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United States Government Accountability Office  
Washington, DC 20548

February 1, 2006

The Honorable Daniel K. Akaka  
Ranking Member  
Committee on Veterans' Affairs  
United States Senate

The Honorable Lane Evans  
Ranking Member  
Committee on Veterans' Affairs  
House of Representatives

*Subject: Veterans Affairs: Limited Support for Reported Health Care Management Efficiency Savings*

The Department of Veterans Affairs (VA) provides a uniform set of health care services to eligible veterans who enroll to receive such care and seek it from VA. These services include preventive and primary health care, a full range of outpatient and inpatient services, and prescription drugs. VA provides additional services, such as nursing home and dental care and other services, as required by law for some veterans and makes these services available to other veterans on a discretionary basis as resources permit. Most of the nation's 24 million veterans are eligible for some aspect of VA's health care services if they choose to enroll. In fiscal year 2005, about 7 million veterans were enrolled to receive VA health care services. In that year, VA planned to provide health care services to about 5 million veterans based on its initial budget request of \$ 30.2 billion.<sup>1</sup> Funding for VA's health care program has increased substantially in recent years.

Congress appropriates funds annually for VA to provide health care services to eligible veterans. Congressional budget deliberations start when the President

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<sup>1</sup>For fiscal year 2005, the President requested \$27.8 billion in appropriations and \$2.4 billion in estimated collections, together amounting to a request for \$30.2 billion in discretionary budget authority to the Veterans Health Administration (VHA) for providing health care. See *Budget of the United States Government—Appendix, Fiscal Year 2005*, at 869-70, 873. In the Departments of Veterans Affairs and Housing and Urban Development, and Independent Agencies Appropriations Act, 2005, Pub. L. No. 108-447, div. I, 118 Stat. 3285, 3287-89 (Dec. 8, 2004), Congress ultimately appropriated \$28.3 billion for health care. Later in fiscal year 2005, in response to the President's request for \$975 million in supplemental appropriations, Congress provided an additional \$1.5 billion in supplemental appropriations for veterans' health care to be available through fiscal year 2006. See the Department of the Interior, Environment, and Related Agencies Appropriations Act, 2006, Pub. L. No. 109-54, title VI, 119 Stat. 499, 563-64 (Aug. 2, 2005). Finally, in the *Budget of the United States Government—Appendix, Fiscal Year 2006*, the President reported that VA's estimated collections for fiscal year 2005 would be \$1.95 billion. Id. at 893.

submits his annual budget request to Congress as the *Budget of the United States Government*. This is soon followed by VA providing the Congress with a more detailed budget justification of the President's policy and funding proposals for its programs.<sup>2</sup> In each of the President's budget requests for fiscal years 2003 through 2006, the proposals assumed implementation of management efficiency initiatives that would save money without reducing the quality of service. Indeed, over these 4 fiscal years, the President's budget proposals assumed that these initiatives reduced funding requests by billions of dollars.

Since savings from management efficiencies were expected to help reduce the level of annual appropriations, you asked us to examine (1) VA's methodology for projecting the health care management efficiency savings that were assumed in the President's budget requests for fiscal years 2003 through 2006 and (2) VA's support for reported actual savings achieved through management efficiency initiatives during fiscal years 2003 and 2004—including the methodology and documentation used to track and report achieved savings. As agreed with your staff, we also summarized prior GAO and VA Office of the Inspector General (OIG) reports that have identified management inefficiencies at VA.

To examine VA's health care management efficiency initiatives, we interviewed officials with VHA's Office of the Chief Financial Officer (CFO). We also interviewed officials from VA's Procurement Reform Task Force, the Pharmacy Benefits Management Strategic Health Care Group, the Office of Prosthetic and Clinical Logistics Group, and the Office of Information Technology, all of which VA reported as the primary sources of the agency's management efficiency savings. We requested documentation for the assumed savings amount from each source. We also interviewed officials responsible for reporting actual savings achieved from management efficiency initiatives at all 21 of VA's regional health care networks. In addition, we obtained and analyzed documentation provided by VA in support of its projected savings and reported actual savings achieved from management efficiencies—including guidance provided to each of the regional health care networks on reporting actual savings achieved as well as documents and spreadsheets used to collect and report efficiency savings. We could only evaluate VA's achieved savings for fiscal years 2003 and 2004 because as of the end of our fieldwork, VA had not yet compiled its fiscal year 2005 achieved savings figures. We also reviewed prior GAO and VA OIG reports to identify management inefficiencies at VA. We conducted our work from September 2005 through January 2006 in accordance with U.S. generally accepted government auditing standards. We requested and received written comments on a draft of this report from VA and have reprinted VA's comments in enclosure II. Enclosure I contains further details on our scope and methodology.

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<sup>2</sup>An agency provides budget justification materials – referred to as the congressional budget justification – to its appropriations subcommittees after the Office of Management and Budget has reviewed the information for consistency with the President's budget request. Although the congressional budget justification is transmitted after the President's budget, the format and timing is determined by the needs of the relevant appropriations subcommittee.

## Results in Brief

VA lacked a methodology for making the health care management efficiency savings assumptions reflected in the President's budget requests for fiscal years 2003 through 2006 and, therefore, was unable to provide us with any support for those estimates. VA officials told us that the management efficiency savings assumed in these requests were savings goals used to reduce requests for a higher level of annual appropriations in order to fill the gap between the cost associated with VA's projected demand for health care services and the amount the President was willing to request.

Further, VA lacks adequate support for the \$1.3 billion it reported as actual management efficiency savings achieved for fiscal years 2003 and 2004 because it lacked a sound methodology and adequate documentation for calculating and reporting management efficiency savings. Specifically, there was little consistency with respect to what VA's regional networks reported as management efficiency savings, how savings were calculated, and what type of documentation was available to support the savings figures reported. In addition, VA's regional networks sometimes reported savings resulting from cost-cutting measures as management efficiency savings. Although both can achieve savings, cost-cutting measures, unlike management efficiency initiatives, are not consistent with VA's objective of providing the same or higher quality and quantity of service at a lower cost. Finally, VA does not have a reliable basis for determining whether it has realized the management efficiency savings that were reflected in the President's budget requests for fiscal years 2003 and 2004. Specifically, VA's use of its savings calculation for its national procurement initiatives is misleading because VA calculates actual savings for these initiatives on a cumulative basis and compares these savings figures with savings goals that are reflected on an incremental basis.

In recent years, the VA OIG and we identified management inefficiencies that, if unaddressed, could contribute to requests for higher amounts of appropriations that could otherwise have been avoided. For example, although VA has instituted a number of procurement reform initiatives aimed at leveraging its purchasing power and improving the overall effectiveness of its procurement actions, the VA OIG and we continue to identify problems with VA's procurement processes. Moreover, the VA OIG identified deficiencies in VA's procurement practices as one of the agency's most serious management challenges. For instance, recent GAO and VA OIG reports disclosed significant problems with VA's acquisitions involving Federal Supply Schedule (FSS) contracts; procurement of health care services; VA construction; acquisition support weaknesses; and inadequate management and oversight of major system initiatives. In addition, recent GAO and VA OIG reports have identified both serious control weaknesses in the agency's inventory management and shortfalls in the agency's efforts to provide reliable cost data to accurately assess the efficiency and effectiveness of VA's programs and initiatives.

VA concurred with our recommendations but disagreed that it had used its management efficiency savings goals to fill the gap between the cost associated with VA's projected demand for health care services and the amount the President was willing to request. However, VA officials uniformly described VA's process for

determining its management efficiency savings goals in this manner and it did not provide us any other explanation. Further, VA did not provide us with any support for the methodology used to develop its management efficiency savings goals. Accordingly, we continue to believe that this characterization is appropriate.

## Background

In the mid-1990s, VA began to change fundamentally the way it delivers health care to veterans to increase the efficiency of its health care system and to improve access to medical services. Applying lessons learned from the private sector's experiences with managed health care, VA began emphasizing certain managed care practices, such as primary, outpatient, and preventive care, and de-emphasizing practices such as inpatient care. To support its health care reform efforts, VA decentralized the management structure of the agency to coordinate the organization of hospitals, outpatient clinics, and other facilities into 21 regional networks or Veterans Integrated Service Networks (VISN). One aspect of VA's health care reorganization was to establish organizationwide goals for improving efficiency and access and to create performance measures to hold network directors accountable for achieving these goals.

To maximize the health care provided to veterans with available resources—although not required as part of the budget process—the President's budget request has included expected savings achieved through various management efficiency initiatives. We have previously reported on the likelihood of VA achieving the management efficiency savings included in the President's budget request. In September 1999, we reported that VA had identified management efficiency initiatives that it expected would result in savings totaling \$1.2 billion.<sup>3</sup> Our 1999 report concluded that it seemed unlikely that VA's savings goal would be achieved through management efficiency initiatives because many of VA's initiatives were not consistent with VA's objective to provide the same or higher-quality services at lower costs. Instead, anticipated savings could possibly cause service delays or diminished service quality. Initiatives that appeared not to affect service quality negatively accounted for only \$600 million.

Then, in March 2005, as part of a review of VA's congressional budget justification, we prepared an issue paper on the likelihood of VA achieving significant management efficiency savings in fiscal year 2006. We reported that VA's fiscal year 2006 estimate of \$590 million in management savings appeared to be achievable based on prior work by GAO and the VA OIG. In conducting the budget justification work, as stated in our issue paper, we did not test the reliability and validity of the data used to calculate the projected savings. With respect to our current engagement, for which you asked us to validate the data used to calculate projected and achieved savings, our work included tests of the reliability and validity of the data used.

## VA Lacks a Methodology for Projecting Savings Resulting from Management Efficiency Initiatives

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<sup>3</sup>GAO, *Veterans' Health Care: Fiscal Year 2000 Budget*, GAO/HEHS-99-189R (Washington D.C.: Sept. 14, 1999).

VA lacked a methodology for making the health care management efficiency savings assumptions reflected in the President’s budget requests for fiscal years 2003 through 2006 and, therefore, was unable to provide us with any support for the savings. VA officials told us that the management efficiency savings assumed in these requests were savings goals used to reduce requests for a higher level of annual appropriations in order to fill the gap between the cost associated with VA’s projected demand for health care services and the amount the President was willing to request.

In its congressional budget justifications, VA has provided additional details on the management efficiency savings reflected in the President’s budget request for fiscal years 2003 through 2006. As shown in table 1, VA presented these savings goals on both an annual and a cumulative basis. However, the level and type of detail provided in the justifications varied from year to year. For example, in fiscal year 2004, the detailed savings amounts presented in VA’s budget justification sum to the cumulative amount of \$950 million—whereas, in fiscal year 2006, the detailed savings sum to the annual amount of \$590 million. In fiscal years 2003 and 2005, VA did not provide information linking savings goals to specific management efficiency initiatives—making it difficult to determine how much savings was expected from each initiative and whether VA’s budget justification detail was intended to support its annual or cumulative savings assumptions.

**Table 1: VA’s Health Care Management Efficiency Savings Goals, Fiscal Years 2003–2006**  
Dollars in millions

Fiscal year	Reported annual savings	Reported cumulative savings	VA reported justification for savings goals
2003	\$316	\$316	Standardization of procurement activities, evaluation of operational community-based outpatient clinics, evaluation of centrally managed programs
2004	634	950	\$150 million - implement competitive sourcing plan \$250 million - procurement standardization \$300 million - maintain administrative costs at 2003 level \$100 million - improve employee productivity \$150 million - shift from inpatient to outpatient care
2005	340	1,290	Improve standardization policies in procurement of supplies, pharmaceuticals, and other capital purchases
2006	590	1,790	\$431 million - operational efficiencies \$159 million - competitive sourcing; improved standardization policies in procurement of supplies, pharmaceuticals, and other operational efficiencies

Source: GAO analysis of VA’s annual budget justifications for fiscal years 2003 through 2006.

The Senate Appropriations Committee also found problems with VA’s fiscal year 2006 budget justification details—concluding that VA’s estimated management efficiencies are not supported by adequate details in its congressional budget justification.<sup>4</sup> Consequently, the Senate Appropriations Committee and its House and Senate conferees—in their reports related to VA appropriations for fiscal year 2006—directed VA to provide more detail on its justification for management efficiencies in future congressional budget justifications on the premise that savings projections

<sup>4</sup>See *Military Construction and Veterans Affairs and Related Agencies Appropriation Bill, 2006*, S. Rep. No. 109-105, at 42-43, 55 (July 21, 2005).

that are well-grounded and supported in the budget request are more likely to be achievable.<sup>5</sup>

VA Lacks Adequate Support for Actual Management Efficiency Savings Achieved

VA also does not have adequate support for the \$1.3 billion it reported as actual management efficiency savings achieved for fiscal years 2003 and 2004 because it lacked a sound methodology and adequate documentation for calculating and reporting actual management efficiency savings. Specifically, there was little consistency with respect to what VA’s VISNs reported as management efficiency savings, how savings were calculated, and what type of documentation was available to support reported savings figures. In addition, VA does not have a consistent basis for reporting actual savings achieved—reporting savings for some initiatives on a cumulative basis and others on an incremental basis—which can be misleading given the context of an annual budget. By reporting some savings on a cumulative basis, VA does not have a reliable way to determine whether it has realized the planned management efficiency savings that are reflected in VA’s budget justifications for fiscal years 2003 and 2004. As shown in table 2, VA reported realized management efficiency savings in two broad areas—savings resulting from local or VISN-level initiatives and savings from national or VA-wide initiatives.

**Table 2: Reported Actual Savings Achieved from Management Efficiency Initiatives for Fiscal Years 2003 through 2004**  
Dollars in Millions

Fiscal year	VISN inventory management, administrative consolidations, VA/Department of Defense resource sharing, competitive sourcing, and other initiatives	National procurement standardization initiatives	Total
2003	\$231	\$396	<b>\$627</b>
2004	235	414	<b>\$649</b>
<b>Total for 2-year period</b>	<b>\$466</b>	<b>\$810<sup>a</sup></b>	<b>\$1,276</b>

Source: VHA Office of the CFO.

<sup>a</sup>Of the \$810 million, according to VA officials, \$756 million was related to pharmaceutical procurements and \$54 million was related to other equipment procurements.

Because VA had not yet compiled the savings information for fiscal year 2005 as of the end of our fieldwork, we could not evaluate VA’s achieved savings figures for that fiscal year. However, according to VA officials, they planned to use the same process as was used in prior years to arrive at VA’s fiscal year 2005 achieved savings.

**VA Lacks a Clear, Consistent Methodology for Tracking and Reporting Achieved Savings Resulting from VISN Initiatives**

VA’s methodology for tracking, reporting, and documenting actual savings achieved through VISN-level initiatives lacked consistency with respect to what was reported as management efficiency savings, how savings were calculated, and type of documentation available to support the savings figures reported. Consequently, VA

<sup>5</sup>Id.; H.R. Conf. Rep. No. 109-305, at 44 (Nov. 17, 2005).

did not have a consistent basis for reporting actual savings achieved—reporting savings for some initiatives on a cumulative basis and others on an incremental basis. In other cases, based on the information provided by VISN officials, VISNs appeared to include cost-cutting measures that, unlike management efficiency initiatives, are not consistent with VA’s objective of providing the same or higher quality and quantity of service at a lower cost.

Each year, VHA’s Office of the CFO requests information on savings achieved through local, or VISN-level, management efficiency initiatives. To obtain this information, the Office of the CFO provides a template to each of VHA’s 21 VISNs that outlines general savings categories—which include standardization of pharmaceuticals, supplies, and material procurement; inventory management; administrative overhead reductions; Department of Defense (DOD) and VA resource sharing activities; productivity improvements; and other initiatives. Using this template, each VISN requests savings figures from the medical centers, clinics, and other organizations within the regional health care network. Beyond a limited description of each of the savings categories, VA provided no other written guidance to the VISNs on what their roles were in providing oversight to the process, what constitutes management efficiency savings, how savings should be calculated, and what type of documentation should be maintained in support of the reported savings figures.

Based on our interviews and documents provided by VISN officials, the type of documentation available in support of the management efficiency savings reported varied widely across the VISNs. According to the 21 VISN officials we interviewed, some received only a completed template, or the summary-level information, from medical centers, clinics, and other organizations within their region and performed only a cursory review of the savings figures before forwarding the information on to the VHA Office of the CFO. Others obtained more detailed information on savings and were involved in calculating the savings figures.

In addition, the VISNs were not consistently defining what constituted a management efficiency. For example, several of the VISNs reported management efficiency savings for actions such as temporary and permanent reductions in full-time equivalent (FTE) workers from one year to the next, delays in hiring, reductions in overtime, and reductions in available resources due to budget cuts—which may not represent management efficiency savings because they are not consistent with VA’s objective of providing the same or higher quality and quantity of service at a lower cost. For example, for fiscal year 2003, one network reported more than \$2.8 million of savings resulting from controlled hiring—or delayed hiring of authorized staff. For that same fiscal year period, another network reported savings of \$131,000 for reductions in overtime and \$264,000 for staffing reductions—without any explanation of whether and, if so, how these savings were achieved without a reduction in the level or quality of service.

Finally, there was little consistency with respect to how savings were calculated. Some VISNs calculated productivity savings based on reductions in the unit cost of providing health care services, while others calculated it based on the decreased cost associated with a reduction in the number of FTEs on board. In some instances, VA reported actual savings achieved on a cumulative basis, instead of an incremental basis. For example, according to one VISN, it reported the savings in fiscal year 2003

resulting from closing one of its hospitals in that year and claimed the same savings again in fiscal year 2004. However, due to inconsistencies in the type of documentation available to support management efficiency savings, we were unable to determine the extent to which VA reported savings on an incremental versus a cumulative basis.

### Methodology for Calculating Achieved Savings Resulting from National Procurement Standardization Initiatives Is Not Appropriate

VA does not have a reliable basis for determining whether it has realized the management efficiency savings that were reflected in the President's budget requests for fiscal years 2003 and 2004. Specifically, VA's use of its savings calculation for its national procurement initiatives is misleading because VA calculates actual savings for these initiatives on a cumulative basis and compares these savings figures with savings goals that are reflected on an incremental basis.

Annually, VHA's Office of the CFO requests information on the agency's national procurement standardization initiatives, which accounted for most of the agency's reported actual management efficiency savings. Using spreadsheets, the Office of the CFO accumulates summary-level efficiency savings data from the Pharmacy Benefits Management Strategic Healthcare Group, the Office of Prosthetics and Clinical Logistic Group, and the Office of Information Technology. According to VA officials, these actual savings figures provide the basis for VA to determine whether it has realized previously reported savings goals.

VA officials told us that the achieved savings for VA's national procurement standardization initiatives were based on data obtained from its pharmaceutical and medical and surgical supplies prime vendor<sup>6</sup> databases. VA officials said that the achieved savings amount represents costs that were avoided by utilizing national contracts in lieu of other available sources. To compute this amount, VA compares the actual cost of each item purchased on contract with the estimated cost of that same item had the contract not been awarded. VA estimated what the cost would be without the contract by multiplying the weighted average price per unit that existed during the 3-month period before the contract took effect by the quantity purchased in the current fiscal year. For example, VA determined that a contract for rabeprazole (used to treat ulcers of the stomach and gastro esophageal reflux disease) awarded in May 2001 resulted in fiscal year 2003 cost avoidance of \$134 million (54 percent of the actual cost) because the cost of the drug purchased on contract in fiscal year 2003 was \$115 million, and the estimated cost of the drug without the contract was \$249 million.

VA's national procurement contract initiatives are not new. The agency has been awarding national contracts to take advantage of larger discounts based on volume purchasing since 1993. However, VA calculates achieved savings each year as if it were the first year of the contract and the savings were occurring for the first time.

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<sup>6</sup>Prime vendors are contractors that buy inventory from a variety of suppliers, store the inventory in commercial warehouses, and ship it to customers when ordered. VA's medical and surgical prime vendor distribution contract has been in effect since fiscal year 2002. The contract provides that the prime vendor reimburse VA about 3 percent of sales to VA medical centers.



As a result, VA’s methodology for calculating actual savings achieved from its national contract initiatives does not clearly distinguish recurring savings from incremental savings—which precludes VA from calculating actual savings figures on an incremental basis.

Using hypothetical figures, table 3 illustrates VA’s savings calculation approach. As noted, actual figures were not available because VA’s savings calculation methodology does not clearly distinguish recurring savings from incremental savings. Table 3 shows that during the first year of a contract, VA would calculate savings by comparing the actual cost of an item purchased on contract with the estimated cost of the same number of items using precontract prices. Based on this calculation, VA would report savings in year one of \$100. Because it is the first year of the contract, the \$100 savings figure reflects an incremental amount. In the second year, assuming utilization increases to 150 units and the contract price remains the same, VA again would calculate savings by comparing the cost of the item purchased on contract with the estimated cost of the item using precontract prices.

**Table 3: Comparison of Cumulative and Incremental Savings Computations**

	VA’s savings computation methodology		Incremental savings computation 2 <sup>nd</sup> year
	1 <sup>st</sup> year	2 <sup>nd</sup> year	
Actual cost when purchased on standardized contract	\$1.5 x 100 units = \$150	\$1.5 x 150 units = \$225	\$1.5 x 50 units = \$75
Estimated cost using weighted average historical price	\$2.5 x 100 units = \$250	\$2.5 x 150 units = \$375	\$2.5 x 50 units = \$125
<b>Savings (actual – estimated)</b>	<b>\$100</b>	<b>\$150</b>	<b>\$50</b>

Source: GAO.

Based on this calculation, VA would conclude that it had achieved savings of \$150 million. However, \$100 of the \$150 reported in year two represents recurring savings from year one—only \$50 would be incremental savings associated with year two. The same principle would also hold for year three and subsequent years. That is, VA would calculate savings as if each year being considered was the first year of the contract and thereby, report savings on a cumulative rather than incremental basis. If, as reflected in table 3, VA used the incremental savings computation, for year two, \$50 would be reported in incremental savings—capturing only the additional costs avoided associated with increased utilization. Taking this logic a step further, any additional reductions in contract unit costs also should be captured as incremental savings in the first year in which they occur.

Presenting actual savings achieved on a cumulative basis can be misleading because VA compared these savings with the original savings goals, which were reported on an incremental basis. In determining whether VA met its savings goals, VA compared its total achieved savings amount for both its national procurement initiatives and VISN-level initiatives with the assumed savings included VA’s budget justification. However, as shown in table 4, VA reports its achieved savings from its national procurement standardization initiatives on a cumulative basis and, as discussed previously, reports its VISN-level initiatives using a combination of cumulative and annual reporting. In table 4, VA compares these figures with the assumed savings

reflected in VA’s budget justifications for fiscal years 2003 and 2004—which are calculated on an incremental basis.

**Table 4: VA’s Reported Actual Cost Savings Compared with Savings Assumed in VA’s Budget Justifications for Fiscal Years 2003 and 2004**  
Dollars in Millions

Reported management efficiency initiatives	Basis of reporting	Fiscal year 2003	Fiscal year 2004
National procurement standardization initiatives	Cumulative	\$396	\$414
VISN-level initiatives	Cumulative and annual	\$231	\$235
<b>Total reported by VA as realized or achieved</b>	Cumulative and annual	<b>\$627</b>	<b>\$649</b>
<b>Savings assumed in VA’s budget justifications</b>	Annual	<b>\$316</b>	<b>\$634</b>

Source: VHA Office of the CFO.

Although VA does not have a reliable basis for determining whether it has achieved its savings goals, this does not mean that new savings have not occurred or that new savings are not achievable in the future. GAO and the VA OIG have reported<sup>7</sup> that VA’s procurement standardization initiatives have saved hundreds of millions of dollars and concluded that additional savings could be achieved through increased resource sharing—especially in the areas of medical services and joint procurement of medical and surgical supplies. Nonetheless, without a sound methodology for tracking and reporting achieved savings, the true extent of VA’s actual management efficiency savings cannot be determined.

Inefficiencies in VA’s Processes Remain

In recent years, the VA OIG and we identified management inefficiencies that, if unaddressed, could contribute to requests for higher levels of annual appropriations that could otherwise have been avoided. Although VA has instituted a number of procurement reform initiatives aimed at leveraging its purchasing power and improving the overall effectiveness of procurement actions, the VA OIG and we continue to identify problems with VA’s procurement processes as well as VA’s ability to provide timely and reliable cost data needed to measure program efficiency. Further, the VA OIG has identified deficiencies in VA’s procurement practices as one of the agency’s most serious management challenges.

As shown in table 5, recent GAO and VA OIG reports disclosed significant problems with VA’s acquisitions involving FSS contracts; procurement of health care services; VA construction; acquisition support weaknesses; and inadequate management and oversight of major system initiatives—including the implementation of VA’s Core Financial and Logistics System (CoreFLS) and E-Travel service. In addition, recent reviews continue to identify serious control weaknesses in the agency’s inventory management, and shortfalls in the agency’s efforts to provide reliable cost data to

<sup>7</sup>GAO, *Contract Management: Further Efforts Needed to Sustain VA’s Progress in Purchasing Medical Products and Services*, GAO-04-718 (Washington, D.C.: June 22, 2004) and Department of Veterans Affairs, Office of Inspector General, *Audit of VA Medical Center Procurement of Medical, Prosthetic, and Miscellaneous Operating Supplies*, Report No. 02-01481-118 (Washington, D.C.: Mar. 31, 2004).

accurately assess the efficiency and effectiveness of VA’s health care initiatives and programs.

**Table 5: Summary of Recent Reports That Cite Management Inefficiencies at VA**

Reporting issues/findings	Report number
<p>VA is at risk of paying excessive prices for goods and services due to weaknesses identified in VA’s preaward and postaward reviews of FSS proposals and contacts.</p> <p>Based on the results of preaward reviews, VA could negotiate reduced prices totaling over \$1 billion.</p> <p>Based on the results of postaward reviews, \$2.3 million in contractor overcharges were identified, which VA subsequently recovered.</p>	<p>VA OIG, <i>Review of Federal Supply Schedule Proposal Submitted by Sandoz, Inc., Under Solicitation Number M5-Q50A-03</i>, Report No. 04-01682-132 (Washington, D.C.: Apr. 28, 2005).</p> <p>VA OIG, <i>Review of Federal Supply Schedule Proposal Submitted by Eastman Kodak Company Under Solicitation Number M5-Q50A-03</i>, Report No. 04-01763-138 (Washington, D.C.: May 18, 2005).</p> <p>VA OIG, <i>Review of Proposal Submitted by New York University, School of Medicine, Under Solicitation Number RFP 10N3-102-05 for Cardiothoracic Surgery Services at Department of Veterans Affairs, New York Harbor Healthcare System</i>, Report No. 05-01215-146 (Washington, D.C.: May 24, 2005).</p> <p>VA OIG, <i>Review of Federal Supply Schedule Proposal Submitted by BioMerieux Inc., Under Solicitation Number RFP-797-FSS-03-0001</i>, Report No. 05-00452-150 (Washington, D.C.: June 7, 2005).</p>
<p>Recent reports cite weaknesses in VA’s acquisition management processes including poor acquisition planning, inadequate risk management and senior management oversight, conflict of interest violations, poorly written solicitations, excessive prices, and inadequate contract negotiations.</p> <p>VA’s acquisition management processes do not adequately protect the interest of VA or veteran patients and may result in VA paying excessive prices for goods and services.</p>	<p>VA OIG, <i>Evaluation of VHA Sole-Source Contracts with Medical Schools and Other Affiliated Institutions</i>, Report No. 05-01318-85 (Washington, D.C.: February 2005).</p> <p>VA OIG, <i>Audit of VA Medical Center Procurement of Medical, Prosthetic, and Miscellaneous Operating Supplies</i>, Report No. 02-01481-118 (Washington, D.C.: Mar. 31, 2005).</p>
<p>Weaknesses were identified in VA’s contract management, construction contract award, and administration processes.</p> <p>Based on a review of over 30 major construction contracts, the VA OIG determined that several projects valued at \$133.6 million were at risk of being excessively priced.</p>	<p>GAO, <i>Contract Management: Further Action Needed to Improve Veterans Affairs Acquisition Function</i>, GAO-06-144 (Washington, D.C.: Oct. 19, 2005).</p> <p>GAO, <i>Contract Management: Further Efforts Needed to Sustain VA’s Progress in Purchasing Medical Products and Services</i>, GAO-04-718 (Washington, D.C.: June 22, 2004).</p> <p>VA OIG, <i>Department of Veterans Affairs, Office of Inspector General, Audit of VHA Major Construction Contract Award and Administration Process</i>, Report No. 02-02181-79 (Washington, D.C.: February 2005).</p>
<p>Weaknesses were identified in VA’s contracting, acquisition support, and program management for major system development initiatives—including the deployment of VA’s CoreFLS and implementation of E-Travel service.</p> <p>After spending roughly \$249 million on its development of CoreFLS, VA discontinued implementation of the system in</p>	<p>VA OIG, <i>Issues at VA Medical Center Bay Pines, Florida and Procurement and Deployment of the Core Financial and Logistics System (CoreFLS)</i>, Report No. 04-01371-177 (Washington, D.C.: Aug. 11, 2004).</p>

<p>September 2004.</p> <p>VA's E-Travel initiative duplicated the General Services Administration's (GSA) efforts to provide E-Travel service options that all federal agencies must use. The VA OIG reported that the agency could save \$7.4 million over the next 10 years by using one of GSA's approved E-Travel service options.</p>	<p>VA OIG, <i>Review of VA Implementation of the Zegato E-Travel Service</i>, Report No. 04-00904-124 (Washington, D.C.: Mar. 31, 2005).</p>
<p>VA's medical centers did not adequately manage their inventories for medical, prosthetic, engineering, and operating supply requirements—often keeping more than the maximum 30-day standard supply level on hand.</p> <p>VA could potentially reduce excess inventories and save hundreds of millions of dollars in funds that are tied up in maintaining excess inventories.</p>	<p>VA OIG, <i>Summary of Combined Assessment Program Reviews at Veterans Health Administration Medical Facilities October 2003 through September 2004</i>, Report No. 04-03310-94 (Washington, D.C.: Mar. 7, 2005).</p>

Source: Summary of GAO and VA OIG reports.

Finally, in our recent report and testimony<sup>8</sup> on VA's managerial cost accounting practices, we raised concerns about the completeness and accuracy of nonfinancial data VA routinely uses to generate cost information to support decisions relating to internal budgeting; resource allocation; performance measurement; and cost finding for programs, activities, and outputs. We found that VA was unable to readily produce documentation that describes the mechanism used to assign costs to cost objects. We concluded that such inaccurate nonfinancial data could skew cost calculations and any resulting managerial decisions, and limit the reliability of data used by management to analyze and properly assign costs.

### Conclusion

As with most federal agencies, VA is under increasing pressure to find ways to do more with less. To reduce amounts requested for annual appropriations, VA has relied, in part, on anticipated savings resulting from management efficiency initiatives. However, without a sound methodology for projecting management efficiency savings VA runs the risk of falling short of its management efficiency savings goals, which may ultimately require VA to take actions—including revisiting the assumptions, priorities, and levels of service assumed in the budget—to stay within its level of available resources. If VA continues to rely on management efficiencies as a means of savings, a sound and well-documented methodology for consistently and accurately reporting both projected and achieved savings related to management efficiency initiatives will be an important factor in providing reliable information for congressional decision makers.

<sup>8</sup>GAO, *Managerial Cost Accounting Practices: Leadership and Internal Controls Are Key to Successful Implementation*, GAO-05-1013R (Washington, D.C.: Sept. 2, 2005) and *Managerial Cost Accounting Practices: Departments of Labor and Veterans Affairs*, GAO-05-1031T (Washington, D.C.: Sept. 21, 2005).

## Recommendations for Executive Action

If VA continues to plan and budget for management efficiency savings, we recommend that the Secretary of Veterans Affairs should direct the Assistant Secretary for Management to

- develop a methodology to project savings for management efficiency initiatives that provides key data and assumptions used to estimate the savings.

To better determine whether management efficiency savings are being achieved as planned, we recommend that the Secretary of Veterans Affairs should direct the Assistant Secretary for Management to establish methodologies for tracking and reporting actual savings achieved through implementation of proposed management efficiencies, including

- clear criteria for what constitutes savings resulting from management efficiencies,
- controls to ensure that actual savings are reported on the same basis as projected savings in the budget request, and
- documentation of such savings.

## Agency Comments and Our Evaluation

In its written comments, which are reprinted in enclosure II, VA concurred with our recommendations and said that VA's Assistant Secretary for Management will establish processes and procedures to ensure proper documentation of savings and a methodology on how realized savings should be tracked and reported. However, VA disagreed that it used its management efficiency savings goals to fill the gap between the cost associated with VA's projected demand for health care services and the amount the President was willing to request. It said that identifying goals, setting challenging targets, and forecasting management efficiency savings are entirely appropriate for a large health care organization like VA.

We agree that VA and other federal agencies have a basic responsibility to identify goals, set challenging targets, and forecast management efficiency savings. However, VA management officials, in three separate interviews, uniformly described VA's process for determining its management efficiency savings goals in terms of filling the gap between the cost associated with VA's projected demand for health care services and the amount the president was willing to request. At the time of our review, VA did not provide another explanation and was unable to provide us with any support for the methodology used to develop its management efficiency savings goals. Therefore, we continue to believe that this characterization is appropriate. VA also provided technical comments for which we have revised our report, as appropriate, as shown in enclosure II.

We are sending copies of this report to the Secretary of Veterans Affairs, interested congressional committees, and other interested parties. We will make copies of the report available to others upon request. This report is also available at no charge on GAO's home page at <http://www.gao.gov>.

If you or your staff have any questions about this report, please contact me at (202) 512-9095 or [williamsm1@gao.gov](mailto:williamsm1@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff making major contributions to this report are listed in enclosure III.

A handwritten signature in cursive script that reads "McCoy Williams".

McCoy Williams  
Director, Financial Management and Assurance

Enclosures - 3

## Enclosure I

### Objective, Scope, and Methodology

To examine the Department of Veterans Affairs' (VA) methodology for determining the projected management efficiency savings assumed in the President's budget requests for fiscal years 2003 through 2006 and VA's support for reported actual management efficiency savings achieved—including methodology and documentation used to track and report achieved savings, we interviewed various VA officials from the Veterans Health Administration (VHA) Office of the Chief Financial Officer, including the Deputy Chief Financial Officer, Budget Office Director, and chief financial officers for all 21 Veterans Integrated Service Networks (VISN), who were responsible for documenting and reporting projected and realized management efficiency savings at VA. We also interviewed officials responsible for implementing VA's National Pharmaceutical/Pharmacy and Medical Supplies and Equipment Procurement Initiatives—which accounted for over half of VA's reported management efficiency savings during fiscal years 2003 through 2006, including the Chair of the former VA Procurement Reform Task Force, Chief and Deputy Chief Consultants for the Pharmacy Benefits Management Strategic Healthcare Group, Chief of the Prosthetics and Clinical Logistics Office, Deputy Chief of the Clinical Logistics Office, and Chief for the Office of Information Technology.

In addition, we obtained and analyzed VA's congressional budget justifications; documentation provided by VA officials in support of its projected and achieved in savings, including guidance provided to each of the VISNs on reporting management efficiency savings; documents and spreadsheets used to collect and report efficiency savings for fiscal years 2003 through 2006; and documentation of VA's approach for calculating efficiency savings amounts. To obtain a broader view of the VA's national procurement initiatives, we reviewed VA's Procurement Reform Task Force report (May 2002) and other documents relating to the Procurement Reform Task Force initiatives.

To summarize prior GAO and VA Office of the Inspector General (OIG) reports that have identified management inefficiencies at VA, we reviewed GAO and VA OIG reports issued during fiscal years 2003 through 2006 that addressed management challenges and inefficiencies in VA's health care programs, processes, and related health care activities.

We conducted our work from September 2005 to January 2006 in accordance with U.S. generally accepted government auditing standards. We requested comments on a draft of this report from the Secretary of Veterans Affairs or his designee. We received written comments from the Deputy Secretary of Veterans Affairs and have reprinted VA's comments in enclosure II.

Comments from the Department of Veterans Affairs



THE DEPUTY SECRETARY OF VETERANS AFFAIRS  
WASHINGTON

January 30, 2006



Mr. McCoy Williams  
Director, Financial Management and Assurance  
U.S. Government Accountability Office  
441 G Street, NW  
Washington, DC 20548

Dear Mr. Williams:

The Department of Veterans Affairs (VA) has reviewed your draft report, **VETERANS' AFFAIRS: Limited Support for Reported Health Care Management Efficiency Savings** (GAO-06-359R).

VA agrees with the report's two recommendations: that we should develop an improved methodology to project savings for management efficiency initiatives, and develop an improved methodology for tracking and reporting actual savings achieved through implementation of proposed management efficiencies. The enclosure provides additional discussion on the recommendations.

However, I disagree with the report's characterization that management efficiencies savings were assumed simply to "fill the [budget] gap." I believe that identifying goals, setting challenging targets and forecasting management efficiency savings is entirely appropriate for a large health care organization like VA. Proper stewardship of taxpayer resources requires that VA strive to become more effective and more efficient in delivering timely, high-quality health care for our veterans. As an example, your report points out that both GAO and VA's Office of the Inspector General have reported recently that VA's procurement standardization initiatives have saved hundreds of millions of dollars.

While VA can and will work to improve our methodologies, your report accurately states that a lack of perfect methodologies "does not mean that new savings have not occurred or that new savings are not achievable in the future."

VA appreciates the opportunity to comment on your draft report.

Sincerely yours,

Gordon H. Mansfield

Enclosure

See comment 1.



Enclosure

THE DEPARTMENT OF VETERANS AFFAIRS (VA) COMMENTS  
TO GOVERNMENT ACCOUNTABILITY OFFICE (GAO)  
DRAFT REPORT  
**VETERANS' AFFAIRS: Limited Support for Reported Health Care Management  
Efficiency Savings**  
(GAO-06-359R)

**If VA continues to plan and budget for management efficiency savings, we recommend that the Secretary of VA direct the Assistant Secretary for Management to**

- **Develop a methodology to project savings for management efficiency initiatives that provides key data and assumptions used to estimate the savings.**

**To better determine whether management efficiency savings are being achieved as planned, we recommend that the Secretary of VA direct the Assistant Secretary for Management to establish methodologies for tracking and reporting actual savings achieved through implementation of proposed management efficiencies-including:**

- **Clear criteria for what constitutes savings resulting from management efficiencies,**
- **Controls to insure that actual savings are reported on the same basis as projected savings in the budget request, and**
- **Documentation of such savings.**

**Concur** – VA fundamentally agrees with GAO's recommendations and will take the necessary steps to develop procedures and guidance for VA Central Office and the Veterans Health Administration to achieve the stated objectives. VA believes it is essential and reasonable to pursue management efficiencies and their resulting savings as part of the budgetary process. Within a health care organization the size of VA's, there exists the potential for savings. Therefore, it is incumbent upon VA to establish a formal process for defining and securing these savings on an annual basis. By developing a methodology for efficiency initiatives through budgeting, tracking, reporting, and documenting, VA can substantiate and realize valid savings. VA's Assistant Secretary for Management will establish processes and procedures to assure the proper documentation is identified and how the realized savings should be tracked and reported.

**Comments** – VA has realized a significant portion of the potential efficiency savings projected in the President's budget requests covering fiscal years 2003 through 2005. The report states "GAO and the VA OIG have reported recently that VA's procurement standardization initiatives have saved hundreds of millions of dollars...." Additional savings have resulted from the purchase of pharmaceuticals; medical supplies,

See comment 1.

Enclosure

THE DEPARTMENT OF VETERANS AFFAIRS (VA) COMMENTS  
TO GOVERNMENT ACCOUNTABILITY OFFICE (GAO)  
DRAFT REPORT  
**VETERANS' AFFAIRS: Limited Support for Reported Health Care Management  
Efficiency Savings**  
(GAO-06-359R)  
(Continued)

equipment and prosthetics; and information technology hardware and software, as well as local VISN efficiencies and resource sharing.

The data to support efficiency savings come from four major groups:

- the Pharmacy Benefits Management Strategic Healthcare Group,
- the Office of Prosthetics and Clinical Logistics Group,
- the Office of Information Systems, and
- the local VISN organizations.

However, VA needs to develop a standard methodology and process for accurately documenting and reporting these efficiencies in the future.

Technical Corrections: There are some inaccuracies in the draft report:

- (1) On page 1, footnote #2 states that "Agencies submit these materials for review and approval to OMB, which provides the final version to the Congress." This is incorrect; VA and not OMB transmits the materials to Congress.
- (2) Throughout the document, the reference to the VA Office of the CFO should instead reference the VHA Office of the CFO.
- (3) On page 6, the last paragraph states "VA also does not have adequate support for the \$1.3 billion it reported...for fiscal years 2003 and 2004." The amount should be \$950 million.
- (4) We disagree with the GAO finding that the calculation of accumulated savings is not accurate due to the inconsistent reporting of incremental and recurring savings. Rather, it is due to the method VA uses for developing the budget using a base year that is 3 years prior to the budget year, and the changes from the base year to the budget year are both incremental and recurring.
- (5) We disagree with the statement that cost-cutting measures or efficiencies are not consistent with providing the same or higher quality care (this appears in three places: on page 3, first paragraph, second sentence; page 7, third paragraph, last sentence; and page 8, second paragraph, second sentence).

See comment 2.

See comment 3.

See comment 4.

See comment 5.

See comment 6.

The following are GAO's comments on VA's letter dated January 30, 2006.

GAO Comments

1. See the Agency Comments and Our Evaluation section of this report.
2. Although our footnote is intended to provide an overview of the budget process followed by executive branch agencies—not VA's specific process—we have removed the reference to OMB's role in transmitting agencies' budget justifications to the Congress.
3. Our report now references the VHA Office of the CFO.
4. Based on the documentation provided by VA officials, VA reported actual management efficiency savings achieved of \$1.3 billion for fiscal years 2003 and 2004. Management efficiency savings amounts assumed in the President's budget requests for fiscal years 2003 and 2004 totaled \$950 million.
5. We recognize that VA's budget justifications include both an incremental and a recurring component. However, we continue to believe that VA's use of its savings calculation for its national procurement initiatives is misleading because VA calculates actual savings for these initiatives on a cumulative basis and compares these savings figures with savings goals that are reflected on an incremental basis.
6. We reaffirm our view that reductions in workforce, delays in hiring, and reductions in overtime and available resources due to budget cuts are cost-cutting measures—not management efficiencies—and therefore are not consistent with VA's objective of providing the same or higher quality and quantity of service at a lower cost.

Enclosure III

GAO Contact and Staff Acknowledgments

McCoy Williams, (202) 512-9095

Acknowledgments

In addition to the contact named above, Diane Handley, Assistant Director; Fannie Bivins, Francine DelVecchio, Denise Fantone, Carmen Harris, James Musselwhite, Tiffany Tanner, and Michael Tropauer made key contributions to this report.

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