The Department of Defense, in commenting on our draft report, in July 1967, concurred, in general, with our findings.

Chairman PROXMIRE. You say "in general." What disagreements were there?

Mr. WEITZEL. With the need for high-level management attention to the inventories, the importance and concern to the Department.

Chairman PROXMIRE. Did they disagree with that?

Mr. WEITZEL. No; they agreed in general.

Chairman PROXMIRE. My question was, What disagreements?

Mr. WEITZEL. The only point they reserved for further study, as I recall, was whether there should be established the high-level management group of the representatives from the military departments and Defense Supply Agency. They indicated they wanted to make a further study of that point. That is the one Mr. Staats said they have now agreed with.

Mr. STAATS. We should strike out the words "in general" in view of the information we received yesterday.

We were advised that each of the military services and DSA had initiated specific programs to eliminate the types of inventory control problems discussed in our report and each was in the process of installing new procedures which were aimed at more accurate inventory control.

I think this point was the reason that they did question the need at that point in time for the overall task force, but which they have now agreed to.

We were advised that the installation of the new procedures had advanced to the point where fruitful results could be anticipated within a relatively short period of time. We were told that the need for establishment of a special inventory study group would be reconsidered and, if necessary, organized after an evaluation of the results was obtained from the new procedures.

In testimony before this subcommittee on November 28, 1967, the Defense representatives testified that the material included in our report dealt with discrepancies that show up in a 4 million item inventory. The Defense representatives went on to say that the net difference between gains and losses in dollars was only 1 percent in 1965 and 1.4 percent in 1966 and that the largest merchandising houses consider 2 percent net adjustment to be quite satisfactory. (See p. 220.)

We recognize that in private industry a net adjustment figure (gains offset by losses) can be used to measure the extend to which profit or loss has been affected during a particular accounting period or the extent to which capital investment in inventories has been affected by inventory adjustment. However, this figure does not give a satisfactory indication of the effectiveness of inventory controls or the reliability of the inventory records. For these purposes, gross adjustment (the total of gains and losses) is a more meaningful figure.

An excessive volume of gross inventory adjustments is a clear indication that, in a large number of instances, the inventory accounts for specific items were inaccurate in relation to actual stocks on hand and, therefore, represented potential management problems.

In those cases where records indicate more stock on hand than actually exists, there is a distinct danger that when stocks are depleted,