



Office of Inspector General

FINAL REPORT
REVIEW OF
VA MEDICAL CENTER ALBUQUERQUE'S
CONTRACT WITH AMERICAN MEDICAL DEPOT
FOR
DISTRIBUTION OF MEDICAL/SURGICAL SUPPLIES

VAMC Albuquerque's contract with AMD was not cost-effective and many of the claimed savings such as reductions in full-time employees never materialized.

Report Number: 99-00113-55
Date: April 4, 2000

Office of Inspector General
Washington, DC 20420



DEPARTMENT OF VETERANS AFFAIRS
Office of Inspector General
Washington DC 20420

April 4, 2000

TO: Interim Network Director, Veterans Integrated Service Network (VISN) 18,
Southwest Network, (10N18), and
Deputy Assistant Secretary for Acquisition and Materiel Management (90)

SUBJECT: Final Report—Review of VA Medical Center Albuquerque’s Contract with
American Medical Depot for Distribution of Medical/Surgical Supplies,
Report No. 99-00113-55

1. In March 1998, the Office of Inspector General (OIG) received allegations of procurement irregularities involving certain contracts awarded by VA Medical Center (VAMC) Albuquerque. The OIG Hotline referred the allegations to the Office of Acquisition and Materiel Management (OA&MM) who sent a team of OA&MM representatives to Albuquerque to investigate the validity of each allegation. The OA&MM report of their findings recommended that the OIG conduct an audit of the contract between Albuquerque and American Medical Depot (AMD) to determine if the contract was cost-effective. The OA&MM report concluded that the so-called contract was not a valid contract and recommended that the present arrangement be replaced as soon as possible with a valid contract. This recommendation to establish a valid contract was forwarded to the Director, VAMC Albuquerque, as part of a June 25, 1999 Memorandum signed by the Deputy Assistant Secretary (DAS) for Acquisition and Materiel Management. In the Memorandum, the DAS stated: “VAMC Albuquerque must refrain from exercising any further option or continuing in any manner this contract, V501P-2488, for medical/surgical prime vendor.” In response, Acquisition and Materiel Management Service (A&MMS) at Albuquerque did not exercise the option and the contract expired on August 31, 1999. Albuquerque then awarded a new 6-month contract to AMD for the period September 1, 1999 to February 29, 2000.

2. Although we initiated our review to determine if Albuquerque’s contract with AMD was cost-effective, we quickly realized that the contract had spawned numerous issues that had resulted in an internal battle between Medical Center management officials (specifically, the Director and his Associate and the Chief, A&MMS) and the Medical Center Resources Committee (MCRC) Cost Reduction Subcommittee and certain A&MMS employees whose complaints about problems with the contract mirrored the views of the subcommittee. During our site visit in June 1999, we were notified of several instances of employee reprisals in connection with the subcommittee’s February 1999 recommendation to terminate the AMD contract. Because these employee reprisals were beyond the scope of our review, we referred the matter to the Interim Network Director, VISN 18, on September 13, 1999. The referral included our July 6, 1999 Memorandum to the Associate DAS for Acquisitions recounting our “Preliminary

Observations” on the state of the supply operations in Albuquerque. As a result of this referral, the Chief Network Officer appointed a Board of Investigation and they conducted an on-site inquiry the week of November 15, 1999, and issued a report on January 12, 2000.

3. The conclusions made in our report reflect our review of information obtained by OA&MM, the Board of Investigation, along with two on-site visits by us to Albuquerque which included testimony from 14 individuals—primarily MCRC Cost Reduction Subcommittee members and A&MMS current and former employees—and an analysis of records maintained at Albuquerque and documents obtained through subpoena from AMD.

4. Our review concluded that VAMC Albuquerque’s contract with AMD was not cost-effective and that many of the claimed savings, such as reductions in full-time staff, never materialized. Our analysis of the top 75 items shows that product prices increased an average of 23 percent from May 1998 (first purchases made under contract with AMD) through August 1999 resulting in additional expenditures of \$491,000. Projecting these results to the total purchases from AMD for the same time period results in additional product costs incurred by Albuquerque of \$1.1 million. Additionally, we found that AMD overbilled Albuquerque by at least \$212,475 for the period May 1998 through August 1999. In light of the additional expenditures and overbillings, it is of significance that the contract was supposed to have generated a guaranteed \$400,000 in savings for the 8-month period, February 1, 1998 through September 30, 1998¹.

5. The initial contract and the subsequent modification to incorporate prime vendor services for Albuquerque’s medical/surgical product requirements were poorly written and, in fact, the modification represented an illegal contract. This caused continuing, significant problems in administering the contract and in satisfying the customer. Problems went unresolved due to management’s decision not to address the problem and/or a lack of accountability. As a result, A&MMS frequently was not able to get the right product, at the right time, at a reasonable price to the user.

6. The Chief, A&MMS, acknowledged in his testimony before the Board of Investigation, that he knew the modification was significant and that it was done incorrectly. Notwithstanding his knowledge of the situation, he proceeded with the implementation of the AMD contract, and persistently defended the contract when faced with complaints and evidence—in several cases from his own A&MMS employees—that the contract was costing the Medical Center money and service was poor.

7. At a December 2, 1999 exit conference with the VAMC Director and Associate Director and certain key staff members, we stated that our report would recommend that the VAMC cease any continuing contractual relationship with AMD beyond the contract expiration date of February 29, 2000. In a December 14, 1999 e-mail to us, the Associate

¹ Supplemental Agreement 1 (hereinafter referred to as the modification) to contract number V501P-2488, page 1, Item E. “Guarantees: AMD guarantees a savings of \$400,000 without loss of purchasing power during the period 2/1/98 to 9/30/98.”

Director stated, in part: "...based on your verbal report and recommendations, we are starting operational planning in preparation for the termination of AMD as our med/surg prime vendor." In more recent discussions with the Associate Director, the Chief, A&MMS, and the VISN Logistics Representative, we have been advised that actions are being taken to obtain medical/surgical items without the services of AMD.

8. We made the following recommendations:

a. For the Interim Network Director, Veterans Integrated Service Network (VISN) 18, Southwest Network:

1. Cancel Solicitation number 501-31-99.
2. Discontinue any unnecessary contractual relationship with AMD beyond the current contract expiration date of February 29, 2000. (A short transition period beyond February 29 supported by a transition plan may be required to ensure an uninterrupted flow of supplies to the Medical Center).
3. Take appropriate action to collect from AMD the \$400,000 in guaranteed savings.
4. Take appropriate action to collect from AMD the \$212,475 in overbillings identified to date.
5. Continue coordinating with the VISN Logistics Representative and the Contract Review and Evaluation Division of the Inspector General's office to develop a plan to ensure continued availability of supply after the AMD contract expires on February 29, 2000.
6. Establish a committee, comprised of representatives of all patient care services, who will be responsible for: (i) converting existing non-standardized items to the standardized source based on the products on the standardized item list; (ii) identifying acceptable contract sources for the remainder of the items ordered; and, (iii) reviewing contract provisions relating to procurement and delivery of items to ensure that the items needed are readily available.
7. Take appropriate administrative action against the Chief, A&MMS, and the Director, and Associate Director, VAMC Albuquerque.

b. For the DAS for Acquisition and Materiel Management:

1. Review the warrant authority of the Chief, A&MMS, and remove or amend, if appropriate.
2. Appoint an OA&MM team to review the management, staff and operations of A&MMS at Albuquerque to ensure that the staff are properly warranted and the service is appropriately staffed and configured to fulfill the supply needs of the Medical Center.

9. VA management officials concurred with all recommendations except for a partial concurrence to recommendation 8.a.2, and a "no comment at this time" to

recommendation 8.a.7. The partial concurrence was due to AMD being awarded national contracts for VA standardized items which the Medical Center was mandated to purchase. In the “no comment” to recommendation 8.a.7, the Interim Network Director further stated that: “Any comment on this recommendation would be premature and possibly prejudicial to the on going VHA Board of Investigation into this matter. The IG report will be considered along with the final report of the Board. At that time appropriate management action will be determined.” (See Appendixes C and D for the full text of management’s comments to the report’s recommendations).

10. We consider the partial concurrence to represent concurrence with recommendation 8.a.2 since we take no exception to Albuquerque purchasing standardized contract items from AMD. These standardized contracts are awarded and administered by the VA National Acquisition Center with strict controls on the source and pricing of the item. As of March 31, 2000, AMD was only distributing three standardized items. We consider the “no comment at this time” to recommendation 8.a.7 to take appropriate administrative action against certain individuals at Albuquerque to be non-responsive. The Board of Investigation was completed and a report issued to VHA’s Chief Network Officer on January 12, 2000. Therefore, any response to our recommendation for administrative action would not be premature or prejudicial to the Board’s investigation. Our follow-up communications with the Interim Network Director and VHA’s Director, Human Resource Management Group, were unsuccessful in resolving the recommendation. Accordingly, the recommendation will be elevated to VHA’s Chief Network Officer for resolution. We consider all remaining issues as resolved and we will follow up on planned actions until they are completed.

Sincerely,

(Original signed by:)

JOHN B. AMES

Director, Contract Review and
Evaluation Division (52C)

Enclosure

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PART I – FINDINGS AND CONCLUSIONS

1. The Contract Modification between VAMC Albuquerque and American Medical Depot was Improperly Executed

On August 29, 1997, James M. Buckley, contracting officer at VA Medical Center (VAMC) Albuquerque, entered into a non-competitive 8(a) contract with American Medical Depot (AMD). The contract's provisions were vaguely written as to what products and services AMD was to provide and at what costs. On January 29, 1998, this contract was modified bilaterally by Mr. Buckley and the President, AMD. Under terms of Supplemental Agreement 1 (hereinafter referred to as the modification), AMD would become VAMC Albuquerque's Prime Vendor primarily for medical/surgical (med/surg) items. The modification represented a significant change to the terms and conditions of the contract. The Office of General Counsel's (OGC) review of the modification determined that it was outside the scope of the original contract and, as such, it rendered the contract, or at least the modification, invalid.

Several aspects involving the formation of the initial contract and the modification were disturbing to VAMC employees. These concerns surfaced in a March 12, 1998 letter to the VA Office of Inspector General (OIG) which alleged contracting irregularities at the VAMC Albuquerque. The letter was referred to the Office of Acquisition and Materiel Management (OA&MM) for action. OA&MM, during an on-site investigation, reviewed the contract with AMD. The OA&MM review team concluded:

- The initial contract, written intentionally vague, was later modified bilaterally into the existing requirements prime vendor contract.
- The modification constituted a cardinal change in that it was outside the general scope of the contract; therefore, the procurement action was subject to the statutory competition requirement, which did not occur.
- The procurement was not submitted for a required legal/technical review ostensibly due to Acquisition and Materiel Management Service (A&MMS) at Albuquerque estimating the total 5-year contract value at \$450,000 which only represented the value of the 12.5 percent distribution fee. The OA&MM review team estimated the contract value at \$5.5 million. VA Acquisition Regulation (VAAR) 801.602-70(3) requires a legal/technical review for all 8(a) contracts exceeding \$500,000.
- The OA&MM review team further noted that: "Regardless of the estimated contract dollar amount, the solicitation/contract would require a legal and technical review due to the unique, novel, or unusual nature of the acquisition as required in VAAR 801.602-70(a)(6)."

A review of the contract file and related correspondence and testimony indicated that the January 1998 contract modification, which established AMD as Albuquerque's prime

vendor for med/surg items, was signed prior to any discussions or involvement with the service chiefs affected by the contract. Furthermore, the Chief, A&MMS, admitted in his testimony before the Veterans Health Administration (VHA) appointed Board of Investigation that he knew the modification had a significant impact and that it was done improperly. Testimony from the VISN Logistics Representative revealed that the award of the contract was in violation of VISN directives and that he raised these concerns about the legality of the modification as early as April 1998, but received no response from the Chief, A&MMS, who failed to take appropriate action to remedy the problem, and, in fact, proceeded with the implementation of the contract. The implementation of the contract resulted in significant problems affecting the ability of A&MMS to effectively administer the contract and satisfy the customer.

In response to these problems, and continuing complaints and evidence—in some cases from his own A&MMS employees—that the contract was costing the Medical Center money and service was poor, the Chief, A&MMS, persistently defended the contract. A significant amount of resources were focused on keeping the contract, despite evidence that it was not working to the benefit of the Medical Center. An inventory management specialist, who voiced numerous complaints to us related to service issues, stated: “This prime vendor is dictating to us. We are constantly changing our processes, going back to processes to fit their needs, which I feel it should be the other way around. They should bend and flex for how we do things in this hospital.” Testimony from other Medical Center employees echoed this employee’s concerns.

The on-site investigation by OA&MM recommended that the OIG conduct an audit of the contract between Albuquerque and AMD and examine the contractor’s pricing methodologies and determine the cost-effectiveness of the contract. During our review, it quickly became apparent that the Chief, A&MMS and Medical Center management continued to proceed with this contract in spite of evidence that it was not cost-effective and was causing problems with customer satisfaction. For example, after being notified of the determination by OGC that the contract modification was illegal, there was no effort by Medical Center management to cancel or otherwise withdraw from the arrangement. We were informed that this was due, at least in part, to the fact that the contract called for significant monetary penalties if cancelled during a contract year. While this may be true, there was no effort by the Chief, A&MMS, or Medical Center management to further review the issue with Regional Counsel, General Counsel, OA&MM or anyone else to identify the options available to the Medical Center. This situation is even more disturbing in view of the testimony by the Chief, A&MMS and the VISN Logistics Representative (noted previously) before the Board of Investigation that the Chief, A&MMS knew this modification was improper. Recognizing that there was no effort on part of the Medical Center to address the issue, discussions ensued between OA&MM, OGC and the OIG to address the issues. It was determined that the Medical Center was about to exercise the next option year of the agreement which would provide AMD the opportunity to recover the contractual penalties if the contract was cancelled. Conversely, if the next option year was not exercised, the Medical Center would incur no liability for penalties related to canceling the contract. Therefore, the Deputy Assistant Secretary for OA&MM, sent a memorandum to the Director, VAMC Albuquerque,

stating: “VAMC Albuquerque must refrain from exercising any further option or continuing in any manner this contract, V501P-2488, for medical/surgical prime vendor.” In response, A&MMS did not exercise the option and the contract expired on August 31, 1999. Notwithstanding all of the problems associated with the med/surg prime vendor contract with AMD, a new 6-month contract was awarded to AMD for the period September 1, 1999 through February 29, 2000.

During the summer of 1999, the National Acquisition Center (NAC) took action which would have allowed the Medical Center to participate along with 61 other medical centers in the med/surg prime vendor contract being awarded by the NAC. Although the Medical Center initially indicated a willingness to participate, the Chief, A&MMS, submitted specifications to the NAC that were so narrow that no one, other than AMD, could be responsive to the solicitation. Accordingly, the Medical Center did not participate in the contract. Subsequently, and utilizing the narrow specifications, the Medical Center prepared a new solicitation on which AMD was the sole bidder.

2. The Prime Vendor Contract with AMD was not Cost-Effective

We could not identify any cost savings associated with this prime vendor contract. In fact, the contract resulted in significant cost increases caused by: (i) the Medical Center’s decision to sell to AMD, and then repurchase, the Medical Center’s existing stock; and, (ii) paying a higher base price for the items than if purchased directly from the manufacturer.

A. The Sale And Repurchase Of Inventory Resulted In The Unnecessary Expenditure Of Funds

When the contract was modified in January 1998, AMD became the Medical Center’s prime vendor for med/surg supplies. Unlike the pharmaceutical prime vendors, who provide services off-site to various medical centers, AMD was to provide services only to the Medical Center using the warehouse at the VAMC Albuquerque. AMD’s primary responsibility was to order and receive items and place them on the shelves in the warehouse they leased from the Medical Center. Distributing the supplies (which included breaking down cases to allow for the distribution of less than case units of measure) from the warehouse to the patient care providers remained the responsibility of A&MMS.

At the time the modification was accepted, A&MMS had to decide what to do with existing inventory. The Chief, A&MMS, reached an agreement with AMD that VA would sell to AMD, at cost, the existing medical supply inventory as well as supplies that had been ordered and not yet received. The Medical Center would subsequently buy back this inventory at cost (the price AMD paid the Medical Center for the item) plus AMD’s 12.5 percent distribution fee. In short, the Medical Center was paying a 12.5 percent distribution fee for items that were on the warehouse shelf when AMD took over and never left the shelf until it was distributed by Medical Center employees. Some of the items sold to AMD under this agreement were items purchased through Owens and

Minor, the prime vendor that preceded AMD. For those items, the Medical Center already had paid a 6.5 percent distribution fee to Owens and Minor. Therefore, under the agreement with AMD, the Medical Center effectively paid 19 percent in distribution fees for any existing stock that was originally purchased through Owens and Minor. Our review estimated that the sale and repurchasing of items resulted in approximately \$168,000 in unnecessary expenditures.

Just prior to the sale of inventory to AMD, the Medical Center made a large inventory purchase. Inventory records for Supply Fund (CP1007) show a 52 percent increase in ending inventory from February 1998 to March 1998. It appears that A&MMS padded the inventory which had the effect of increasing the dollar value of the distribution fees paid to AMD.

We also found that some suppliers, particularly those with Federal Supply Schedule (FSS) or national contracts, refused to honor AMD as a distributor. Therefore, to purchase these items, the Medical Center continued to order the supplies, sold them to AMD and then repurchased them with the 12.5 percent distribution fee added to the products' price. In other words, the Medical Center was doing AMD's job without any off-set to AMD's distribution fee. While arguably the sale and repurchasing of items on hand or items on order and due-in when the contract started resulted in additional expenses only for a short time period, the sale and repurchasing of items from sources who would not honor AMD as a distributor resulted in the continuous unnecessary expenditure of funds. In addition to paying a 12.5 percent distribution fee when the contractor provided no service, the Medical Center expended a great deal of effort in corresponding with suppliers in order to convince them to recognize AMD as a distributor.

B. Supply Costs Increased As A Result Of The Contract With AMD

To determine the cost-effectiveness of the AMD contract, we compared the prices paid for items purchased through AMD with the prices that would have been paid had the Medical Center purchased the items directly from the manufacturer. In performing our analysis, we considered all factors that the Medical Center indicated off-set the 12.5 percent distribution fee. As discussed later in this report, we concluded that these cost-savings factors never materialized.

Our review revealed that VAMC Albuquerque incurred about \$1.1 million in additional product costs attributable to the contract with AMD. Comparing the direct vendor price to the AMD price as of August 31, 1999 shows an average increase in product prices of 23 percent. Applying the price differences to quantities from May 1998 through August 1999 shows excess expenditures of \$490,805 for 75 items. (We used quantities purchased from AMD, for the timeframe May 1998 through August 1999, that we extracted from sales transaction data obtained from AMD through a subpoena.) To project the sample to total purchases from AMD, we calculated a rate (see Exhibit 1 for detailed computations) that represents additional dollar expenditures and applied that rate to the total AMD purchases through August 31, 1999. The result is an estimated amount

of additional dollar expenditures of \$1,085,989 attributed to all of the products under contract with AMD. On December 12, 1999, we provided the Medical Center Director and Associate Director a preliminary spreadsheet showing the effect of the increased prices.

Because we were unable to obtain line item visibility regarding product price, quantity and vendor data from Medical Center records, we issued a subpoena to AMD. Before we could complete our analysis of the data, the Chief, A&MMS, provided us with the undated report (hereinafter referred to as the report) on September 21, 1999, that purported to show that the contract had been cost-effective. This report was compiled for and distributed to the A&MMS Service Chiefs in VISN 18 to encourage them to contract with AMD for prime vendor services. We determined that the report's conclusions were grossly inaccurate due in part to the fact that inappropriate periods of comparison were used. Among other things, the report concluded that the Medical Center had benefited from an overall cost decrease of ½ percent by contracting with AMD. The conclusions were flawed because rather than comparing sales from like quarters or data from a longer period of time, the report's conclusions were based on comparing sales from the first quarter of fiscal year 1998 to the second quarter of fiscal year 1999. Using the data in the report, we plotted the Medical Center's usage data over time and found that usage peaked in the second and third quarters and dropped off significantly during the first and fourth quarters. In essence, the report compared sales in a valley to those in a peak to support the assertion that the increase in costs was based on increased usage.

Our analysis showed no viable correlation between usage data and supply costs. Unless the Medical Center can compare supply costs with procedures, bed days of care, or outpatient visits, usage cannot be used as the rationale to explain fluctuations in supply costs. We first voiced our concerns about the accuracy of the A&MMS report to the Associate Director on October 6, 1999, when we recommended that the report not be disseminated, or if it had that it be recalled. Over the next month we requested and received supporting data from the Medical Center. On November 5, 1999, when our preliminary analysis was complete, we sent an e-mail to the Acting VISN Director informing him of our concerns. The e-mail was shared with the Medical Center Director, Associate Director, and Chief, A&MMS.

C. Claimed Savings Never Materialized

The decision to award AMD the prime vendor contract despite the high 12.5 percent distribution fee was based on the Chief, A&MMS, representations and belief that the additional costs would be off-set, and actually result in a cost savings due to: (i) AMD's guarantee to the Medical Center of \$400,000 in savings without loss of purchasing power; (ii) contract incentives such as volume incentive discounts and manufacturer's rebates; and, (iii) savings associated with income from the lease of warehouse space to AMD, reduced shipping costs and a reduction in full-time employees (FTE). Our review determined that these cost saving benefits either never materialized or were nominal in nature.

(1) The Guaranteed \$400,000 In Savings Was Never Realized

The modification to contract number V501P-2488 included a provision which stated: “AMD guarantees a savings of \$400,000 without loss of purchasing power during the period 2/1/98 to 9/30/98”. Although this guarantee was unconditional in the contract, the Medical Center has never received a penny of the \$400,000. The Chief, A&MMS, testified that because the Medical Center was unable to produce good data from the Generic Inventory Package (GIP), the \$400,000 was forgone. Conversely, we believe that AMD should be required to make good on its guarantee for the following reasons: (i) the contract obligates AMD to pay \$400,000 to the Medical Center; (ii) the guarantee represented a financial incentive for the Medical Center to award the procurement to AMD; and, (iii) the modification contained stipulated monetary penalties owed to AMD in the event the Medical Center terminated the contract for convenience of the Government. For these reasons, we recommend that the VISN direct the Medical Center to take appropriate action to collect the \$400,000 from AMD.

(2) No Volume Incentive Discounts and Rebate Savings Were Realized

The modification identified two pricing incentives that were represented to be provisions that would result in cost savings: the Volume Incentive Discount Schedule and Manufacturer Rebates. The Volume Incentive Discount Schedule provided that AMD would pay the Medical Center a rebate based on a 5 percent reduction in distribution fees (from 12.5 to 7.5 percent) on all purchases over the volume incentive threshold dollar. The volume incentive threshold established by the contract was sales greater than \$5 million dollars, which was more than the stated value of the contract. In other words, as long as the Medical Center’s purchases were within the scope of the estimated value of the contract, no dollar savings would be realized. In fact, none was.

The Manufacturer Rebates’ clause provided that the Medical Center would receive all rebates resulting from the joint effort of the Medical Center and AMD to establish product pricing agreements with manufacturers/suppliers for products to be distributed under the contract. In other words, if the Medical Center entered into an agreement with a supplier whereby the Medical Center would be entitled to rebates based on criterion such as volume purchased, AMD would collect the rebates and pass them on to the Medical Center. Instead of requiring that any rebates would be passed on to the Medical Center when received, the modification provided that manufacturer rebates were “...payable to the VA within 30 days after the end of each calendar year in a form to be mutually established at the time.” Not only did the modification allow AMD to realize interest for as much as a year on the cash rebates it received from manufacturers, the modification did not require that the Medical Center would receive the rebates in monetary form. More importantly, we found no evidence of any contracts with suppliers that resulted in actual rebates to the Medical Center. The contract further stated that the anticipated product pricing agreements that were expected to result in rebates “shall consist of prices available under Federal Supply Schedule, blanket purchase agreements (BPA’s), national, regional, local and the resultant 8(a) contract for open market items.” It would be highly unlikely that the Medical Center would enter into product pricing

agreements with prices based on FSS or national contracts because these contracts are awarded by the NAC, not individual Medical Centers.

In a May 19, 1999, letter announcing our review, we specifically asked the Medical Center Director whether the Medical Center had received all rebates earned during the term of the contract. To respond to our request, the Chief, A&MMS had AMD run a report for the purpose of identifying any rebates. This is an example of one of the more significant problems with the contract in that the Medical Center, specifically A&MMS, did not maintain any data relative to AMD's performance under the terms of the contract and had to rely on AMD to respond to inquiries. The report, generated by AMD, listed every item ordered by Albuquerque, and where the price billed was different from AMD's price plus the 12.5 percent distribution fee, AMD computed either an overcharge or undercharge. This report, referred to by AMD as a rebate/reclaim (overcharge/undercharge) report, bore no relationship to the rebate provision in the contract. It was impossible to determine if any of the amounts presented by AMD represented rebates as defined in the contract or represented something else. The Chief, A&MMS, provided testimony before the Board of Investigation that there was a formal rebate agreement in place with Hudson, and that he thought that AMD had paid rebates in the \$40,000 range. We believe the amount he was referring to was the \$40,214 partial payment from the rebate report AMD provided to us during our June site visit. This rebate report reflected all sales transactions between AMD and the VAMC and showed all differences between the amount AMD paid for the item plus the distribution fee and the amount AMD billed the VAMC. The report showed amounts due the VA in the amount of \$94,963 of which AMD submitted a check in the amount of \$40,214 on May 28, 1999, and held the balance until alleged payment issues with the VAMC were resolved. We contacted Finance in Austin to inquire about the payment issues with AMD and we were informed that they worked with AMD on disputed invoices, and no money was due to AMD. We confirmed with the Chief of Finance at the Medical Center that the remainder of the amount due has not yet been received from AMD, and the Medical Center has not made any effort to recover the amount due.

(3) **Claimed Savings Relating To Leased Warehouse Space, Reductions In FTE And Reduced Shipping Costs Were Either Non-Existent Or Nominal**

a. Lease Revenue: The contract provided that AMD would lease warehouse space from the Medical Center. However, the amount received was insignificant compared to the costs associated with the 12.5 percent distribution fee. The Medical Center received \$4,585 monthly in lease revenue compared to paying AMD an average of \$46,375 monthly in distribution fees. Our review, and the inquiry conducted by VHA's Board of Investigation reviewing allegations of reprisal, further concluded that the Medical Center leased the space to AMD for far less than the appraised value of the space. This is yet another example where the Medical Center failed to take advantage of an opportunity to off-set expenses associated with this contract.

b. Staffing: Both the Chief, A&MMS, and the President, AMD, have claimed that the contract resulted in significant cost savings associated with a reduction in FTE, primarily by obviating the need for Medical Center personnel to prepare and issue purchase orders. AMD published data claiming \$750,000 in savings for FY99¹ and the Medical Center claimed savings of \$165,685 for the same time period.² A&MMS claims that the savings were calculated based on a VA Central Office standard of \$65 for the processing of a single purchase order which was multiplied by the reduction in processed purchase orders. Our review disclosed that any savings related to a reduction in the processing of purchase orders was minimal because the reduction in FTE needed to realize the savings never occurred. Medical Center records show that there were five purchasing agents on the payroll in January 1998, before the contract was implemented, and five purchasing agents were on board in November 1999.

The Chief, A&MMS, also has stated that the contract with AMD resulted in cost savings because he was able to reduce three FTE in his service (other than purchasing agents).³ In the previously discussed undated report issued in September 1999, the Chief, A&MMS, claimed annual savings of \$200,000 associated with a reduction in FTE. The report represents that the AMD contract allowed a 2 FTE reduction in staff and the relocation of 4 FTE to implement the 24-hour, 7 days a week service. We analyzed A&MMS payroll records from January 1998 through November 1999 and concluded that there was no reduction in FTE as a result of the AMD contract. Although there were some changes in staffing levels, these were attributed to normal personnel actions such as retirements, delays in backfilling positions, and reasons other than supply chain efficiencies.

c. Reduction in Shipping Costs: The Chief, A&MMS, also claims to have realized savings associated with reduced shipping costs. However neither he, nor anyone else, was able to provide us with data to support this claim. Our review found that very few of the items purchased through AMD were purchased off FSS, national or other existing contracts even though like or similar items were available on those contracts, often at lower prices that typically included shipping charges.

3. Significant Deficiencies in Contract Formation and Administration

In addition to the fact that the contract with AMD was not cost-effective, the prime vendor provided no useful services to the Medical Center and caused a number of customer satisfaction problems. We concluded that this was due to significant deficiencies in contract formation and administration that were not addressed by the

¹ "VA Partnership," Volume 1, Issue 2, January 1999.

² Undated Albuquerque A&MMS report regarding the success of the prime vendor program, page 10.

³ The March/April Albuquerque VA Medical Center Newsletter, contains an article on the prime vendor which states: "O'Loughlin was immediately able to reduce his staff by three FTEs."

Medical Center's Director, Associate Director and Chief, A&MMS, all of whom were aware or should have been aware of these problems.

A. Deficiencies in Contract Formation

The contract with AMD was developed, awarded and significantly modified in January 1998 without A&MMS conducting an economic or cost/benefit analysis and without the knowledge of, and more importantly, input from, personnel involved in patient care services who would be most affected by the contract. Medical Center employees consistently testified that affected personnel in A&MMS and the clinical services had no knowledge of the terms of the agreement until late February 1998, even though the contract modification establishing AMD as the prime vendor was signed in January. As noted by the review conducted by OA&MM, the modification was illegal because it constituted a cardinal change to the contract, and, therefore, required that the contract be competed. The VISN Logistics Representative testified that the award of the contract was in violation of VISN policies that require acquisitions over \$25,000 to be brought to the VISN Acquisition & Materiel Management Group and that he informed the Medical Center in April 1998 that the modification was illegal. In his testimony before the Board of Investigation, the Chief, A&MMS, stated that he was aware of the modification and that it was done incorrectly. Although it is unclear from our review that the Director and his Associate were aware of the deficiencies related to the contract formation, they were clearly aware of problems associated with the administration of the contract and the problems with customer satisfaction soon after the contract was implemented.

There is no evidence that the Medical Center considered past performance of AMD **prior** to the award. In its proposal, AMD cited its contract with the VAMC San Juan as evidence that it was a responsible contractor; however we found no evidence that A&MMS contacted the VAMC San Juan to inquire about AMD's performance prior to the award and subsequent modification of the contract. Had the appropriate inquiries been made, the Medical Center would have learned that the VAMC San Juan had significant billing problems with AMD that caused significant resources to be expended by staff at San Juan. Based on our review we found that the contracting officer failed to comply with Subpart 9.1 of the Federal Acquisition Regulations (FAR), which requires the contracting officer to make a determination of contractor responsibility prior to awarding a contract.

The terms and conditions of the contract clearly demonstrate the lack of planning for this contract which precluded the Medical Center from achieving any benefit from the contractual arrangement. As previously discussed, the contract modification cited incentives such as rebates and volume discounts, but was vaguely written as to reasonable benchmarks for attaining these incentives and no mechanism was in place for the Medical Center to track and account for the incentives. The contract provided that AMD would be paid the price of the product, as established by the Medical Center, plus a percentage of the price (12.5 percent) as a distribution fee. This fee was supposedly based on a stockless program and would have been considered reasonable had AMD provided a stockless program, which they did not. No effort was made by A&MMS to modify the

distribution fee to reflect the services rendered, which amounted to AMD simply selling to the VA in the same unit of measure that they purchased in (i.e. case for case). A&MMS was still responsible for breaking down the case in accordance with the supply needs of the wards. We found that the 12.5 percent distribution fee far exceeds fees on other prime vendor agreements providing the same service. For example, the distribution fee in the med/surg prime vendor contract recently awarded by the NAC is only 3 percent and the distribution fee for the prior prime vendor contract with Owens & Minor at the Medical Center was only 6.5 percent. The contract does not provide for any services by AMD that would justify this excessive distribution fee. We were unable to identify any real service that AMD provided under the contract other than to acquire and stock the item that Albuquerque ordered.

Under the terms of the modification, the Medical Center was responsible for establishing the price of the product. This provided the Medical Center with the opportunity to save money by identifying specific products to be provided through AMD at the lowest possible prices, thereby not only saving on the price of the item but also on the distribution fee, which remained fixed but would be applied to a lower price. The Medical Center did not realize any benefit from this contract provision because it did not set up appropriate mechanisms to identify and attain favorable pricing. In most cases, prices were based on the last price the Medical Center paid for an item. There was no evidence that the Medical Center performed any research to determine if the price was reasonable, nor was there any evidence that the Medical Center continually reviewed and amended the initial prices. In fact, our review found that the Medical Center was paying inflated prices for many items primarily due to the high percentage of items (about 77 percent of the items purchased) not being purchased from a contracted source.

As stated, the modification provided that the price to be paid by the Medical Center was the price of the item, i.e., the price established by the Medical Center, plus the distribution fee. Conversely, the initial contract (before the modification) provided that the Medical Center would pay AMD's cost plus the distribution fee⁴. To further confuse who was responsible for establishing the product price, the language in the modification was unclear as to whether the Medical Center or AMD would be responsible for entering into pricing agreements with suppliers that would establish the base price VA would pay. The Chief, A&MMS, testified to the Board of Investigation that if AMD paid less than the price established then they would owe a refund to the VA. In actuality, the modification did not provide for any price reduction to the Medical Center in the event AMD was able to procure the item at a lower price than the Medical Center's price. Therefore, if the price established by the Medical Center was higher than the price AMD was able to procure the item, AMD profited at the expense of VA. However, because the modification did not state that the original contract provisions were deleted, we are recommending that appropriate action be taken to review the contract and collect \$212,475 in net overbillings. This amount represents the difference between AMD's cost

⁴ The original contract, signed in August 1997, provided that the Medical Center would pay the actual cost of items procured by AMD plus a distribution fee. The January 1998 modification, which established AMD as the Med/Surg prime vendor, did not contain the same provision.

plus the distribution fee and the amounts billed by AMD for the period May 1998 through August 31, 1999.

The contract failed to provide controls to recognize that the purchase of items already on contract (for example, FSS and national contracts) would have priority over the purchase of open market items. This absence of controls resulted in the Medical Center paying higher prices because items being procured through AMD were often being purchased open market. Our review determined that about 77 percent of the items that the Medical Center purchased through AMD were open market purchases. This was due to the fact that prior to the modification, no one at the Medical Center conducted the necessary research to determine whether suppliers would sell to AMD; and, after award, the Medical Center did not enter into contracts with vendors as contemplated by the terms and conditions of the modification. As a result, unless the Medical Center procured the items from existing contracts with suppliers, which it then sold to and repurchased from AMD, AMD had no choice but to purchase items open market.

In addition to higher prices, AMD's inability or unwillingness to purchase items on existing FSS or national contracts resulted in the procurement of defective or inferior products in some cases. One of the biggest complaints from clinicians was that at least three brands of latex gloves procured by AMD were defective. The gloves not only cost more than the gloves on VA's national contract, but also had to be discarded. Sometimes entire boxes were discarded. Even more significant than the pricing issue, the defective gloves posed a serious and unnecessary health hazard to VA employees. There was one reported HIV exposure incident related to the defective gloves provided by AMD.

B. Contract Administration Problems

We identified a number of problems related to the administration of the contract. The most significant was the absence of data at the Medical Center needed to monitor and assess AMD's performance and compliance with the contract. When data relating to contract performance was needed, the Chief, A&MMS obtained it from AMD. The Chief, A&MMS, placed critical contract compliance factors in the hands of AMD with no means to verify reported numbers. For example, the contract contains specific provisions relating to fill rates (the percentage of time products will be readily available) and turn around times (the length of time AMD had to provide requested items). Failure by AMD to meet these contract requirements would constitute grounds for terminating the contract for non-performance. A&MMS not only failed to monitor AMD's compliance with these provisions, it did not maintain the information necessary to monitor and assess compliance. During his interview with the Board of Investigation, the Chief, A&MMS, provided documentation to show that AMD was complying with the fill rate requirements. The Chief, A&MMS implied that the report was generated from Medical Center maintained data when, in fact, as he admitted during his interview with us, the report was prepared by AMD. Information maintained by individual Medical Center personnel showed that AMD was not meeting the fill-rate requirements or the turn around requirements. Employees testified that the Chief, A&MMS, and Medical Center management were aware of the problems but took no corrective action.

Also, as previously discussed, the Chief, A&MMS, declined to participate in the national med/surg prime vendor contract awarded by the NAC in October 1999. His reason for declining was because contractor performance requirements (such as fill-rate and turn around times) in the NAC solicitation were slightly relaxed from the requirements established in the AMD contract. However, the Chief, A&MMS, had to rely on AMD to tell him if they were meeting contractual requirements. And, in fact, they were not meeting the fill-rate and turn around requirements.

There was testimony from the Chief, A&MMS, that the Medical Center did not maintain the information needed to monitor contract compliance because a subordinate employee failed to create the necessary information system - GIP Module. GIP permits services to maintain their own line of inventory and establish a stock level requirement, record the distribution of goods to secondary locations, and automatically generate Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) requests for replenishment purposes. Although we agree that the establishment of the GIP module may have provided the Medical Center with the information necessary to monitor the contractor's performance, the Chief, A&MMS should have ensured that the system was available prior to awarding the contract. Even at the time of our review, almost 2 years into the contract, the system was not functioning. We further concluded that this was not the fault of the subordinate employee.

C. Customer Satisfaction Problems

We found that from the time AMD took over prime vendor services in May 1998 there were a host of complaints regarding the ability of the patient care wards to obtain med/surg items in a timely manner. For example, in June 1998, the wards began experiencing significant problems in receiving supplies needed to provide patient care. These problems continued to exist and did not decrease in number or severity despite repeated complaints to Medical Center management and to the Chief, A&MMS. In our view, all these problems are related to the AMD contract, but all of the blame does not fall to AMD. Some of the problems were created by a reorganization within A&MMS which changed the delivery process. For example, with AMD as the prime vendor, the Medical Center reduced the number of materiel handlers and at the same time went to a 24-hour per day, 7 days a week distribution coverage without fully assessing the FTE required to ensure adequate coverage. As a result there were periods of time with no coverage, particularly when employees took planned and unplanned leave.

The problems were exacerbated by the fact that Medical Center management did not adequately prepare the Medical Center for the prime vendor conversion and the consequential reduction of supply on the wards. With an on-site prime vendor, products that previously were housed in the hospital were now stocked in the warehouse. The materiel handlers and patient care services no longer had access to the supplies which resulted in the inability to obtain items when needed. One service chief maintained detailed records of these problems and presented them to Medical Center management. Her concerns were largely ignored.

In some cases, when A&MMS employees were unable to obtain requested items through AMD, they began using their impact cards to purchase needed products. Instead of correcting the supply problem, management took away the impact cards. This is but one example of the contract and the contractor being more important than the needs of the patients.

If left unresolved, dissatisfaction between the users and A&MMS and a lack of focus with regard to procuring the best product at the best price could be detrimental to patient care at the hospital. Therefore, it is our recommendation that before entering into a new prime vendor contract, the Medical Center should establish a committee, comprised of representatives of all patient care services, who will be responsible for: (i) converting existing non-standardized items to the standardized source based on the products on the standardized item list; (ii) identifying acceptable contract sources for the remainder of the items ordered; and, (iii) reviewing contract provisions relating to procurement and delivery of items to ensure that the items needed are readily available. We further recommend that the Medical Center, and in particular the committee, should obtain assistance from the NAC and the VISN Logistics Representative to help identify contract sources for the items used at the Medical Center. The users should evaluate the product based on functionality rather than personal preference.

D. Solicitation Number 501-31-99

On September 15, 1999, A&MMS issued solicitation number 501-31-99 for distribution of med/surg supplies. Once again, A&MMS issued the solicitation without first obtaining legal/technical review. However this time—unlike the January 1998 modification—a legal/technical review was requested even though the review occurred after the solicitation was issued. The intent of the solicitation was to conduct a competitive, 8(a) acquisition for Prime Vendor services. Notwithstanding the purported competitive nature of the solicitation, AMD was the only respondent. The Chief, A&MMS, informed us that the solicitation was sent to 22 companies.

We reviewed the request letters of the 21 companies, other than AMD, who requested the solicitation, but failed to submit a bid. Only two of those companies state that they are 8(a) certified and one was a telemedicine, teleradiology, videoconferencing firm (not a strong candidate for med/surg prime vendor services), the other company who represented itself as an 8(a) firm with the correct Standard Industrial Classification code (5047) code never received the solicitation. According to the Chief, A&MMS, solicitations are mailed to the requestors via regular mail with no receipt confirmations. Two other companies represented themselves as small disadvantaged businesses but were not 8(a). In short, there was only one company, other than AMD, eligible to submit a bid from the firms that had requested the solicitation and that company never received the solicitation.

Both the legal and technical reviews of the solicitation conducted by OGC and OA&MM respectively, addressed the competition factor. The legal review dated December 1,

1999, states: “Please make sure that the file documentation adequately supports this procurement method and, in particular, that it shows a reasonable expectation that at least two eligible and responsible 8(a) firms will submit offers. FAR 19.805-1.” In response to the fact that only one firm submitted an offer, the technical review dated December 2, 1999, states: “Please verify prior to award, that the terms and conditions of the solicitation and the statement of work are not unduly restrictive so that all responsible sources are realistically permitted to compete for the requirements contained in the solicitation”. We have no reason to believe that the Medical Center had any intention of acting on the recommendations contained in the legal or technical reviews.

4. Estimated Annual Requirements

Based on our review of the two contracts with AMD, it appears that A&MMS improperly estimated the contract requirements to ensure that the total dollar requirements were below the dollar thresholds that would require competing the procurement.

In accordance with FAR 19.805-1(2), acquisitions should be competitive among 8(a) firms if: “The anticipated total value of the contract, including options, will exceed \$5,000,000 for acquisitions assigned manufacturing standard industrial classification (SIC) codes and \$3,000,000 for all other acquisitions.” The initial contract awarded in August 1997, contract number V501-2488, cited SIC code 4225 on the cover sheet (General Warehousing and Storage), however two manufacturing SIC codes⁵, 3841 and 3842, were referenced in the contract. The estimated value of the contract was \$4,999,999. The 6-month extension awarded in August 1999, contract V501P-2569, cited SIC code 5047 (Medical, Dental, and Hospital Equipment and Supplies), was awarded in August 1999, had estimated requirements of \$1.5 million for 6 months. Given these numbers, it appears that the medical center was estimating contract values based upon the sole-source restrictions contained in FAR rather than first determining the estimated contract value, and then determining the appropriate procurement method. In our opinion, the requirements were understated in order to stay below the dollar threshold requiring competition in order to award a sole-source contract to AMD.

⁵ All SIC codes that begin with 3 are classified as manufacturing.

PART II – RECOMMENDATIONS

A. We recommend that Interim Network Director, VISN 18, Southwest Network: (See APPENDIX C for full text of response).

1. Cancel Solicitation number 501-31-99.

Interim Network Director's Comments: Concur. Implemented by canceling the solicitation, effective January 28, 2000.

2. Discontinue any contractual relationship with AMD beyond the current contract expiration date of February 29, 2000. (A short transition period beyond February 29 supported by a transition plan may be required to ensure an uninterrupted flow of supplies to the Medical Center).

Interim Network Director's Comments: Concur with the exception of purchasing certain VA standardized items for which AMD has been awarded.

Office of Inspector General's Response: We take no exception to Albuquerque purchasing standardized contract items from AMD because those contracts are awarded and administered by the VA's NAC with strict controls on the source and pricing of the item. As of March 31, AMD was only distributing three standardized items.

3. Take appropriate action to collect from AMD the \$400,000 in guaranteed savings.

Interim Network Director's Comments: Concur. By April 17, 2000, a claim for the full amount will be submitted to AMD.

4. Take appropriate action to collect from AMD the \$212,475 in overbillings identified to date.

Interim Network Director's Comments: Concur. Additional information is required from the OIG to determine how the \$212,475 was calculated in order to submit a detailed claim to AMD.

Office of Inspector General's Response: Additional information will be provided to the VISN Logistics Representative.

5. Continue coordinating with the VISN Logistics Representative and the Contract Review and Evaluation Division of the Inspector General's office to develop a plan to ensure continued availability of supply after the AMD contract expires on February 29, 2000.

Interim Network Director's Comments: Concur. This process has started and is ongoing.

6. Establish a committee, comprised of representatives of all patient care services, who will be responsible for: (i) converting existing non-standardized items to the standardized source based on the products on the standardized item list; (ii) identifying acceptable contract sources for the remainder of the items ordered; and, (iii) reviewing contract provisions relating to procurement and delivery of items to ensure that the items needed are readily available.

Interim Network Director's Comments: Concur. This process has started and is ongoing. The first meeting was held on March 6, 2000.

7. Take appropriate administrative action against the Chief, A&MMS, and the Director, and Associate Director, VAMC Albuquerque.

Interim Network Director's Comments: “No Comment at This Time. Any comment on this recommendation would be premature and possibly prejudicial to the on going VHA Board of Investigation into this matter. The IG report will be considered along with the final report of the Board. At that time appropriate management action will be determined.”

Office of Inspector General's Response: We consider the Interim Network Director's comments to the recommendation as being non-responsive. Because the Board of Investigation completed its report and issued it to VHA's Chief Network Officer on January 12, 2000, we believe that a response to our recommendation for administrative action would not be premature or prejudicial to the Board's investigation. Our follow-up efforts to resolve the recommendation with the Interim Network Director and with VHA's Director, Human Resource Management Group, were unsuccessful. Accordingly, we will elevate the recommendation to the Chief Network Officer for resolution.

B. We recommend that the DAS for Acquisition and Materiel Management: (See APPENDIX D for full text of response).

1. Review the warrant authority of the Chief, A&MMS, and remove or amend, if appropriate.

DAS A&MM's Comments: Concur.

2. Appoint an OA&MM team to review the management, staff and operations of A&MMS at Albuquerque to ensure that the staff are properly warranted and the service is appropriately staffed and configured to fulfill the supply needs of the Medical Center.

DAS A&MM's Comments: Concur.

Office of Inspector General's Response: On April 3, 2000, we obtained via telephone a status report on OA&MM's actions to address the recommendations. During the period March 13-24, 2000, an OA&MM team visited VAMC Albuquerque to review the management, staff and operations of A&MMS at the Medical Center. A report is being prepared that will address staff qualifications, the needs of the customer, and whether the supply service is configured and staffed appropriately to fulfill the customer's needs. OA&MM also is considering the appropriate action to take regarding the warrant of the Chief, A&MMS, at Albuquerque. The extent of the action taken will be determined by carefully considering the findings in our report, the VHA Board of Investigation report, and the OA&MM report.

EXHIBIT 1 – ANALYSIS OF PRICING THROUGH AMD AND DIRECT

IMF	DESCRIPTION	QTY 5/98- 8/99	AMD PRICE as of 8/31/99	TOTAL	DIRECT PRICE	TOTAL	PERCENT CHANGE B TO D	SOURCE FOR PRICE
		A	B	(A*B=C)	D	(A*D=F)	((B-D)/D=G)	F
315	CHLORIDE,SDM250(2B1322Q)	741	\$ 29.16	\$ 21,607.56	\$ 25.92	\$ 19,206.72	12.50%	CdeBaca Submission/AMD Cost
1082	CHLORIDE,SDM(7972-08)	805	\$ 27.47	\$ 22,113.35	\$ 22.36	\$ 17,999.80	22.85%	CdeBaca Submission
2825	SPONGE,LAP18IN(1-1818)	204	\$ 94.15	\$ 19,206.60	\$ 52.32	\$ 10,673.28	79.95%	Q4FY99 PHF
2882	VACUTNR,21G3/4(367281)	112	\$ 249.84	\$ 27,982.08	\$ 188.00	\$ 21,056.00	32.89%	CdeBaca Submission
2935	PACK,OPENHRT/SORIN(3827A)	304	\$ 765.00	\$ 232,560.00	\$ 680.00	\$ 206,720.00	12.50%	Albuquerque A&MM
2936	PAPER,EXAM(NON24324)	360	\$ 14.40	\$ 5,184.00	\$ 12.80	\$ 4,608.00	12.50%	AMD Cost
2940	BAG,URNDRNG(0154002)	374	\$ 66.66	\$ 24,930.84	\$ 29.90	\$ 11,182.60	122.94%	BPA w/Bard
2947	DIAP,ADTLG(06541)	1237	\$ 31.30	\$ 38,718.10	\$ 25.87	\$ 32,001.19	20.99%	AMD Cost
2951	TUBE,10MLREDGRY(6510)	192	\$ 287.82	\$ 55,261.44	\$ 210.84	\$ 40,481.28	36.51%	CdeBaca Submission/AMD Cost
2986	TOWEL,PAPR12X14(02505)	1709	\$ 24.98	\$ 42,690.82	\$ 22.20	\$ 37,939.80	12.52%	CdeBaca Submission/AMD Cost
2994	LINE,SCT1.5(65651-515)	151	\$ 156.79	\$ 23,675.29	\$ 139.37	\$ 21,044.87	12.50%	VAMCNM Contract with Allegiance
3007	CANNISTER, SUCTION 3.0LTR	173	\$ 93.11	\$ 16,108.03	\$ 65.20	\$ 11,279.60	42.81%	Q4FY99 PHF/BPA
3026	SET,CATH,(CS14703)	204	\$ 90.36	\$ 18,433.44	\$ 80.32	\$ 16,385.28	12.50%	CdeBaca Submission/AMD Cost
3030	PAD,ELECTRD(402-2204)	89	\$ 260.04	\$ 23,143.56	\$ 231.15	\$ 20,572.35	12.50%	Q4FY99 PHF/CdeBaca Submission/AMD cost
3058	PACK,HEART(SCV730HVAL)	317	\$ 485.49	\$ 153,900.33	\$ 431.55	\$ 136,801.35	12.50%	CdeBaca Submission/AMD Cost
3059	PAD,PRTV36X24(006622)	2063	\$ 25.25	\$ 52,090.75	\$ 20.87	\$ 43,054.81	20.99%	AMD Cost
3501	TRANSDUCER(042920006B)	71	\$ 354.38	\$ 25,160.98	\$ 315.00	\$ 22,365.00	12.50%	AMD Cost
3810	CEMENT,BONE(61911010)	48	\$ 773.81	\$ 37,142.88	\$ 687.83	\$ 33,015.84	12.50%	AMD Cost
3837	OXISENSOR PULSE D-25	720	\$ 344.25	\$ 247,860.00	\$ 306.00	\$ 220,320.00	12.50%	CdeBaca Submission
3877	HEMOSTAT(1951)	31	\$ 688.08	\$ 21,330.48	\$ 588.64	\$ 18,247.84	16.89%	AMD Cost
4311	DRAIN,UNPL(57133)	182	\$ 162.00	\$ 29,484.00	\$ 144.00	\$ 26,208.00	12.50%	AMD Cost

IMF	DESCRIPTION	QTY 5/98- 8/99	AMD PRICE as of 8/31/99	TOTAL (A*B=C)	DIRECT PRICE D	TOTAL (A*D=F)	PERCENT CHANGE B TO D ((B-D)/D=G)	SOURCE FOR PRICE F
		A	B					
4493	IRRIG SYS(207-559)	72	\$ 231.75	\$ 16,686.00	\$ 206.00	\$ 14,832.00	12.50%	CdeBaca Submission/AMD Cost
4928	CATH BALLOON INTAOR 40CC 025501	63	\$ 838.13	\$ 52,802.19	\$ 745.00	\$ 46,935.00	12.50%	CdeBaca Submission
5534	GAUZE KERLIX 4-1/2 6715	320	\$ 69.08	\$ 22,105.60	\$ 50.00	\$ 16,000.00	38.16%	BPA w/Kendall/CdeBaca Submission
5711	SYRINGE 20CC LL, 9661	200	\$ 90.51	\$ 18,102.00	\$ 34.85	\$ 6,970.00	159.71%	AMD Cost
5862	CELLSVR,SFTWR(EE2S00)	15	\$ 846.00	\$ 12,690.00	\$ 752.00	\$ 11,280.00	12.50%	CdeBaca Submission/AMD Cost
6056	HEMOCONCENTRTR(C8058Y1B)	138	\$ 222.75	\$ 30,739.50	\$ 198.00	\$ 27,324.00	12.50%	AMD Cost
6231	YANKAUER,SCT(3495)	266	\$ 56.25	\$ 14,962.50	\$ 50.00	\$ 13,300.00	12.50%	CdeBaca Submission
6232	PADS,INCT(FCPP23363)	445	\$ 29.75	\$ 13,238.75	\$ 26.44	\$ 11,765.80	12.52%	AMD Cost
6289	KIT START IV 264805	438	\$ 71.96	\$ 31,518.48	\$ 63.96	\$ 28,014.48	12.51%	CdeBaca Submission/AMD Cost
6291	SET,MONTR(041576504A)	437	\$ 118.13	\$ 51,622.81	\$ 105.00	\$ 45,885.00	12.50%	CdeBaca Submission/AMD Cost
6380	EXER LUNG(19009)	204	\$ 93.38	\$ 19,049.52	\$ 57.00	\$ 11,628.00	63.82%	AMD Cost
6397	ELECTRODE,ECG(MT530)	245	\$ 101.25	\$ 24,806.25	\$ 90.00	\$ 22,050.00	12.50%	CdeBaca Submission/AMD Cost
7181	ENVISION,JRF6FR(061009)	114	\$ 94.39	\$ 10,760.46	\$ 83.90	\$ 9,564.60	12.50%	AMD Cost
7184	SYRINGE,INFLATE KT (K0500598D)	84	\$ 399.38	\$ 33,547.92	\$ 355.00	\$ 29,820.00	12.50%	CdeBaca Submission
7195	MANIFLD,HRTLFT(K090224D)	318	\$ 92.95	\$ 29,558.10	\$ 82.92	\$ 26,368.56	12.10%	AMD Cost
7197	GLOVE,PWDFRLG(8878)	935	\$ 54.00	\$ 50,490.00	\$ 43.50	\$ 40,672.50	24.14%	AMD Cost
7416	TAPE ADHESIVE 1IN NYLON(7138)	69	\$ 88.19	\$ 6,085.11	\$ 78.39	\$ 5,408.91	12.50%	Q4FY99 PHF/CdeBaca Submission/AMD cost
7506	HEXABRIX200ML(550521)	49	\$ 1,438.02	\$ 70,462.98	\$ 1,116.24	\$ 54,695.76	28.83%	CdeBaca Submission/AMD Cost
8781	KIT LAP CHOLE FDC10	27	\$ 1,585.83	\$ 42,817.41	\$ 885.08	\$ 23,897.16	79.17%	CdeBaca Submission
9291	SLEEVE,SCDMD(5330)	278	\$ 270.60	\$ 75,226.80	\$ 240.52	\$ 66,864.56	12.51%	AMD Cost
9691	GLV,PWDFRMD(8877)	1032	\$ 54.00	\$ 55,728.00	\$ 43.50	\$ 44,892.00	24.14%	AMD Cost

IMF	DESCRIPTION	QTY 5/98- 8/99	AMD PRICE as of 8/31/99	TOTAL	DIRECT PRICE	TOTAL	PERCENT CHANGE B TO D	SOURCE FOR PRICE
		A	B	(A*B=C)	D	(A*D=F)	((B-D)/D=G)	F
10209	APPLIER LIGACLIP SM MCS20	147	\$ 379.80	\$ 55,830.60	\$ 336.02	\$ 49,394.94	13.03%	CdeBaca Submission
10460	PACK,SURG LAP (29137)	247	\$ 103.07	\$ 25,458.29	\$ 90.67	\$ 22,395.49	13.68%	CdeBaca Submission
10462	PACK,GWNTWLXLG(9541)	657	\$ 66.34	\$ 43,585.38	\$ 58.97	\$ 38,743.29	12.50%	AMD Cost
10484	PACK,SRGGWNXXLG(9571)	178	\$ 111.31	\$ 19,813.18	\$ 90.93	\$ 16,185.54	22.41%	CdeBaca Submission
10492	PACK,SURG CRDVSC(29153)	172	\$ 174.43	\$ 30,001.96	\$ 155.05	\$ 26,668.60	12.50%	AMD Cost
10493	PACK,SRGART(SOP73ARVAE)	100	\$ 268.29	\$ 26,829.00	\$ 238.48	\$ 23,848.00	12.50%	CdeBaca Submission
10562	SLEEVE,SCDLG(5480)	100	\$ 193.62	\$ 19,362.00	\$ 172.11	\$ 17,211.00	12.50%	AMD Cost
10566	SLEEVE,SCDSM(5345)	74	\$ 258.18	\$ 19,105.32	\$ 229.49	\$ 16,982.26	12.50%	AMD Cost
10764	CATHETER, HOHN PERCUTANEOUS	18	\$ 1,084.78	\$ 19,526.04	\$ 959.50	\$ 17,271.00	13.06%	AMD Cost
10849	STERILANT(S2000)	94	\$ 111.38	\$ 10,469.72	\$ 92.07	\$ 8,654.58	20.97%	AMD Cost
10854	PAD,ELECTODE (8900-4003)	43	\$ 436.50	\$ 18,769.50	\$ 388.00	\$ 16,684.00	12.50%	CdeBaca Submission/AMD Cost
11113	BASIN,MAJOR(7897-T8)	592	\$ 194.54	\$ 115,167.68	\$ 172.92	\$ 102,368.64	12.50%	CdeBaca Submission/AMD Cost
11331	HOOD,UVDISP(5410-50)	31	\$ 230.60	\$ 7,148.60	\$ 205.00	\$ 6,355.00	12.49%	AMD Cost
11513	TRAY,PIC 4FR(7715407)	41	\$ 632.68	\$ 25,939.88	\$ 546.00	\$ 22,386.00	15.88%	CdeBaca Submission
11562	WRAP,PLEX(235340)	32	\$ 421.88	\$ 13,500.16	\$ 302.50	\$ 9,680.00	39.46%	CdeBaca Submission
11723	DRAPE,SLUSH(ORS-331)	14	\$ 1,080.00	\$ 15,120.00	\$ 923.06	\$ 12,922.84	17.00%	AMD Cost
11744	SYR,SFTY,10CC(305559)	104	\$ 163.71	\$ 17,025.84	\$ 98.56	\$ 10,250.24	66.10%	AMD Cost
11993	GLOVE BIOGEL 6-1/2(30465)	36	\$ 360.00	\$ 12,960.00	\$ 313.92	\$ 11,301.12	14.68%	Q4FY99 PHF
11994	GLOVE BIOGEL 7(30470)	43	\$ 360.00	\$ 15,480.00	\$ 313.92	\$ 13,498.56	14.68%	Q4FY99 PHF
12099	GEM PREMERE(5328)	41	\$ 1,136.25	\$ 46,586.25	\$ 1,000.00	\$ 41,000.00	13.63%	Q4FY99 PHF/CdeBaca Submission
12109	PACK,TOTALJNT(P73EXVAA)	77	\$ 406.13	\$ 31,272.01	\$ 361.00	\$ 27,797.00	12.50%	AMD Cost
12323	GLV,PWDFRSM(8876)	644	\$ 54.00	\$ 34,776.00	\$ 43.50	\$ 28,014.00	24.14%	AMD Cost
12328	GLOVE BIOGEL 7-1/2(30475)	46	\$ 360.00	\$ 16,560.00	\$ 313.92	\$ 14,440.32	14.68%	Q4FY99 PHF
12561	TRAY,FOLEY16(902816)	135	\$ 136.24	\$ 18,392.40	\$ 121.10	\$ 16,348.50	12.50%	Q4FY99 PHF
12674	SET EXTENSION IV 20039E	269	\$ 180.00	\$ 48,420.00	\$ 130.00	\$ 34,970.00	38.46%	CdeBaca Submission
12680	SET SECONDARY IV 72213N	257	\$ 117.00	\$ 30,069.00	\$ 104.00	\$ 26,728.00	12.50%	CdeBaca Submission/AMD Cost
12698	OCUTOME UNIPAK(20111MM)	35	\$ 515.35	\$ 18,037.25	\$ 450.00	\$ 15,750.00	14.52%	CdeBaca Submission
12790	DIALYZERS(CLT175)	358	\$ 236.25	\$ 84,577.50	\$ 210.00	\$ 75,180.00	12.50%	CdeBaca Submission/AMD Cost

IMF	DESCRIPTION	QTY 5/98- 8/99	AMD PRICE as of 8/31/99	TOTAL (A*B=C)	DIRECT PRICE D	TOTAL (A*D=F)	PERCENT CHANGE B TO D ((B-D)/D=G)	SOURCE FOR PRICE F
		A	B					
12796	CARTRIDGES(C-3)	366	\$ 71.72	\$ 26,249.52	\$ 63.75	\$ 23,332.50	12.50%	CdeBaca Submission/AMD Cost
12899	HEXABRX100ML(5505080)	72	\$ 786.11	\$ 56,599.92	\$ 609.24	\$ 43,865.28	29.03%	CdeBaca Submission/AMD Cost
13162	SET PRIMARY IV 72033E	886	\$ 366.75	\$ 324,940.50	\$ 300.00	\$ 265,800.00	22.25%	Q4FY99 PHF
13163	SET BLOOD 72980E	105	\$ 189.00	\$ 19,845.00	\$ 168.00	\$ 17,640.00	12.50%	CdeBaca Submission/AMD Cost
13208	CATHETER CORONARY(C2018)	60	\$ 720.00	\$ 43,200.00	\$ 640.00	\$ 38,400.00	12.50%	CdeBaca Submission/AMD Cost
				\$ 3,132,203.41		\$ 2,641,398.64		
	Average Price Increase						23.13%	
	Additional Dollar Expenditures					\$ 490,804.77		
	Rate of Additional Dollar Expenditures (\$490,804.77/\$3,132,203.41=15.67 Percent)					15.67%		
	Total Billed by AMD May 98 through August 99					\$ 6,930,530.01		
	Projected Additional Dollar Expenditures (\$6,930,530.01 * 15.67%)					\$ 1,085,988.60		

APPENDIX A – SCOPE AND METHODOLOGY

Our review included:

- Reviewing the report issued by the OA&MM team that was tasked with investigating the propriety of the contract based on a hotline allegation.
- Collecting background information on AMD to include: Confirming their authorized size standards from the SBA, obtaining their most current financial disclosure information submitted to SBA, obtaining from VA records of all payments from all sources to AMD. Contacting those Medical Centers doing business with AMD. Contacting the contract administrator who administered the AMD contract in Puerto Rico.
- Obtaining and reviewing contract file for contract number V501P-2488 issued to AMD with an effective date of August 29, 1997, to include the modification, effective January 29, 1998 that changed to scope of the contract to the med/surg prime vendor contract.
- Obtaining and reviewing contract number V501P-2569.
- Obtaining and reviewing solicitation number 501-31-99.
- Conducting interviews of current and former VA Albuquerque personnel, and current and former AMD personnel.
- Reviewing billing records of AMD for the period May 1998 through August 1999.
- Reviewing testimony taken by the Board of Investigation.
- Working with Finance personnel in Austin to determine the resolution of the alleged payment issues.
- Reviewing Integrated Funds Distribution, Control Point Activity, Accounting and Procurement (IFCAP) files downloaded by Austin from the Albuquerque Medical Center.
- Performing a purchase order match on the AMD transaction file and the Albuquerque IFCAP file to determine completeness of the file.
- Reviewing all correspondence between the MCRC Cost Reduction Subcommittee and Albuquerque A&MMS (as well as the other services) and the A&MMS responses to the correspondence.
- Collecting and reviewing usage data used by A&MMS to support their claim that Medical Center usage has increased.
- Reviewing Albuquerque's A&MMS report related to the cost-effectiveness of AMD as the prime vendor.
- Contacting all companies on the mailing list for solicitation number 501-31-99 to inquire as to why they did not bid on the solicitation.

APPENDIX B – CHRONOLOGY OF SIGNIFICANT EVENTS

<u>DATE</u>	<u>EVENT</u>
August 29, 1997	Contract number V501P-2488 is awarded to AMD
January 29, 1998	AMD contract is modified beyond the original scope to add prime vendor services
March, 1998	Med/surg inventory shows a 52 percent increase from February 1998 to March 1998
March 3, 1998	Albuquerque’s Chief, Acquisition Management obtains contractor past performance information from the National Acquisition Center
March 12, 1998	OIG Hotline receives complaint
April 15, 1998	OIG Hotline refers the complaint to OA&MM
April 16-21, 1998	Albuquerque conducts physical inventory of med/surg supplies
May 15, 1998	First Purchase Order processed by AMD
May 29, 1998	AMD purchases \$550,441.32 worth of inventory after VAMC conducts a physical inventory. This inventory eventually will be sold back to Albuquerque with the 12.5 percent distribution fee added.
July 13, 1998	OA&MM team conducts on-site visit
August 24, 1998	AMD purchases \$226,680.66 in inventory ordered by Albuquerque but “due-in” at the time of conversion. This inventory eventually will be sold back to Albuquerque with the 12.5 percent distribution fee added.
January 11, 1999	OA&MM issues report of their review in response to the OIG Hotline complaint
February 10, 1999	AMD pays \$274,039.80 representing inventory ordered by Albuquerque during implementation. This inventory eventually will be sold back to Albuquerque with the 12.5 percent distribution fee added.
February 18, 1999	AMD pays \$43,146.02 representing inventory ordered by Albuquerque during implementation. This inventory eventually will be sold back to Albuquerque with the 12.5 percent distribution fee added.
May 19, 1999	OIG’s Contract Review and Evaluation Division announces review to VAMC officials and requests documentation.
June 3, 1999	AMD pays \$256,755.29 representing inventory ordered by Albuquerque but “due-in” at the time of conversion. This inventory eventually will be sold back to Albuquerque with the 12.5 percent distribution fee added.
June 13, 1999	OIG’s Contract Review and Evaluation Division conducts on-site visit.
June 25, 1999	DAS, for A&MM issues memorandum to VAMC Albuquerque instructing discontinuance of the AMD contract

<u>DATE</u>	<u>EVENT</u>
July, 1999	At the OIG's request the NAC offers to include Albuquerque in the national contract for med/surg prime vendor distribution. Albuquerque A&MMS responds with specifications that are too restrictive for inclusion in the solicitation
July 6, 1999	OIG Contract Review and Evaluation Division issues its interim report to the Associate DAS for Acquisitions
July 23, 1999	Austin Automation Center downloads data from Albuquerque
August 30, 1999	OIG issues a subpoena to AMD for all sales data related to contract number V501P-2488
August 31, 1999	Contract number V501P-2488 expires
September 1, 1999	Contract number V501P-2569 (a 6-month contract) becomes effective
September 13, 1999	OIG Contract Review and Evaluation Division refers employee reprisal issues to Acting Director, VISN 18.
September 15, 1999	Albuquerque A&MMS issues solicitation number 501-31-99
September 21, 1999	A&MMS concludes that the cost of supply chain is less expensive using AMD
October 12, 1999	Receive data subpoenaed from AMD
October 15, 1999	One offer is received to solicitation number 501-31-99 ¹
October 18, 1999	Chief Network Officer at request of Interim Network Director, VISN 18, appoints four Board Members to an Administrative Board of Investigation to investigate employee reprisal issues at VAMC Albuquerque
November 15, 1999	Board of Investigation conducts on-site visit
December 1, 1999	Legal review of solicitation is completed
December 2, 1999	Technical review of solicitation is completed

¹ The contracting officer requests the legal/technical review sometime after bid closing date.

APPENDIX C – INTERIM NETWORK DIRECTOR’S COMMENTS

Department of
Veterans Affairs

Memorandum

Date: March 29, 2000

From: Interim Network Director, VISN 18, Mesa, AZ (10N18)

Subj: Response to Draft OIG Report of VA Medical Center Albuquerque's contract with American Medical Depot for Distribution of Medical/Surgical Supplies

To: OIG
CNO

1. Thank you for offering us the opportunity to respond to the above draft report. Response to the OIG's specific findings and conclusions are set out below. I have also reviewed Albuquerque's response to the report and because of the specificity of their arguments, have included it as an attachment to this memorandum.
2. While you will note that we have, for the most part, concurred with your report's findings and recommendations, we have done so only on the global level. We would encourage you to take the specific Albuquerque responses into consideration before preparing your final report.

FINDINGS

(1) The Contract Modification between VAMC Albuquerque and American Medical Depot was Improperly Executed.

Concur

(2) The Prime Vendor Contract with AMD was not Cost-Effective.

Partially concur. The actual amount of costs and savings of this contract is still a matter of debate. However, at most given the 1.1 million that the OIG estimates the medical center may have overspent and the amount of off-set savings the maximum amount that could have been overspent is approximately \$500,000. Further, there were other unquantifiable benefits gained such as improved customer service through 24-hour, 7 day per week coverage. If the medical center recoups the funds recommended by the OIG the \$500,000 will be reduced to a negligible amount. Furthermore, had the medical center negotiated a third contract with AMD at a reduced distribution fee there would may have been a net savings for the government.

(3) Significant Deficiencies in Contract Formation and Administration.

Concur

(4) Estimated Annual Requirements

2105
VA FORM

2.

OIG

Response to Draft OIG Report of VA Medical Center Albuquerque's contract with American Medical Depot for Distribution of Medical/Surgical Supplies

Concur

RECOMMENDATIONS

(1) Cancel solicitation #501-31-99

Concur. The solicitation was cancelled effective January 28, 2000.

(2) Cease to continue any contractual relationship with AMD beyond the current contract expiration date of February 29, 2000. (A short transition period beyond February 29 supported by a transition plan may be required to ensure an uninterrupted flow of supplies to the medical center).

Partially Concur. The medical/surgical prime vendor contract expired on March 29, 2000 and the medical center is currently on transition plan through April, 30, 2000 which concludes the contract closeout. However, AMD has now been awarded national contracts for VA standardized items and the medical center is therefore mandated to purchase items from them.

(3) Take appropriate action to collect from AMD the \$400,000 in guaranteed savings.

Concur. Contract action will be taken to recoup the \$400,000 in savings. However, at this point it is the judgment of the contracting officer that \$200,000 of the \$400,000 is recoverable. However, in order to establish the actual recoverable amount a claim will be submitted to AMD by April 17, 2000 for the full amount of \$400,000.

(4) Take appropriate action to collect from AMD.

Concur. Additional information is required from the OIG to determine how the \$212,475 was calculated in order to submit a detailed claim to AMD. A detailed action plan will be developed upon receipt of this information from the OIG.

(5) Continue coordinating with the VISN Logistics Representative and the Contract Review and Evaluation Division of the Inspector General's office to develop a plan to ensure continued availability of supply after the AMD contract expires on February 29, 2000.

Concur. This process has started and is ongoing.

(6) Establish a committee, comprised of representatives of all patient care services, who will be responsible for: (I) converting existing non-standardized

3.

OIG

Response to Draft OIG Report of VA Medical Center Albuquerque's contract with American Medical Depot for Distribution of Medical/Surgical Supplies

items to the standardized source based on the products on the standardized item list: (ii) identifying acceptable contract sources for the remainder of the items ordered; and, (iii) reviewing contract provisions relating to procurement and delivery of items to ensure that the items needed are readily available.

Concur. This process has started and is ongoing. The first meeting was held on March 6, 2000.

(7) Take appropriate administrative action against the Chief, A&MMS, and the Director, and Associate Director, VAMC Albuquerque.

No Comment at This Time. Any comment on this recommendation would be premature and possibly prejudicial to the on going VHA Board of Investigation into this matter. The IG report will be considered along with the final report of the Board. At that time appropriate management action will be determined.

3. If you have questions regarding this report, please contact Mr. Ron Bednarz, Chief Logistics Officer for VISN 18 at (520) 629-4704 .

(Original signed by:)

Jonathan H. Gardner, FACHE

Attachments: Response from 00/501, dated March 16, 2000
Response from 90/501, dated March 15, 2000

**APPENDIX D – DAS FOR ACQUISITION AND MATERIEL MANAGEMENT'S
COMMENTS**

**Department of
Veterans Affairs**

Memorandum

Date: FEB 10 2000
Deputy Assistant Secretary for Acquisition and Materiel Management (95A)
From:
Subj: Draft Report--Review of VA Medical Center Albuquerque's Contract with American
Medical Depot for Distribution of Medical/Surgical Supplies
To: Director, Contract Review and Evaluation Division (52C)

1. The subject draft report has been received and reviewed. We concur with the review findings and recommendations. We offer no comments other than implementation plans with target completion dates for the recommendations.
2. We concur with the first recommendation that the Deputy Assistant Secretary for Acquisition and Materiel Management take appropriate action to review the warrant authority of the Chief, Acquisition and Materiel Management Service (A&MMS), and remove or amend if appropriate. We will review the issues raised by the report and take action on the warrant appropriate to the seriousness of the situation. This action will be completed by March 15, 2000.
3. We concur with the second recommendation that the Deputy Assistant Secretary for Acquisition and Materiel Management appoint an Office of Acquisition and Materiel Management team to review the management, staff and operations of A&MMS at Albuquerque to ensure that the staff are properly warranted and the service is appropriately staffed and configured to fulfill the supply needs of the Medical Center. A team is being assembled to visit the Veterans Affairs Medical Center in Albuquerque in March 2000. The team will interview the staff and evaluate their qualifications, determine the present structure and workload of the organization, and interview the customer services to determine their requirements. Additionally, the team will review the existing contracts and their administration. With the information garnered by the team, and in cooperation with Veterans Integrated Service Network (VISN) 18, we will make recommendations to the VISN regarding staffing, organization, training, and improved acquisition procedures. These recommendations will be completed by June 1, 2000.
4. Please direct any questions to Kenneth D. Hayes at (202) 273-8828.

(Original signed by:
Gary J. Krump