Department stated that the number of stores has been significantly reduced since 1993 and that it is

not feasible to reduce the number of stores very much further in the short term due to the high capital costs involved in providing new multi-purpose stores or adapting the existing ones.

At December 1999 there were 101 civilian staff employed on full time stores duties. The gross annual salary cost for these employees was about £1.5m which represents about 5% of the annual stores budget. A further 120 Defence Forces personnel were also employed on stores duties on a part time basis.

Inventory Management

The efficient management of the stores function is dependent on quality and timely management information.

Since the early 1990s the Military Information Technology section in conjunction with the Department has been developing an in-house software computer stock system known as the Inventory Management System (IMS), with the objective of supplying accurate and timely information on stock levels, turnover, usage, status of deliveries and purchase orders and cumulative expenditure relative to budgets.

Although this system has been operational since 1992 in some stores and is potentially available to all stores, only 61 out of a total of 92 stores were availing of it at the end of 1999. The remaining stores were using either manual ledgers, kardex systems or locally developed computer spreadsheets, with the exception of the Air Corps, which has purchased a computerised Aircraft Maintenance Management System. This system is capable of providing an inventory management system combined with an aircraft maintenance costing system, but is not linked to IMS and is not regarded as providing reliable values for stocks.

Obsolete and Surplus Stocks

There would appear to be significant surplus and obsolete stocks in respect of Air Corps and Naval stores.

The following are examples of items identified on audit which would appear to be either surplus to requirements or obsolete:

- Stocks of Land Rover spare parts, some of which were purchased up to 20 years ago and cost in the region of £100,000. The particular Land Rover jeeps have been scrapped some years ago and replaced by Nissan vehicles.
- The value of stocks of army clothing, footwear and raw cloth for the manufacture of military uniforms has been in the region of £10m since 1995, while purchases and usage in each of the years 1998 and 1999 were in the region of £3m to £4m. Much of this stock would appear to be surplus to requirements, because, recently, new ready to wear combat uniforms were purchased for army personnel where previously uniforms had been made from pre-purchased cloth. It has been decided that the old uniforms will be issued to the FCA and the remaining cloth will be offered for sale.
- Substantial quantities of barbed wire having a value of some £60,000, as well as some timber and felt stocks having a value of £4,200, were noticed during an inspection of the stocks held in the central engineering store, much of which would appear to be surplus to requirements or obsolete.

Conclusions

- The management, supervision and accounting procedures were well documented and were adequate to ensure that stocks are properly safeguarded and accounted for in relation to quantities. However, the failure to maintain stock control accounts which would provide assurance on the correctness of the detailed stores balances and the failure to reconcile payments for stores items as charged in the Appropriation Account to the values of items booked into stock is an accounting weakness which should be addressed.
- The recorded stock values did not represent their true worth insofar as apparently high quantities of surplus or obsolete items were being carried at full value. Furthermore, pricing errors and inaccuracies discovered in the course of the audit raise questions as to the reliability of the recorded values for some stocks.
- The failure to install IMS in all stores over a period of some eight years raises questions as to the commitment given to the project. The absence of the management information which this system would provide, if fully implemented in all stores, militates significantly against the effective and efficient management of the stores operation.
- While stock levels would appear to be higher than could be justified when financial and economic factors are taken into account, the change in buying policy indicates that the matter is being addressed. However, it would appear that a more systematic and coherent policy needs to be developed on stock levels and purchasing policies for the different categories of stock, which can only be achieved following the installation of IMS in all stores.
- The evidence would suggest that surplus and obsolete stocks are being retained, which seems to be due to a failure in the past to address and deal with this question. Recent exercises carried out on Air Corps and Naval Service stocks indicate that a process of review is in train with the object of reducing stocks to appropriate levels.

The Accounting Officer of the Department of Defence made the following comments in relation to the report:

- He accepted that surplus and obsolete stocks had been allowed to build up in the past and that the issue needed to be addressed. The existence of surplus and obsolete stocks had been identified by the Department prior to the audit taking place and measures had been put in place which should significantly reduce stock levels. Work had commenced in the Naval Service and Air Corps and all other corps would be required to commence reviews immediately. These measures coupled with the full implementation of IMS in all stores accounts, would further enhance stores management in the Defence Forces.

The issue of surplus and obsolete stores had been highlighted in recent annual reports of the Department's Internal Audit Unit and had also been discussed by the Internal Audit Committee. The present Board of Survey procedures were cumbersome and militated against the review of stock on a regular basis and the Internal Audit Unit had made proposals in relation to a more streamlined procedure for dealing with the disposal of surplus and obsolete items. The efficient use of the Board of Survey system, in conjunction

with the use, whenever possible, of “just in time” purchasing techniques, should significantly reduce stock levels.

- He accepted that the pace of development and implementation of IMS had not been satisfactory, due in the main to:
 - the loss of experienced Defence Forces’ IT personnel to the private sector
 - the extensive re-organisation of the logistics function in the Defence Forces over the past few years
 - the need to concentrate the available IT resources on year 2000 issues in 1998/99
- The absence of a fully computerised stores system had made it impractical to operate stock control accounts because of the complexity of the military stores system and the huge number of transactions undertaken each year. However, control accounts would be maintained when the IMS had been fully implemented and the requirement would also be included in the planning for the introduction of the Generic Model Financial Management System which is currently in train throughout the Civil Service.
- The need to expedite the roll-out of the IMS to all stores was now being actively addressed and substantial progress was expected to be made over the next 12 months.