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United States Government Accountability Office  
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July 6, 2007

The Honorable Christopher Shays  
Ranking Member  
Subcommittee on National Security and Foreign Affairs  
Committee on Oversight and Government Reform  
House of Representatives

The Honorable Dennis J. Kucinich  
House of Representatives

Subject: *Sales of Sensitive Military Property to the Public*

Each year the Department of Defense (DOD) sells millions of dollars worth of excess property to the public through a Web site run by its contractor, Government Liquidation. Before excess property can be sold on this site, it is DOD policy to screen the property to ensure it cannot be reutilized by the department in another location or that its sale would not result in sensitive military property becoming publicly available. DOD assigns demilitarization codes to sensitive military property so that, when the property is no longer in use, it is recognized and disposed of properly. However, on several prior occasions—most recently at a July 2006 hearing—we reported that management control breakdowns in DOD’s excess property reutilization program resulted in the sale of sensitive military property to the public through the liquidation Web site,<sup>1</sup> including property subject to demilitarization controls (demil-required property) such as F-14 aircraft parts. One country with operational F-14s, Iran, is known to be seeking these parts. If such parts were publicly available, it could jeopardize national security.

At the July 2006 hearing, DOD officials testified that they would take action to prevent the improper sale of sensitive military property, including demil-required property. Given the seriousness of the security risk posed by the sale of sensitive military property to the public, you requested that we investigate whether (1) demil-required property was still being sold on DOD’s contractor-run liquidation Web site and (2) whether DOD has taken steps to prevent further improper sales of sensitive items, including controlled and demil-required property.

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<sup>1</sup>GAO, *DOD Excess Property: Control Breakdowns Present Significant Security Risk and Continuing Waste and Inefficiency*, [GAO-06-981T](#) (Washington, D.C.: July 25, 2006).

To perform this investigation, we relied primarily on the national stock numbers (NSN)<sup>2</sup> DOD assigns to each property item. Relying on the NSN created some limitations to our investigation—for example, if an item was coded improperly, we would not have been able to identify it. To determine whether DOD had taken steps to prevent the improper sale of sensitive military property to the public, we obtained and reviewed information from the Defense Reutilization and Marketing Service (DRMS), which is part of DOD. The limitations to our investigation are discussed more fully in the Scope and Methodology section below. We conducted our work from September 2006 through June 2007 in accordance with quality standards for investigations as set forth by the President’s Council on Integrity and Efficiency.

## **Results in Brief**

After monitoring excess property sales for about 7 months, we concluded that DOD has made significant improvements in preventing the sale, through the contractor-run liquidation Web site, of property coded as being demil-required. During the first month of our investigation, in September 2006, we determined that DOD had sold 295 items coded as being demil-required to the public. Although a number of demil-required items were offered for sale on the liquidation Web site after September 2006, these items were detected by DOD or the contractor and the property was withdrawn prior to sale.

Furthermore, DRMS reported that, between August 2006 and March 2007, 59,762 line items of demil-required and sensitive property were removed from the excess property disposal system prior to sale, representing a total of 1.3 million individual pieces of demil-required or other sensitive property items.<sup>3</sup> This included items that would have been sold on the liquidation Web site. DOD told us that it has taken steps to prevent further improper sales by implementing various controls, including

- restructuring the batch lot processes (the way property is grouped into lots for sale),
- increasing scrutiny of property before sale,
- tightening controls on the release of property,
- creating a postsale review and retrieval process to account for improper sales, and

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<sup>2</sup>An NSN is a 13-digit number that identifies standard use inventory items. The first 4 digits of the NSN represent the Federal Supply Classification, such as 8430 for men’s footwear, followed by a 2-digit North Atlantic Treaty Organization (NATO) code and a 7-digit designation for a specific type of boot, such as cold weather boot.

<sup>3</sup>As of May 31, 2007, 105,655 line items of demil-required and sensitive property had been removed from public sale representing 2.4 million individual pieces of demil-required or other sensitive property removed from the disposal stream, according to the Defense Logistics Agency.

- newly designating some property items as controlled and taking steps to prevent their sale to the public.

Although DRMS has clearly taken a proactive approach to identifying and removing sensitive items from its system, we determined that approximately 1,400 items newly designated as controlled property were sold to the public in February 2007. DRMS told us the parts were sold to the public because it did not successfully update its automated control list and remove these items prior to their being listed on the Web site. DRMS had identified these items as parts that could be used on the F-14 fighter aircraft.

### **Scope and Methodology**

We focused our work on demil-required property, non-demil-required F-14 parts, and non-demil-required technology related to the F-14. To determine if controlled or demil-required property continued to be sold to the public, we obtained the NSN for approximately 10 million property items sold by DOD's contractor from September 2006 through March 2007. We then compared the NSNs to database files of property that was coded as controlled or demil-required. The control files we used included Federal Logistics Information System (FLIS) data, which was used to identify the demilitarization code for military equipment and property items, a control file of defective or nonconforming property, and other control files listing parts and technology associated with the F-14 fighter aircraft. If the NSN of property offered for sale matched those in the control files, we monitored the sales event to determine whether the property was sold or removed from the liquidation Web site prior to sale.<sup>4</sup>

We have used the data contained in the FLIS and Defense Logistics Agency excess property databases in our prior work and found them to be reliable. Consequently, for the purposes of the analyses performed in this investigation, we determined the data to be reliable with certain limitations. These limitations result from our use of NSNs listed on the contractor-run Web site. First, we did not attempt to review the DOD system that assigns demilitarization categories to military property, meaning that we accepted the coding system as it exists currently. Second, we could not account for coding errors in the process of listing property on the Web site, meaning that demil-required property may have been sold during this time period because they were not coded properly. Finally, about 10 percent, or approximately 1 million property items offered for sale during our investigation, did not have a valid NSN, and for these we were unable to make a comparison to control files. These items had either an incomplete NSN or a local stock number (LSN).<sup>5</sup> Given a partial NSN, we were often able to identify the type of property being sold.

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<sup>4</sup>During this investigation we reviewed only those items listed for sale on the Government Liquidation Web site. We did not investigate items throughout the entire excess property disposal system.

<sup>5</sup>An LSN consists of the four-digit federal supply classification number, a two-digit NATO code, and up to a seven-character description, such as "monitor" for a computer monitor and "boots" for cold weather boots.

To determine whether DOD had taken steps to prevent the improper sale of sensitive military property to the public, we gained an understanding of the controls that DOD had implemented and those planned in the future, reviewed DOD's statistics on the number of sensitive property items it identified and removed from its excess property disposal system, and received briefings from DRMS officials on their progress. We also monitored DRMS actions to implement improvements in excess property systems, processes, and controls.

DOD was given an opportunity to review a draft of this report and provide comments. In providing oral comments, DOD officials agreed with our investigative results and conclusions.

## **Background**

In 2002 we reported on serious breakdowns in management processes, systems, and controls that resulted in substantial waste and inefficiency in DOD's excess property reutilization program or significant vulnerabilities involving the release of sensitive military property. Our June 2002<sup>6</sup> testimony revealed that DOD sold excess chemical and biological protective gear at the same time it was procuring these garments. Then, in a November 2003<sup>7</sup> report, we described how we established a fictitious company and purchased over the Internet, from DOD's liquidation contractor, key excess DOD biological equipment and related protective clothing necessary to produce and disseminate biological warfare agents.

In a May 2005 report,<sup>8</sup> we noted that DOD claimed nearly \$500 million in lost, damaged, and missing excess property from fiscal years 2002 through 2004, including demil-required property, such as chemical and biological protective suits, body armor, and guided missile warheads. This report also included information on continued waste and inefficiency in DOD's reutilization program. To illustrate this point, our undercover investigator used a fictitious identity to purchase over the Internet, from DOD's liquidation contractor, new and unused excess military property that DOD continued to buy and utilize. Over a year later, in July 2006,<sup>9</sup> we reported that our undercover investigator purchased sensitive military equipment items that were improperly sold to the public by DOD's liquidation contractor. These items included body armor inserts, known as SAPIs, which were currently in demand by U.S. soldiers in Iraq and Afghanistan; a time-selector unit used to ensure the accuracy of computer-based equipment, such as global positioning systems and system-level clocks; digital microcircuits used in F-14 fighter aircraft; and numerous other controlled items. We also identified nearly 80 individuals who purchased over 2,500

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<sup>6</sup>GAO, *DOD Management: Examples of Inefficient and Ineffective Business Processes*, [GAO-02-873T](#) (Washington, D.C.: June 25, 2002).

<sup>7</sup>GAO, *DOD Excess Property: Risk Assessment Needed on Public Sales of Equipment That Could Be Used to Make Biological Agents*, [GAO-04-15NI](#) (Washington, D.C.: Nov. 19, 2003).

<sup>8</sup>GAO, *DOD Excess Property: Management Control Breakdowns Result in Substantial Waste and Inefficiency*, [GAO-05-277](#) (Washington, D.C.: May 13, 2005).

<sup>9</sup>GAO, *DOD Excess Property: Control Breakdowns Present Significant Security Risk and Continuing Waste and Inefficiency*, [GAO-06-943](#) (Washington, D.C.: July 25, 2006).

sensitive items from DOD's liquidation contractor between November 2005 and June 2006. These sensitive excess military items should not have been sold to the public.

### Demil-Required Property Sales

After monitoring excess property sales for about 7 months, we concluded that DOD has made significant improvements in preventing the sale, through the contractor-run liquidation Web site, of property coded as being demil-required. Throughout our investigation, we detected items that were coded as being controlled or demil-required, but DRMS or the liquidation contractor regularly identified the same property items and removed them from the liquidation Web site before they were sold. In September 2006, we detected the sale of 295 military items coded as being demil-required, including F-14 parts that should not have been sold to the public.<sup>10</sup> We referred pertinent information about these sales to the Defense Criminal Investigative Service (DCIS) and Immigration and Customs Enforcement (ICE), a branch of the Department of Homeland Security, for review and appropriate action. More detailed information on the number of demil-required property items and our results by month are provided in the following table.

**Table 1: Results of Testing for the Sale of Demil-Required Property on Liquidation Web Site**

Month and year	Number of property items offered for sale	Number of property items tested (items with an NSN)	Percent of property that was tested	Number of demil-required items actually sold
September 2006	697,889	587,796	84	295
October 2006	551,894	470,277	85	0
November 2006	3,172,916	2,888,118	91	0
December 2006	1,662,949	1,416,766	85	0
January 2007	1,411,296	1,294,750	92	0
February 2007	1,183,428	1,088,941	92	0
March 2007	2,704,962	2,504,011	93	0
<b>Total</b>	<b>11,385,334</b>	<b>10,250,659</b>	<b>90</b>	<b>295</b>

Source: GAO analysis of DOD data.

As discussed in the Scope and Methodology section above, there were some limitations to using the NSNs listed on the contractor-run Web site for our investigation. First of all, we did not attempt to review the DOD system that assigns demilitarization categories to military property, meaning that we accepted the coding system as it exists currently. Second, we could not account for coding errors in the process of listing property on the Web site, meaning that demil-required property may have been sold during this period because they were not coded properly. Finally, about 10 percent, or approximately 1 million property items offered for sale during our investigation, did not have a valid NSN, and for these we were unable to make a comparison to control files. Many of these items often had a partial stock number, indicating that they were generally office and computer equipment, furniture, parts,

<sup>10</sup>Of these 295 items, 216 were demil category D (requiring total destruction) and 79 were demil category C (requiring demilitarization through the removal of key points, parts, components, or accessories).

and machinery. Usually this type of property is offered for sale in batch lots. However, the lack of valid NSNs increases the risk that demil-required property may not have been identified and processed correctly. According to DRMS, it has tried to reduce this risk by performing a physical inspection of property with an incomplete NSN or an LSN. DRMS said it excludes any item from sale if the proper demilitarization code cannot be determined.

### **DRMS Corrective Actions**

DRMS reported that, between August 2006 and March 2007, it removed 59,762 line items of demil-required and sensitive property from the excess property disposal system prior to sale, representing a total of 1.3 million individual pieces of demil-required or other sensitive property items.<sup>11</sup> DOD told us that it has taken steps to prevent further improper sales by implementing various controls, including

- restructuring the batch lot processes (the way property is grouped into lots for sale) by consolidating it at four locations and performing a physical inspection of all property,
- increasing scrutiny of property before sale,
- tightening controls on the release of property,
- creating a postsale review and retrieval process to account for improper sales, and
- newly designating some property items as sensitive and taking steps to prevent their sale to the public.

To increase scrutiny on property before sale, DRMS told us that it took the following actions:

- Modified its contract with the liquidation company in September 2006 to include incentives and disincentives based on performance. Under the terms of the new contract, if the company discovers export-controlled property or demil-required property and removes it from the Web site prior to sale, it is rewarded financially. DRMS told us that, if such property is sold by the contractor, there are financial penalties.

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<sup>11</sup>Note that we reviewed only items listed for sale on the Government Liquidation Web site and did not investigate items throughout the entire excess property disposal system. Moreover, our review was limited to the period of September 2006 through March 2007. As of May 31, 2007, 105,655 line items of demil-required and sensitive property had been removed from public sale representing 2.4 million individual pieces of demil-required or other sensitive property removed from the disposal stream, according to the Defense Logistics Agency.

- Increased screening of property before sale by performing automated reviews of the property being sold on the liquidation Web site and dedicating staff to physically review the site.
- Match, before it is sold, all property to a specific list of property types that should not be sold. Included in DRMS and contractor verification efforts is a daily automated screening of the entire inventory of FLIS to detect any changes in demilitarization codes.

Furthermore, DRMS told us that it has also strengthened controls in the release of property to minimize the risk of unauthorized release to walk-in customers. To address future situations in which new NSNs are added to control lists or changes in demilitarization codes occur, DRMS told us that it has established a postsale review process to identify and recover any property that, after sale, is determined to be sensitive or demil-required. In these situations, DRMS told us that the liquidation contractor contacts the customer to reacquire the property.

During the course of our investigation we learned that additional property items were determined to be sensitive by the Defense Logistics Agency and should not be sold on the Government Liquidation Web site. DOD has a separate listing of controlled military property, which includes non-demil-required items such as uniforms, lab equipment, defective property, and non-demil-required F-14 parts. When we obtained an updated list of controlled military property with property items that had been newly designated as sensitive, we screened Web site sales and compared it with the new list. We then determined that approximately 1,400 newly designated sensitive items were sold to the public in February 2007.<sup>12</sup> Although these were not demil-required property items, they were identified as parts that could be used on the F-14 fighter aircraft. DRMS told us that it added these parts to its control list; however, the automated system that screens property sold on the Web site was not properly updated to reflect the additional property items. DRMS reported that this problem was resolved in March 2007 and that it has reacquired (or is in the process of reacquiring) these property items. In some cases, however, accountability for the property may have been lost since some customers have denied receiving the property and the government contractor is unable to locate it. According to DRMS, the contractor is researching the sales to determine whether the property was in fact released to the customer.

## **Conclusion**

DOD has made significant progress in preventing demil-controlled and sensitive property from being sold through the Government Liquidation Web site. However, we did observe two occasions where demil-required and controlled property was sold

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<sup>12</sup>Of these 1,385 items, 1,362 were demil category A (no demilitarization requirements) and 23 were demil category B (no demilitarization requirements but may be subject to trade security controls).

after DOD had implemented new controls. The postsale review process DOD is implementing may help it recover many of the improperly sold items. Nevertheless, as DOD moves forward identifying additional items that could be considered sensitive, it is important for program managers to test controls and provide oversight at the implementation phase.

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As agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies to the Director of the Defense Logistics Agency. We will provide copies to others on request, and the report is available at no charge on GAO's Web site at <http://www.gao.gov>. GAO staff who made key contributions to this report are Mario Artesiano, Andrew McIntosh, Richard Newbold, John Ryan, and Viny Talwar. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. If you or your staffs have any questions about this report, please contact me at (202) 512-9505 or [kutzg@gao.gov](mailto:kutzg@gao.gov).

A handwritten signature in black ink that reads "Gregory D. Kutz". The signature is written in a cursive style with a large, stylized initial "G".

Gregory D. Kutz  
Managing Director  
Forensic Audits and Special Investigations

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