



DEPARTMENT OF DEFENSE

AUDIT REPORT

ADMINISTRATION OF THE CONTRACT CLOSEOUT PROCESS
AT THE
DEFENSE CONTRACT MANAGEMENT DISTRICT MID ATLANTIC

No. 91-064

March 20, 1991

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INSPECTOR GENERAL
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March 20, 1991

MEMORANDUM FOR DIRECTOR, DEFENSE LOGISTICS AGENCY
COMMANDER, DEFENSE CONTRACT MANAGEMENT DISTRICT
MID ATLANTIC

SUBJECT: Report on the Audit of the Administration of the
Contract Closeout Process at the Defense Contract
Management District Mid Atlantic (Report No. 91-064)

This is our final report on the Audit of the Administration of the Contract Closeout Process at the Defense Contract Management District Mid Atlantic (DCMDM) (formerly the Defense Contract Administration Services Region, Philadelphia), submitted for your information and use. Comments from the Defense Logistics Agency (DLA) on a draft of this report were considered in preparing the final report. This is the second in a series of reports issued as part of a Government-wide President's Council on Integrity and Efficiency audit of the contract closeout process. The audit was made from September 1989 through January 1990. The objectives of the audit were to determine the timeliness of the contract closeout process, the validity of unliquidated obligations on contracts awaiting closeout, and the timeliness of collections of any refunds due on incentive contracts with cost underruns. As part of the audit, we also evaluated internal controls over the contract closeout process. As of May 31, 1989, the Contract Administration Report at DCMDM showed that administrative contracting officers were administering 85,010 contracts, and that 31,291 of these contracts were complete and awaiting contract closeout. The 31,291 contracts had \$836.5 million of unliquidated obligations.

The contract closeout process at DCMDM was not effective for closing contracts in a timely manner, for removing excess funds from contracts, and for recovering overpayments on incentive contracts. The audit showed that DCMDM, as well as its parent organization, DLA, took actions to improve the closeout process. While those actions were commendable, the contract closeout process remained untimely. The results of the audit are summarized in the following paragraphs, and the details, audit recommendations, and management comments are in Part II of this report. The complete text of the comments is in Appendix A.

DCMDM did not close contracts in a timely manner. Delays in contract closeout created a backlog of about 11,700 overage contracts with an estimated \$166.2 million in unliquidated obligations. We recommended that a working group be formed to close all overage contracts in section 2 (contracts that were physically complete and awaiting closeout) and section 4

(contracts that were closed and reopened for payment adjustments) of the Contract Administration Report. We also recommended that the ACO's be held accountable for the contract closeout process through their performance plans (page 5).

Administrative contracting officers did not make required fund reviews on 86 percent of the physically complete contracts reviewed to determine whether the contracts had unliquidated obligations that could be released and reused for other purposes. As a result, \$3.5 million could have been deobligated, but was not. A total of \$3.3 million of the \$3.5 million was stock fund money that could be reused. In addition, there were overstated obligations of \$36.9 million and understated disbursements of \$7.3 million. We recommended that DLA revise its DLA Manual (DLAM) 8105.1, "Contract Administration Manual for Contract Administration Services," September 22, 1988, to include procedures specifying how to conduct fund reviews and update training curriculum to include the new fund review procedures. We also recommended that DCMDM request procurement offices to deobligate \$3.5 million (page 11).

Administrative contracting officers were late in recovering overpayments to contractors totaling \$363,000 on three fixed-price incentive contracts. Delays in recovering the overpayments cost the Government an estimated \$60,600 in interest and exposed the Government to the unnecessary risks associated with debt collection. DLA concurred with the recommendation and has collected the three overpayments (page 15).

Since the completion of this audit, a new law has been instituted that directly impacts contract closeout. The FY 1991 Appropriation Act changed the way expired funds and M Accounts are handled. The new rules place specific time limits on the availability of appropriated monies. After the time expires, all balances are canceled and obligations outstanding must be charged to a current appropriation. There will no longer be any M Accounts. These changes make timely contract closeout an essential part of contract management. DLA has provided guidance to field activities emphasizing the importance of closing contracts on time (Appendix D). We expect that the timeliness of contract closeout will improve as a result of the new rules for funds availability.

Draft report Recommendations A.1.a. and A.1.b. were deleted from the report based on discussions with DLA officials concerning actions and procedures in effect. See the draft report dated July 19, 1990, page 18, for the text of the draft recommendations. See Appendix A for the complete text of DLA's comments. Draft report Recommendations A.2.a., A.2.b., and A.2.c. were renumbered sequentially in the final report.

DLA partially concurred with Recommendation A.1.a. (formerly draft report Recommendation A.2.a.) in this report, to establish a working group to close overage contracts in sections 2 and 4 of

the Contract Administration Report. DCMDM is establishing a Quality Management Board to close out all overage contracts in section 4 of the Contract Administration Report. Section 2 contracts were excluded since only normal closeout actions were pending. Our audit indicated that normal closeout actions were not accomplished in a timely manner. DLA offered no evidence that the problem will improve without assistance to the administrative contracting officers. We request that the Director, DLA, reconsider the position and provide additional comments to the final report addressing closeout of contracts in section 2 of the Contract Administration Report. DLA concurred with Recommendation A.1.b. in this report. Draft Recommendation A.2.c. (final report Recommendation A.1.c) was revised, and we request that the Director, DLA, provide additional comments to the final report on the revised recommendation.

DLA nonconcurred with Recommendation B.1. to add fund review information to DLAM 8105.1. DLA interpreted our recommendation to require that step-by-step instructions be included in DLAM 8105.1. This was not our intent. We clarified the intent in discussions with DLA officials and request that the Director reconsider the position and provide additional comments to Recommendation B.1. in this report. DLA partially concurred with Recommendation B.2.a. and concurred with Recommendation B.2.b. Funds have been deobligated or will be deobligated when DCAA audits are complete. We request additional comments on Recommendation B.2.a. in the final report based on the clarification of Recommendation B.1. Additional comments on Recommendation B.2.b. in the final report are not required.

The audit also identified internal control weaknesses as defined by Public Law 97-255, Office of Management and Budget Circular A-123, and DoD Directive 5010.38. Specifically, we identified weaknesses in the controls for closing contracts in a timely manner, for identifying and deobligating excess funds from physically complete contracts, and for recovering overpayments on incentive type contracts. Recommendation A.1.c. in this report, if implemented, will correct the weaknesses and improve the controls over the contract closeout process. We could not determine the monetary benefits to be realized by implementing Recommendation A.1.c. because the recommended action relates to accountability for the contract closeout process rather than to specific contracts that have identifiable dollar values. Copies of this report are being provided to the senior officials who are responsible for internal controls at DLA and DCMDM.

DoD Directive 7650.3 requires that all audit recommendations be resolved promptly. Accordingly, final comments on the unresolved issues in this report should be provided within 60 days of the date of this memorandum.

The courtesies extended to the audit staff are appreciated. If you have any questions on this audit, please contact Mr. Salvatore D. Guli, Program Director, at (703) 614-6285 (AUTOVON 224-6285) or Ms. Linda A. Pierce, Project Manager at (703) 693-0560 (AUTOVON 223-0560). A list of audit team members who participated in the audit is shown in Appendix F. Copies of this report are being provided to the activities listed in Appendix G.



Edward R. Jones
Deputy Assistant Inspector General
for Auditing

Enclosure

cc: Secretary of the Army
Secretary of the Navy
Secretary of the Air Force

REPORT ON THE AUDIT OF THE ADMINISTRATION OF
THE CONTRACT CLOSEOUT PROCESS AT THE DEFENSE CONTRACT
MANAGEMENT DISTRICT MID ATLANTIC

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Prepared by:
Contract Management Directorate
Project No. 9AC-0021

REPORT ON THE AUDIT OF THE ADMINISTRATION OF
THE CONTRACT CLOSEOUT PROCESS AT THE DEFENSE CONTRACT
MANAGEMENT DISTRICT MID ATLANTIC

PART I - INTRODUCTION

Background

The Defense Contract Management District Mid Atlantic (DCMDM) is one of five Defense Contract Management Districts (formerly nine Defense Contract Administration Services Regions) within the Defense Logistics Agency (DLA) that provide contract administration services to DoD and other departments and agencies of the Federal Government. As of May 31, 1989, DCMDM was administering 85,010 contracts with unliquidated obligations of \$13.8 billion.

DCMDM uses an automated system, "Mechanization of Contract Administration Services," (MOCAS) to maintain control over the administration of contracts, including the contract closeout process. The system is designed to allow DCMDM employees to enter various types of basic contract data and actions into the data base for every contract the region administers. Data items and actions include contract numbers, obligation amounts, scheduled delivery dates, contract administration services required by the contract, modifications and changes to the basic contract, actual delivery quantities and dates, and payments. This information permits administrative contracting officers (ACO's) to monitor the status of the contracts, including the status of funds, deliveries, and other administrative actions.

The Contract Administration Report (the Report) is one element of the MOCAS system. The Report is organized into five primary sections. Section 1 contains active contracts on which delivery and acceptance of supplies, performance of services, or periods of performance have not been completed. Section 2 contains physically complete contracts on which delivery of supplies and services are completed and accepted, but contract administration is still pending. Section 3 contains dormant contracts on which one or more of the following are pending: complete terminations for convenience, public law claims, investigations, bankruptcy, litigation, final payments withheld contingent on extended testing after shipment, and contingent value engineering payments. Section 4 contains contracts requiring payment adjustments. These contracts have been closed and reopened by the finance office for financial adjustments or collections. Section 5 contains contracts that have been closed during the month.

The procedures for closing out contracts are listed in the Federal Acquisition Regulation (FAR) 4.804-5, "Detailed Procedures For Closing Out Contract Files." These procedures specify that the office administering the contract is responsible for initiating closeout procedures to ensure: that the

disposition of classified material is completed; that the final patent report and the royalty reports are cleared; that there is no outstanding value engineering change proposal; that the plant clearance report and the property clearance reports are received; that the prime contractor settles all interim or disallowed costs; that prior year indirect cost rates are settled; that the termination docket, the contract audit, and the contractor's closing statement are completed; that the contractor's final invoice has been submitted; and that the deobligation of excess funds is recommended. The Defense Logistics Agency Manual (DLAM) 8105.1, "Contract Administration Manual for Contract Administration Services," dated September 22, 1988, requires the ACO's to initiate and ensure that all the closeout procedures are accomplished prior to contract closeout. Once all of these actions have been completed, the ACO can close the contract.

Objectives and Scope

The overall objective was to determine whether the contract closeout process at DLA was accomplished in an efficient and effective manner. Specific objectives were to determine the timeliness of the closeout process, the validity of unliquidated obligations, the recovery of refunds on fixed-price incentive contracts with cost underruns, and the adequacy of internal controls over the contract closeout process.

To accomplish the audit objectives, we reviewed contracts from the active, physically complete, and pay adjustment sections of the Report, as of May 31, 1989. Statistical techniques were used to select samples of contracts for review, but the sample sizes were not large enough to allow statistical projections. Therefore, all results reported are limited to the sampled data reviewed and are not intended to represent a projection to the total universe. We selected 89 active contracts, 54 physically complete contracts, 55 pay adjustment contracts, and 9 fixed-price incentive contracts. One contract was included in both the physically complete and fixed-price incentive contracts. In total, we reviewed 206 contracts with unliquidated obligations of \$465.2 million from a universe of 85,010 contracts with unliquidated obligations of \$13.8 billion. We selected nine fixed-price incentive contracts using the criteria that the contract had to have an unliquidated obligation in excess of \$500,000 or negative unliquidated progress payments.

We reviewed the 89 active contracts to determine whether active contracts were physically complete and should be included in the closeout process. We reviewed the 54 physically complete contracts and the 55 pay adjustment contracts to determine the timeliness of the closeout process. We also reviewed 28 of the physically complete contracts for validity of unliquidated obligations. The 28 physically complete contracts included one of the nine fixed-price incentive contracts. The remaining eight fixed-price incentive contracts were also assessed for

validity of unliquidated obligations. Finally, the nine fixed-priced incentive contracts were reviewed to determine whether refunds were received.

At the time of audit, DCMDM had 18,155 physically complete cost-type contracts. The backlog of Defense Contract Audit Agency (DCAA) audits prevented about 42 percent of those contracts from being closed. However, this problem was not within the authority of DLA or DCMDM to correct and will be addressed in the report on the President's Council on Integrity and Efficiency Audit of the Contract Closeout Process, Project No. OCF-0045.01.

Internal Controls

The internal controls reviewed focused on the implementation of the Federal Managers' Financial Integrity Act (FMFIA) at DCMDM, as it related to our audit scope. Contract closeout was identified for evaluation of internal controls under the Internal Management Control Program. The internal control objective for contract closeout was to "Insure proper closeout of physically complete contracts and subcontracts (after all deliverables, data items, certifications, and acceptances are received) and timely reporting of contract completion status to the cognizant procuring contracting officer." DCMDM identified specific internal control techniques for the contract closeout process and developed a checklist for use in the Internal Management Control Reviews. The internal control techniques included the ACO reviews of the Report, section 2, to ensure that all closeout actions were initiated on physically complete contracts. The techniques also included ACO reviews of status of funds to determine whether monies were available for deobligation. The implementation of FMFIA, as it related to our audit scope, was documented in management reviews of the contract closeout process and contained the essential elements required by the Act. However, execution of the Internal Management Control Reviews failed to identify the internal control weaknesses we identified in the audit.

The audit identified internal control weaknesses as defined by Public Law 97-255, Office of Management and Budget Circular A-123, and DoD Directive 5010.38. Controls were not adequate to ensure: timely closeout of contracts, validity of unliquidated obligations, and timely collection of overpayments on fixed-price incentive contracts. Guidance was lacking on how to conduct fund reviews and ACO's were not held accountable in their performance plans for the contract closeout process. Recommendation A.1.c., if implemented, will correct the internal control weaknesses identified in this report.

This program results audit was made from September 1989 through January 1990 and included reviews of ACO's contract files and accounting and finance payment records dated from June 1975 through January 1989. The audit was made in accordance with

auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD, and accordingly, included such tests of the internal controls as were considered necessary. A list of the activities visited or contacted during the audit is in Appendix E.

Prior Audit Coverage

Since 1986, the Air Force Audit Agency, DLA, and the U.S. Army Audit Agency, issued a total of four audit reports on the administration of the contract closeout process. In addition, we issued the first in a series of reports on the contract closeout process in September 1990. We identified the same problem areas in the contract closeout process as were identified in the prior audit reports. Problem areas identified in prior reports included untimely contract closeout, untimely deobligation of excess funds, and delays in recovery of overpayments. See Appendix C for additional details on each report.

PART II - FINDINGS AND RECOMMENDATIONS

A. Closing of Contracts

FINDING

Contract closeouts at DCMDM were not timely or in compliance with existing FAR and DLAM guidance. Of the 109 physically complete contracts reviewed, 40 contracts were overage for periods ranging from 1 to 162 months, with a median of 9 months, based on the closeout time frames specified in the FAR. Causes for delays in closing contracts were the incorrect assignment of contracts to section 4 of the Report, and the backlog of audits of overhead rates. In addition, the ACOs' performance plans did not hold them accountable for the contract closeout process. As a result, delays in closing contracts have created a backlog of about 11,700 overage contracts requiring closeout with an estimated \$166.2 million of unliquidated obligations. The backlog has required additional management attention from the Services' procuring agencies.

DISCUSSION OF DETAILS

Background. The FAR 4.804-1, "Closeout by the Office Administering the Contract," prescribes periods of 6 months to close firm-fixed-price contracts, 36 months to close contracts requiring the settlement of overhead rates, and 20 months for all other types of contracts. The closeout time periods are counted from the date contracts are considered physically complete to the closure date. Section 2 of the Report tracks physically complete contracts to closure and identifies contracts that are overage. No other section of the Report measures the closure time that has elapsed on contracts.

DLAM 7000.1, "Accounting and Finance Manual," states that section 4 of the Report is for contracts that have been closed and subsequently reopened for payment adjustments, collections, and review of unliquidated obligations. DLAM 8105.1, "Contract Administration Manual for Contract Administration Services," dated September 22, 1988, states that contracts in the pay adjustment section of the Report are the responsibility of the Accounting and Finance Directorate of the Region. This responsibility includes the movement of contracts into and out of section 4. The closeout time periods prescribed in the FAR for physically complete contracts are not applied to contracts awaiting pay adjustments in section 4.

Timeliness of Contract Closeout. We tested contracts shown in sections 2 and 4 of the Report, as of May 31, 1989, to determine whether DCMDM officials were closing contracts within the prescribed time frames. We reviewed the overage dates in section 2 of the Report to determine whether physically complete contracts were overage. The overage date is the date the contract becomes overage based on the prescribed closeout time

frames. We reviewed the payment records for contracts in section 4 of the Report to determine the contract status and how long the contracts were awaiting pay adjustments. The following chart shows the number of contracts in sections 2 and 4 of the Report and the number of contracts we reviewed during the audit.

<u>Report Sections</u>	<u>Number of Contracts</u>	
	<u>Total</u>	<u>Reviewed</u>
Section 2 - Physically Complete Contracts	26,697	54
Section 4 - Contracts Needing Payment Adjustments	<u>1,047</u>	<u>55</u>
Total	<u>27,744</u>	<u>109</u>

Of the 109 contracts reviewed, 40 contracts (37 percent) were physically complete, but were not closed within the prescribed time frames. The 40 contracts were from both sections of the Report (24 contracts from section 2 with \$37 million of unliquidated obligations, and 16 contracts from section 4 with \$853,000 of unliquidated obligations). None of the 40 contracts had been closed, but had been physically complete for periods ranging from 1 to 162 months, with a median of 9 months, in excess of the time frames prescribed for closeout. About 28 percent of these overage contracts had been overage for more than 2 years. A distribution of the 40 overage contracts by the number of months lapsed from the prescribed closeout period is shown below.

Distribution of Overage Contracts by Months

<u>Type of Contract</u>	<u>1-12</u>	<u>13-24</u>	<u>25-36</u>	<u>37-48</u>	<u>49-60</u>	<u>More Than 60</u>
Firm-fixed-price	14	0	2	2	0	0
Cost	<u>9</u>	<u>6</u>	<u>3</u>	<u>0</u>	<u>2</u>	<u>2</u>
Total	<u>23</u>	<u>6</u>	<u>5</u>	<u>2</u>	<u>2</u>	<u>2</u>

Section 4 Contracts. Of the 55 contracts reviewed in section 4, 16 were overage, physically complete contracts that had not been closed. Another 21 contracts were physically complete, not closed, but not yet overage. These 37 contracts should have been shown in section 2, but the contracts were erroneously assigned to section 4 (the pay adjustment section) because the contract funds were out of balance and required reconciliation. In addition, seven contracts we reviewed in section 4 belonged in section 1, and three other contracts we reviewed in section 4 belonged in section 3. Our analysis showed that the 16 overage contracts erroneously reported in section 4 were overage for periods ranging from 6 to 162 months. Since contracts were held in section 4 for payment adjustments, the responsibility for the contracts in that section was assigned to the Accounting and Finance Directorate, rather than the ACOs.

The closeout timeliness criteria in the FAR did not apply because all contracts in section 4 should have been closed prior to going into section 4 and reopened only for the payment adjustment. The ACO's were not held accountable for the timeliness of actions on contracts in section 4. Had the 16 contracts been correctly assigned to section 2, the ACO's would have been responsible for the timeliness of the contract closeout, and the contracts would have been reported as being overage when the prescribed closeout time periods expired.

Eight of the fifty-five contracts reviewed were correctly assigned to section 4 for payment adjustments. Five of the eight contracts were awaiting pay adjustments for periods ranging from 6 months to 11 months.

Section 2 Contracts. We found that 24 of the 54 physically complete contracts in section 2 were overage. ACO's did not close 14 of the 24 contracts on time because final overhead rates were pending audit by DCAA. Further, contractors had not submitted final invoices on 3 of the 24 contracts. Four of the other seven contracts had no reason code for not closing the contracts, and three contracts had miscellaneous reason codes for not closing the contracts. The ACO's do not control the DCAA audit process and, under current policy, should not close contracts awaiting audit or final invoices, even when they become overage. As of May 31, 1989, DCMDM had 18,155 physically complete cost-type contracts in section 2. The DCAA backlog of overhead audits prevented the ACO's from closing about 42 percent of those contracts. The problem of contracts becoming overage while awaiting DCAA audit will be addressed in our ongoing President's Council on Integrity and Efficiency Audit of the Contract Closeout Process (Project No. OCF-0045.01). The other seven contracts were correctly reported as overage and should be closed out by the ACO's.

Accountability for Timely Contract Closeout. We believe that the lack of specific standards in ACOs' performance plans contributed to the backlog of contracts awaiting closeout. Performance plans did not include job elements or performance standards for timely contract closeout. As a result, the ACO's were not held accountable when contracts were not closed within prescribed time frames. Since the closeout process includes reviewing funds to identify excess monies for deobligation and initiating collections on overpayments, timely contract closeout could result in monetary benefits for the DoD.

Effects of Untimely Contract Closeout. We estimated that DCMDM had a backlog of about 11,700 overage contracts with \$166.2 million of unliquidated obligations requiring closeout. As a result of the backlog of contracts, the Services' procurement offices and DLA initiated actions to expedite contract closure. These initiatives used resources that could have been used for other purposes if the contract closeout process had been effective. For example, the Air Force Logistics

Command established "Operation Clean Sweep" to deal with the problem of closing its physically complete contracts. The Army Missile Command sent procurement officials to several Defense Contract Administration Services Regions in an effort to close physically complete contracts. Also, the Navy obtained contractual resources to assist in closing some of its contracts administered by Defense Contract Administration Services Regions. The actions taken by DLA to improve the contract closeout process are discussed in the next paragraph.

Actions Taken by DLA. Management at DLA and DCMDM initiated actions to resolve closeout problems. DLA issued a series of directives to field activities on managing the contract closeout process. These directives emphasized the importance of timely closeout of physically complete contracts and of early identification of excess funds to procuring contracting officers. The directives required that ACO's comply with closeout procedures in DLAM 8105.1, Part 4.804-1; review the overage report; monitor settlement of indirect cost rates; identify excess funds; and inform the appropriate procuring contracting officer of excess funds.

DCMDM also initiated action to reduce the number of overage contracts by coordinating its efforts with DCAA to speed the negotiation of final overhead rates. In addition, task groups were formed in December 1989 to identify contractors responsible for the majority of overage contracts. According to DCMDM officials, this program reduced the number of overage contracts for contractors who were frequent offenders. As a result of our audit, a region task group was established to deal with the entire MOCAS Integrity and Contract Closeout process. The goal of this group is to review the closeout actions of the field offices to help them better focus their closeout efforts.

The efforts taken by management to improve the closeout process were commendable; however, we believe that additional actions are required to reduce the backlog of contracts awaiting closeout. DCMDM needs a working group dedicated to closing contracts in sections 2 and 4 of the report if the backlog is to be significantly reduced. The working group's responsibilities should include reviewing unliquidated obligations to identify excess monies that could be deobligated, and issuing demand letters to collect overpayments on fixed-price incentive contracts. Additional details on the need to review funds for deobligation are discussed in Finding B, "Reviewing Unliquidated Obligations," and details on the collection of overpayments are discussed in Finding C, "Recovering Overpayments on Incentive Contracts."

RECOMMENDATIONS, MANAGEMENT COMMENTS, AND AUDIT RESPONSE

DLA provided comments on the findings and recommendations. The complete text of the comments is in Appendix A. Draft report Recommendations A.1.a. and A.1.b. were deleted from this final report, and the remaining draft report Recommendations A.2.a., A.2.b. and A.2.c. were renumbered sequentially. Draft report Recommendation A.2.c. was revised.

Recommendation A.1.a. We recommend that the Commander, Defense Contract Management District Mid Atlantic, establish a working group to close all overage contracts in sections 2 and 4 of the Contract Administration Report; to review funds in order to identify excess monies and to recommend deobligation to procuring contracting officers (Finding B); and to initiate collection of overpayments (Finding C).

Management Comments. DLA partially concurred and stated that the Defense Contract Management District Mid Atlantic is establishing a Quality Management Board to close out all overage contracts in section 4 of the Contract Administration Report. The overage contracts in section 2 remain the responsibility of the individual administrative contracting officers for normal closeout actions. DLA agreed that an internal control weakness existed.

Audit Response. DLA's comments were partially responsive. Establishment of the Quality Management Board and its charter to close out all overage contracts in section 4 of the Contract Administration Report is partially responsive to the recommendation. We believe that the Quality Management Board should assist administrative contracting officers in closing the overage contracts in section 2. It was evident in our audit that normal administrative contracting officer closeout actions were not accomplished in a timely manner. DLA has not provided evidence that the problem will improve without assistance. We request that the Director, DLA, reconsider the position and provide additional comments to the final report addressing the closeout of contracts in section 2 of the Contract Administration Report.

Recommendation A.1.b. We recommend that the Commander, Defense Contract Management District Mid Atlantic, establish milestones for the working group and require periodic reports on the progress of reducing the backlog of contracts requiring closeout.

Management Comments. DLA concurred. The Quality Management Board will establish milestones and provide periodic reports on their progress toward reducing the backlog of contracts requiring closeout. A completion date of March 1, 1991, has been set for these actions.

Recommendation A.1.c. We recommend that the Commander, Defense Contract Management District Mid Atlantic, establish and include

performance standards in the administrative contracting officers' and their supervisor's performance plans for the contract closeout process to include timely closing of contracts, timely review of funds for excess monies that could be deobligated (Finding B), and timely initiation of collection of overpayments (Finding C).

Management Comments. DLA nonconcurred with the draft report recommendation for a critical job element in the administrative contracting officers' and their supervisor's performance plans.

Audit Response. We discussed the recommendation with management officials and have changed the recommendation in this final report to focus on establishing performance standards for timely closing of contracts. We request that the Director, DLA, provide comments to the final report on the revised recommendation.

Management Comments on the Finding. DLA concurred with Finding A, qualifying the response by stating that delays in contract closeout are often beyond the control of the administrative contracting officers. DLA also concurred that delays in closing contracts were an internal control weakness.

B. Reviewing Unliquidated Obligations

FINDING

The ACO's did not make required fund reviews on 86 percent of the physically complete contracts we reviewed to determine whether the contracts had unliquidated obligations that could be released and reused for other purposes. The fund reviews were not made because the DLA Manual contained no guidance on how to conduct the reviews and ACO's were not trained in the fund review process. As a result, \$3.5 million was not identified to the procuring office for deobligation. A total of \$3.3 million of the \$3.5 million was stock fund money and could be reused. In addition, obligations were overstated by \$36.9 million, and disbursements were understated by \$7.3 million.

DISCUSSION OF DETAILS

Background. The DLAM 8105.1, Change 6, Part 4.804-3, states, "When a contract is physically complete, the ACO will review the status of funds to ascertain whether funds are available for removal prior to final payments." Fund reviews are performed to determine the amount of excess funds on contracts and to recommend deobligation to the procuring contracting officer.

Contract Administrators' Reviews of Unliquidated Obligations. We reviewed 36 physically complete contracts from section 2 of the Report, as of May 31, 1989, to determine whether ACO's identified excess funds and recommended deobligation of those funds from contracts during the contract closeout process. Specifically, we reviewed the ACOs' files for required documentation of their fund reviews on each contract. We found no documentary evidence in the contract files that ACO's made fund reviews on 31 (86 percent) of the 36 contracts. The 31 contracts had \$53.9 million of unliquidated obligations.

We attributed the absence of fund reviews to the lack of guidance in DLAM 8105.1. The manual did not explain how the ACO's should determine whether contracts had excess funds or erroneous obligations. Procedures were not available on how to perform fund reviews for each type of contract, and high-dollar unliquidated obligations on completed contracts did not require reporting to higher management levels.

Effects of Unliquidated Obligations. We found that \$3.5 million of the \$53.9 million of unliquidated obligations on the 31 contracts without ACO fund reviews could have been deobligated. We requested ACO's to review the funds on contracts that had not been previously reviewed. The ACO's identified about \$1.3 million in excess funds that could be deobligated on four different contracts. In addition to the contracts reviewed by the ACO's at our request, we reviewed contract F09603-84-G-1461/GB38 for excess funds. We estimated that about \$2.2 million

could be deobligated on that contract. Contracts and estimated deobligation amounts of excess funds are shown in the following chart.

<u>Contract Number</u>	<u>Estimated Excess Funds</u>
N00189-82-C-0960	\$ 111,600
N00189-82-C-0270	1,104,242
N61339-79-C-0116	60,767
MDA908-85-C-1694	70,000
F09603-84-G-1461/GB38	<u>2,176,400</u>
Total	<u>\$3,523,009</u>

A total of \$3.3 million of the \$3.5 million was stock fund money and could be reused. Additionally, we found errors in the MOCAS system that overstated obligations by \$36.9 million and understated disbursements by \$7.3 million. For example, contract N00019-78-C-0221 showed a \$9.7 million unliquidated obligation in MOCAS as of May 31, 1989. As a result of our audit in September 1989, the ACO reviewed the contract and determined that the obligation was entered in the system twice and that the actual unliquidated obligation balance was zero. Delays in identifying and correcting errors in obligations and disbursements contributed to the untimely closeout of contracts.

RECOMMENDATIONS, MANAGEMENT COMMENTS, AND AUDIT RESPONSE

Recommendation B.1. We recommend that the Director, Defense Logistics Agency, revise Defense Logistics Agency Manual 8105.1, "Contract Administration Manual for Contract Administration Services," dated September 22, 1988, to include procedures specifying how to review unliquidated obligations on each type of contract, including a requirement for documented explanations for high-dollar amounts of unliquidated obligations that cannot be deobligated.

Management Comments. DLA nonconcurred with the recommendation and stated that the Manual requires the ACO to review the status of funds. Since review methods vary with contract type and supplies or services being provided, it is impractical to incorporate step-by-step instructions in the regulations. DLA also did not agree that documented explanations of unliquidated obligations should be required. Such obligations may represent monies that are due the contractor or that are unavailable for deobligation prior to final audit. DLA stated that this area did not represent an internal control weakness.

Audit Response. We clarified the intent of this recommendation in discussions with officials of DLA. We were not suggesting that a step-by-step set of procedures be incorporated into the regulations. That kind of guidance should be reserved

for training curriculum; however, our intention was that more information be provided to the administrative contracting officers on what a fund review was in respect to their job. The administrative contracting officers in the field told us they had too little knowledge to effectively conduct a fund review. We request that the Director, DLA, reconsider the position and provide additional comments to this recommendation in the final report.

Recommendation B.2.a. We recommend that the Commander, Defense Contract Management District Mid Atlantic, update the training curriculum to include the procedures in Recommendation B.1.

Management Comments. DLA partially concurred. Training to acquaint personnel with methodology and computer reports available for contract reconciliation would be beneficial. Officials at Headquarters, DLA, will work with Defense Contract Management District personnel to develop a training curriculum. DLA officials did not agree that procedures should be added to the manual (see Recommendation B.1.).

Audit Response. The comments from DLA were responsive, considering the clarification of our intent in Recommendation B.1.

Recommendation B.2.b. We recommend that the Commander, Defense Contract Management District Mid Atlantic, request the procuring offices to deobligate \$3.5 million on the following contracts.

<u>Contract Number</u>	<u>Estimated Excess Funds</u>
N00189-82-C-0960	\$111,600
N00189-82-C-0270	1,104,242
N61339-79-C-0116	60,767
MDA908-85-C-1694	70,000
F09603-84-G-1461/GB38	<u>2,176,400</u>
Total	<u>\$3,523,009</u>

Management Comments. DLA concurred. Funds were deobligated on two of the contracts, and funds will be deobligated on the remaining three contracts when the Defense Contract Audit Agency audits are complete and final payments are made to the contractors. The estimated completion date is December 31, 1991.

Management Comments on the Finding. DLA partially concurred with the finding and stated that DCMDM reminded ACO's of their responsibility to review the unliquidated obligations of contracts that are physically complete in a February 12, 1990

memorandum. DLA did not agree that the reviews were not performed because its manual did not contain guidance on "how to" conduct reviews. Incorrectly stated obligations and disbursements were corrected. DLA agreed that an internal control weakness existed.

Audit Response. Since discussions with DLA officials clarified our intent on Recommendation B.1., we request that the Director, DLA, reconsider the position and provide additional comments to this finding in the final report.

C. Recovering Overpayments on Incentive Contracts

FINDING

ACO's were late in recovering \$363,000 in overpayments made to contractors on three fixed-price incentive contracts. The overpayments existed for periods ranging from 23 months to 39 months, with a median of 26 months, as of January 31, 1990. This condition occurred because ACO's did not obtain and review contractors' quarterly limitation on payment statements. Delays in recovering the overpayments cost the Government an estimated \$60,600 in interest and exposed the Government to the unnecessary risks associated with outstanding debts.

DISCUSSION OF DETAILS

Background. The FAR and DLM 8105.1 do not list the recovery of overpayments to contractors as a required step in the contract closeout process. However, procedures for identifying and recovering overpayments are included in each regulation. FAR 16.405, "Incentive Contracts, Contract Clauses," requires contracting officers to insert FAR clause 52.216-16, "Incentive Price Revision-Firm Target," in fixed-price incentive contracts. The clause stipulates that the contractor will furnish the Government with "Quarterly Limitation on Payment Statements." The quarterly statements should include the cost of all items the Government receives and the payments the contractor receives for the delivered items. If the amount of payments exceeds the cost of the delivered items, the contractor is required to immediately refund the overpayment to the Government. If the contractor does not refund overpayments within 30 days of the due date of the quarterly statements, the Government should assess interest in accordance with FAR clause 52.232-17, "Interest." FAR 42.302, "Contract Administration Functions," and DLM 8105.1, Part 16.4-4c., require ACO's to analyze the quarterly limitation on payment statements and recover overpayments not refunded by the contractors.

Recovery of Overpayments. We performed a four-part review to determine whether ACO's at DCMDM collected overpayments on fixed-price incentive contracts. Sixteen fixed-price incentive contracts, valued at \$330.5 million, were shown as physically complete on the Report for May 31, 1989. From those 16 contracts, we selected all the contracts with unliquidated obligations in excess of \$500,000 and all the contracts with negative unliquidated progress payments. Nine contracts, valued at \$304.4 million, met those criteria. To determine whether the contractors had been overpaid, we reviewed the latest cost information the contractor provided, including quarterly limitation on payment statements and final price proposals. In addition, we reviewed the ACO's records to determine whether overpayments had been recovered. ACO's had not recovered \$373,073.34 in overpayments on three of the nine contracts we reviewed in October 1989. We were later informed that an

overpayment of \$10,446.07 was negotiated in favor of the contractor in the final price on one contract. As a result of our audit, overpayments of \$323,192.99 and \$38,502.28 were recovered in January and February 1990, respectively. An overpayment of \$932 remained outstanding as of January 31, 1990.

Reasons For Delays in Recovering Overpayments. The overpayments were not collected timely because ACO's did not obtain and review the contractors' quarterly limitation on payment statements. Our review of the final cost statements indicated refunds were due the Government on three contracts. The ACO's should have initiated demand letters to the contractors. We identified overpayments totaling \$373,073.34 on the following contracts, which had not been recovered at the time of our audit.

<u>Contract Number</u>	<u>Amount of Overpayment</u>
F30602-86-C-0016	\$ 10,446.07
F30602-86-C-0016	932.00
N00024-80-C-6107	38,502.28
N61339-81-C-0082	<u>323,192.99</u>
Total	<u>\$373,073.34</u>

Action Taken by Management to Collect Overpayments. On January 11, 1990, the ACO for contract N61339-81-C-0082 issued a demand letter for a \$323,192.99 overpayment and received a refund for this amount on January 18, 1990. The ACO for contract N00024-80-C-6107 also issued a demand letter and received a refund of \$38,502.28 in February 1990. The final price for contract F30602-86-C-0016 was negotiated and the overpayment was \$932.00. In our review of the final price, we found that the procuring contracting officer negotiated a final price equal to the payments received by the contractor. The final profit negotiated exceeded the terms of the contract and negated the \$10,446.07 overpayment we identified based on the contractor's final cost statement. The \$932.00 overpayment was related to a progress payment and was in addition to the \$10,446.07. The \$932.00 was still outstanding at the conclusion of our audit. We believe that the \$10,446.07 would not have been included in the final price if the ACO had initiated collection action when the final price proposal was received in 1987.

Effect of Not Recovering Overpayments. When overpayments were not collected from contractors, the Government lost not only the use of the overpaid monies but also the cost of that money (interest) to the U.S. Treasury. We obtained the interest costs from the U.S. Treasury for the years during which the overpayments were outstanding and estimated the interest cost to the U.S. Treasury at \$60,600.00.

CALCULATION OF INTEREST EXPENSE FOR OVERPAYMENTS

<u>Contract Number *</u>	<u>\$ Amount of Overpayment</u>	<u>Interest Rate</u>	<u>Months</u>	<u>Interest Expense</u>
N0024-80-C-6107	38,502.28	7.11%	3	\$ 684.38
N0024-80-C-6107	38,502.28	7.68%	12	2,956.98
N0024-80-C-6107	38,502.28	8.30%	12	3,195.69
N0024-80-C-6107	38,502.28	8.07%	12	<u>3,107.13</u>
TOTAL				<u>\$ 9,944.18</u>
N61339-81-C-0082	323,192.99	8.30%	11	24,589.60
N61339-81-C-0082	323,192.99	8.07%	12	<u>26,081.67</u>
TOTAL				<u>\$50,671.27</u>
GRAND TOTAL				<u>\$60,615.45</u>

* Interest for overpayments on contract F30602-86-C-0016 was not included in the estimate.

In addition, the inherent risk associated with debt collection placed the Government unnecessarily at risk when overpayments existed because of the uncertainty of recovery. DoD could avoid these effects if ACO's promptly identify and collect overpayments.

RECOMMENDATIONS, MANAGEMENT COMMENTS, AND AUDIT RESPONSE

Recommendation C. We recommend that the Commander, Contract Management District Mid Atlantic, issue a demand letter for the overpayment of \$932.00 identified on contract F30602-86-C-0016, and assess interest in accordance with the Federal Acquisition Regulation 52.216-16, "Incentive Price Revision - Firm Target," and Federal Acquisition Regulation 52.232-17, "Interest," clauses in the contract.

Management Comments. DLA concurred. The funds have been collected. DLA agreed that an internal control weakness existed.

Management Comments on the Finding. DLA concurred with the finding. The three overpayments were not collected in a timely manner. The funds were collected as a result of our audit.

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DEFENSE LOGISTICS AGENCY
HEADQUARTERS
CAMERON STATION
ALEXANDRIA, VIRGINIA 22304-6100



IN REPLY
REFER TO DLA-CI

21 SEP 1990

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING,
ATTN: DIRECTOR, CONTRACT MANAGEMENT
DIRECTORATE

SUBJECT: DoD IG Draft Report on the Audit of the Administration
of the Contract Closeout Process at the Defense
Contract Management Region, Philadelphia (Project No.
9AC-0021)

This is a partial response to your memorandum of 19 July 1990,
requesting comments on the draft report. The enclosed seven
positions have been approved by Ms. Helen McCoy, Deputy
Comptroller, Defense Logistics Agency. Additional time is
required to formulate qualitative responses on the remaining
five positions. These positions will be provided to your office
no later than 1 October 1990.

7 Encl

Reatha E. Holmes

REATHEA E. HOLMES
Chief, Internal Review Division
Office of Comptroller

TYPE OF REPORT: AUDIT

DATE OF POSITION: 19 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the Administration
of the Contract Closeout Process at the Defense
Contract Management Region, Philadelphia
(Project No. 9AC-0021)

Final Report

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FINDING A: Closing of Contracts. Contract closeouts at Defense Contract Management Region, Philadelphia, were not timely or in compliance with existing Federal Acquisition Regulation (FAR) and Defense Logistics Agency Manual guidance. Of the 109 physically complete contracts reviewed, 40 contracts were overage for periods ranging from 1 to 162 months, based on the closeout time frames specified in FAR. Causes for delays in closing contracts were the lack of closeout time frames for contracts not in the physically complete section of the Contract Administration Report (the Report), and the backlog of audits of overhead rates. In addition, the administrative contracting officers (ACO's) performance plans did not hold them accountable for the contract closeout process. As a result, delays in closing contracts have created a backlog of about 11,700 overage contracts requiring closeout with an estimated \$161 million of unliquidated obligations. The backlog has required additional management attention from the Services' procuring agencies.

DLA COMMENTS:

Concur with the finding that contract closeout is not always in compliance with the Federal Acquisition Regulation (FAR) recommended time frames. Causes for delay are often beyond the control of the Administrative Contracting Officer (ACO). In July 1987 the Air Force attempted to increase the contract closeout time frame for cost-type contracts from 36 to 60 months in recognition of the actual time required to perform the required indirect rate settlement activities. The Defense Acquisition Regulatory (DAR) Council rejected the proposal because of high-level DoD and Service interest in expediting contract closeout. The DAR Council also attempted to implement regulatory changes to increase fee withholdings to encourage earlier submission of contractor overhead proposals. The DAR Council had to withdraw the proposed changes because of strong opposition from industry and the Office of Federal Procurement Policy. DLA is working closely with DCAA to focus their efforts on the contractors with the highest number of contracts where closeout is delayed pending DCAA audit of overhead or other indirect rates. The unliquidated obligations may not be available for deobligation but rather may represent monies due the contractor or in the case of cost-type contracts, money unavailable for deobligation prior to final audit.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- () Nonconcur.
- (X) Concur; however, weakness is not considered material.
We do not agree there is a material internal control
weakness reportable to the Secretary of Defense on our part.
The present internal controls are inherently strong.
- () Concur; weakness is material and will be reported in the DLA
Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy

TYPE OF REPORT: AUDIT

DATE OF POSITION: 19 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the
Administration of the Contract Closeout
Process at the Defense Contract Management
Region, Philadelphia (Project No.
9AC-0021)

Final Report

RECOMMENDATION A.1.b: We recommend that the Director, Defense
Logistics Agency, establish a separate section in the Contract
Administration Report to record contracts that require audits of
indirect costs before the contracts can be closed.

A.1.b.
dropped
from
Final Report

DLA COMMENTS:

Nonconcur. Each contract in Section 2 has an overage reason
code, entered by the ACO which indicates why the contract cannot
be closed (e.g., H=Final Audits in Process; M=Negotiation of
Overhead Rates Pending). Therefore, there is no clear benefit
for setting up a new section. The programming effort required
to accomplish this task outweighs any perceived benefit. On a
monthly basis, contract administration personnel monitor
contracts that are in Section 2 of the Contract Administration
Report. These reviews alert the ACO to pending actions on
contracts awaiting closeout.

DISPOSITION:

- () Action is ongoing; Final Estimated Completion Date:
- (X) Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- (X) Nonconcur. We do not agree there is a material internal
control weakness reportable to the Secretary of Defense on
our part. The present internal controls are inherently
strong.
- () Concur; however, weakness is not considered material.
(Rationale must be documented and maintained with your copy
of the response.)
- () Concur; weakness is material and will be reported in the DLA
Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy

TYPE OF REPORT: AUDIT

DATE OF POSITION: 19 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the
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Renumbered

A.1.b.

RECOMMENDATION A.2.b: We recommend that the Commander, Defense
Contract Management Region, Philadelphia, establish milestones
for the working group and require periodic reports on the
progress of reducing the backlog of contracts requiring
closeout.

DLA COMMENTS:

Concur. The Quality Management Board will establish milestones
and provide periodic reports on their progress toward reducing
the backlog of contracts requiring closeout.

DISPOSITION:

(X) Action is ongoing; Final Estimated Completion Date: 1 Mar 91
() Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

() Nonconcur.

(X) Concur; however, weakness is not considered material. We do
not agree there is a material internal control weakness
reportable to the Secretary of Defense on our part. The
present internal controls are inherently strong.

() Concur; weakness is material and will be reported in the DLA
Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy

TYPE OF REPORT: AUDIT

DATE OF POSITION: 19 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the
Administration of the Contract Closeout
Process at the Defense Contract Management
Region, Philadelphia
(Project No. 9AC-0021)

RECOMMENDATION B.2.a: We recommend that the Commander, Defense
Contract Management Region, Philadelphia, update the training
curriculum to include the procedures in Recommendation B.1.

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DLA COMMENTS:

Partially concur. Training to acquaint personnel with
methodology and computer reports available for contract
reconciliation would be beneficial. HQ DLA personnel will work
with Defense Contract Management District personnel to develop a
training curriculum. We do not agree that reconciliation
procedures should be added to the manual.

DISPOSITION:

(X) Action is ongoing; Final Estimated Completion Date: 1 Sep 91
() Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

() Nonconcur.
(X) Concur; however, weakness is not considered material. We do
not agree there is a material internal control weakness
reportable to the Secretary of Defense on our part. The
present internal controls are inherently strong.
() Concur; weakness is material and will be reported in the DLA
Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy

TYPE OF REPORT: AUDIT

DATE OF POSITION: 19 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the
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RECOMMENDATION B.2.b: We recommend that the Commander, Defense
Contract Management Region, Philadelphia, initiate requests to
procuring offices to deobligate \$3.5 million on the following
contracts:

<u>Contract Number</u>	<u>Estimated Excess Funds</u>
N00189-82-C-0960	\$ 111,600
N00189-82-C-0270	1,104,242
N61339-79-C-0116	60,767
MDA908-85-C-1694	70,000
F09603-84-G-1461/GB38	2,176,400
	<u>\$ 3,523,009</u>

DLA COMMENTS:

Concur. Contracts N61339-79-C-0116 and F09603-84-G-1461-GB38
are closed. Funds were deobligated. The remaining three
contracts are cost type contracts awaiting DCAA audit. When the
audit is complete, final payment to the contractor or
deobligation will occur.

DISPOSITION:

(X) Action is ongoing; Final Estimated Completion Date: 31 Dec 91
() Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

() Nonconcur.

(X) Concur; however, weakness is not considered material. We do
not agree there is a material internal control weakness
reportable to the Secretary of Defense on our part. The
present internal controls are inherently strong.

() Concur; weakness is material and will be reported in the DLA
Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47544

DLA APPROVAL: Helen T. McCoy

TYPE OF REPORT: AUDIT

DATE OF POSITION: 19 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the
Administration of the Contract Closeout
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FINDING C: Recovering Overpayments on Incentive Contracts. The administrative contracting officers (ACO's) did not recover \$932 in overpayments made to contractors on one physically complete fixed-price incentive contract and were late in recovering \$362,000 on two contracts. The overpayments existed for periods ranging from 23 months to 39 months as of January 31, 1990. This condition occurred because ACO's did not obtain and review contractors' quarterly limitation on payment statements. Delays in recovering the overpayments cost the Government an estimated \$60,600 in interest and exposed the Government to the unnecessary risks associated with outstanding debts.

DLA COMMENTS:

Concur. The three overpayments were not collected in a timely manner. In accordance with Recommendation C, the funds have now been collected.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- () Nonconcur.
- (X) Concur; however, weakness is not considered material. We do not agree there is a material internal control weakness reportable to the Secretary of Defense on our part. The present internal controls are inherently strong.
- () Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy

TYPE OF REPORT: AUDIT

DATE OF POSITION: 19 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the
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RECOMMENDATION C: We recommend that the Commander, Defense
Contract Management Region, Philadelphia, issue a demand letter
for the overpayment of \$932.00 identified on contract
F30602-86-C-0016, and assess interest in accordance with the
Federal Acquisition Regulation 52.216-16, "Incentive Price
Revision - Firm Target," and Federal Acquisition Regulation
52.232-17, "Interest," clauses in the contract.

DLA COMMENTS:

Concur. The Defense Contract Management District Mid-Atlantic
collected the outstanding debt on contract F30602-86-C-0016 by
check on 21 June 1990.

DISPOSITION:

- () Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- () Nonconcur.
(X) Concur; however, weakness is not considered material. We do
not agree there is a material internal control weakness
reportable to the Secretary of Defense on our part. The
present internal controls are inherently strong.
() Concur; weakness is material and will be reported in the DLA
Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy



DEFENSE LOGISTICS AGENCY
HEADQUARTERS
CAMERON STATION
ALEXANDRIA, VIRGINIA 22304-6100



IN REPLY
REFER TO DLA-CI

01 OCT 1990

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING.
ATTN: DIRECTOR, CONTRACT MANAGEMENT
DIRECTORATE

SUBJECT: DoD IG Draft Report on the Audit of the Administration
of the Contract Closeout Process at the Defense
Contract Management Region, Philadelphia (Project No.
9AC-0021)

This is the second increment of approved comments on the draft
report. The enclosed positions have been approved by Ms. Helen
McCoy, Deputy Comptroller, Defense Logistics Agency. The
comments on Recommendation A.2.c. will be sent to you by
9 October 1990.

4 Encl

Reatha E. Holmes

REATHEA E. HOLMES
Chief, Internal Review Division
Office of Comptroller

TYPE OF REPORT: AUDIT

DATE OF POSITION: 26 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the Administration
of the Contract Closeout Process at the Defense
Contract Management Region, Philadelphia
(Project No. 9AC-0021)

Final Report

RECOMMENDATION A.1.a: We recommend that the Director, Defense
Logistics Agency, revise Defense Logistics Agency Manual 8105.1, A.1.a.
'Contract Administration Manual for Contract Administration Services,' dropped
dated September 22, 1988, to specify time frames for contracts in from
section 4 of the Contract Administration Report and to require overage Final
reporting for any contract that remains in section 4 in excess of these Rpt.
time frames.

DLA COMMENTS: Nonconcur. Contracts should be in this section
only for two reasons: (1) contracts that have been coded for
closing but for which the system detects funds remaining are
mechanically placed in the section and (2) contracts that are
reopened by accounting and finance personnel to process an
additional payment or collection. All contracts in this section
were closed by the Administrative Contracting Officer and have
no pending administrative actions. We do not agree that
specified time frames need to be established for contracts in
section 4 of the Contract Administration Report. The complexity
of contracts controls the time frames required to move the
contracts from section 4 into a closed position.

DISPOSITION:

- () Action is ongoing; Final Estimated Completion Date:
- (X) Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- (X) Nonconcur. We do not agree there is a material internal
control weakness reportable to the Secretary of Defense on
our part. The present internal controls are inherently
strong.
- () Concur; however, weakness is not considered material.
(Rationale must be documented and maintained with your copy
of the response.)
- () Concur; weakness is material and will be reported in the DLA
Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy

TYPE OF REPORT: AUDIT

DATE OF POSITION: 26 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the
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Renumbered
A.1.a.

RECOMMENDATION A.2.a: We recommend that the Commander, Defense Contract Management Region, Philadelphia, establish a Working Group to close out all overage contracts in sections 2 and 4 of the Contract Administration Report, to review funds in order to identify excess monies and to recommend deobligation to procuring contracting officers (Finding B), and to initiate collection of overpayments (Finding C).

DLA COMMENTS:

Partially concur. The Defense Contract Management District Mid-Atlantic (formerly Defense Contract Management Region, Philadelphia) is establishing a Quality Management Board. The purpose of the Board is to close out all overage contracts in section 4 of the Contract Administration Report. The remaining contracts in section 2 of the Contract Administration Report are the responsibility of the individual Administrative Contracting Officers since the contracts in section 2 are awaiting normal ACO closeout actions.

DISPOSITION:

(X) Action is ongoing; Final Estimated Completion Date: 1 Mar 91
() Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

() Nonconcur.
(X) Concur; however, weakness is not considered material. We do not agree there is a material internal control weakness reportable to the Secretary of Defense on our part. The present internal controls are inherently strong.
() Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy

TYPE OF REPORT: AUDIT

DATE OF POSITION: 26 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the
Administration of the Contract Closeout
Process at the Defense Contract Management
Region, Philadelphia
(Project No. 9AC-0021)

Final Report
Page No. 11

FINDING B: Reviewing Unliquidated Obligations. The administrative contracting officers (ACO's) did not make required fund reviews on 83 percent of the physically complete contracts we reviewed to determine whether the contracts had unliquidated obligations that could be released and reused for other purposes. The fund reviews were not made because the Defense Logistics Agency Manual contained no guidance on how to conduct the reviews. As a result, \$3.5 million was not deobligated. A total of \$3.3 million of the \$3.5 million was stock fund money and could be reused. In addition, obligations were incorrectly overstated by \$36.9 million, and disbursements were incorrectly understated by \$7.3 million.

DLA COMMENTS:

Partially concur. Defense Contract Management District Mid-Atlantic reminded the Administrative Contracting Officers (ACOs) of their responsibility to review the unliquidated obligations of contracts that are physically complete by a 12 February 1990 memorandum. The Defense Logistics Agency Manual 8105.1 requires ACOs to review the status of funds on physically complete contracts to determine whether funds are available for removal before final payment and contract closeout. We do not agree that the reason the reviews were not performed is because the Defense Logistics Agency Manual contains no guidance on 'how to' conduct reviews. Incorrectly stated obligations and disbursements were corrected.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- () Nonconcur.
- (X) Concur; however, weakness is not considered material. We do not agree there is a material internal control weakness reportable to the Secretary of Defense on our part. The present internal controls are inherently strong.
- () Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy

TYPE OF REPORT: AUDIT

DATE OF POSITION: 26 Sep 90

PURPOSE OF INPUT: INITIAL POSITION

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(Project No. 9AC-0021)

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Page No. 12

RECOMMENDATION B.1: We recommend that the Director, Defense Logistics Agency, revise Defense Logistics Agency Manual 8105.1, 'Contract Administration Manual for Contract Administration Services,' dated September 22, 1988, to include procedures specifying how to review unliquidated obligations on each type of contract, including a requirement for documented explanations for high-dollar amounts of unliquidated obligations that cannot be deobligated.

DLA COMMENTS:

Nonconcur. The Defense Logistics Agency Manual requires the ACO to review the status of funds. Since review methods vary with contract type and supplies or services being provided, it is impractical to incorporate step-by-step instructions for accomplishing contract reconciliation. The unliquidated obligations do not necessarily represent funds available to the Government for additional procurement but may be due the contractor as payment on the final public voucher or invoice. In difficult reconciliation situations, the ACO can request assistance from the comptroller, who has access to the individual payment records. We do not agree that documented explanations of unliquidated obligations not available for deobligation should be provided when they may represent monies due the contractor or in the case of cost type contracts, unavailable for deobligation prior to final audit.

DISPOSITION:

() Action is ongoing; Final Estimated Completion Date:
(X) Action is considered complete.

MONETARY BENEFITS: None

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

(X) Nonconcur. We do not agree there is a material internal control weakness reportable to the Secretary of Defense on our part. The present internal controls are inherently strong.
() Concur; however, weakness is not considered material.
() Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy



DEFENSE LOGISTICS AGENCY
HEADQUARTERS
CAMERON STATION
ALEXANDRIA, VIRGINIA 22304-6100



IN REPLY
REFER TO

DLA-CI

5 OCT 1990

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING.
ATTN: DIRECTOR, CONTRACT MANAGEMENT
DIRECTORATE

SUBJECT: DoD IG Draft Report on the Audit of the Administration
of the Contract Closeout Process at the Defense
Contract Management Region, Philadelphia (Project No.
9AC-0021)

Enclosed are comments for Recommendation A.2.c. on the draft
report on the Contract Closeout Process at Philadelphia. The
position has been approved by Ms. Helen McCoy, Deputy
Comptroller, Defense Logistics Agency.

1 Encl

Reatha E. Holmes

REATHEA E. HOLMES
Chief, Internal Review Division
Office of Comptroller

TYPE OF REPORT: AUDIT

DATE OF POSITION: 4 Oct 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Report on the Audit of the
Administration of the Contract Closeout
Process at the Defense Contract Management
Region, Philadelphia (Project 9AC-0021)

Final Report
Page No. 10
Renumbered
A.1.c.

RECOMMENDATION A.2.c: We recommend that the Commander, Defense Contract Management Region, Philadelphia, establish and include a critical job element in the administrative contracting officers' and their supervisors performance plans specifying performance standards for the contract closeout process to include timely closing of contracts, timely review of funds for excess monies that could be deobligated (Finding B), and timely initiation of collection of overpayments (Finding C).

DLA COMMENTS: Nonconcur. The Administrative Contracting Officers' (ACOs) tasks are multifaceted and include complex analytical functions. We strongly disagree with the suggestion to isolate one aspect such as contract closeout as a critical job element in their performance plans. FAR 42.302 and DFARS 242.302 delineate 82 separate contract administration functions. All these elements are potentially 'critical.' Often contract closeouts are delayed as a consequence of action not being taken by persons or functional elements other than the ACO (e.g. audit of contractor indirect rates or final public vouchers by the DCAA, submission of those same rates or final vouchers by the contractor, etc.). Because so many of the actions delaying contract closeout are beyond the ACOs control we do not feel that the ACO should be evaluated on the basis of something over which they have no control. Contract closeout and overage is one of the management indicators that DLA has historically evaluated and monitored on a monthly basis. Individual ACOs are held accountable for the overall management of the contract administration workload assigned to their group.

DISPOSITION:

- () Action is ongoing; Final Estimated Completion Date:
- (X) Action is considered complete.

MONETARY BENEFITS: N/A

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

INTERNAL MANAGEMENT CONTROL WEAKNESS:

- (X) Nonconcur. We do not agree there is a material internal control weakness reportable to the Secretary of Defense on our part. The present internal controls are inherently strong.
- () Concur; however, weakness is not considered material.
- () Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

ACTION OFFICER: Mrs. Nanette Audet, DLA-AC, 47644

DLA APPROVAL: Helen T. McCoy

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**SUMMARY OF POTENTIAL MONETARY AND OTHER
BENEFITS RESULTING FROM AUDIT**

<u>Recommendation Reference</u>	<u>Description of Benefit</u>	<u>Amount and Type of Benefit</u>
A.1.a. and b.	Economy and Efficiency. Will result in more efficient use of DoD contract administration resources, and will facilitate the reorganization and consolidation of the contract administration finance function.	Nonmonetary.
A.1.c.	Internal Control. Provides accountability for compliance with existing internal controls.	Nonmonetary.
B.1.	Economy and Efficiency. Will result in more efficient use of DoD contract administration resources and facilitate the review and release of excess funds.	Nonmonetary.
B.2.a.	Program Results. Will facilitate implementation of procedures established as a result of Recommendation B.1.	Nonmonetary.
B.2.b.	Economy and Efficiency. Stock fund monies can be reused for other procurements when deobligated.	Monetary. Funds can be put to better use by deobligating stock fund monies not required on contracts. The amount of benefit could not be determined based on audit results.

**SUMMARY OF POTENTIAL MONETARY AND OTHER
BENEFITS RESULTING FROM AUDIT (Continued)**

<u>Recommendation Reference</u>	<u>Description of Benefit</u>	<u>Amount and Type of Benefit</u>
C.	Economy and Efficiency. Interest cost as a result of delays in collecting overpayments.	Cost avoidance of interest resulting from future prompt collection of overpayments cannot be computed based on audit results.

SYNOPSIS OF PRIOR AUDIT REPORTS ON ADMINISTRATION
OF THE CONTRACT CLOSEOUT PROCESS

Inspector General, Department of Defense, Report No.90-108,
"Final Report on the Audit of the Administration of the Contract
Closeout Process at the Defense Contract Management Region,
Dallas," September 18, 1990.

The report stated that the overall administration of the contract closeout process at the Defense Contract Management Region, Dallas, was generally effective. Contracts were generally closed within time frames prescribed in the Federal Acquisition Regulation, and excess funds were identified for deobligation. No problems were reported on the collection of overpayments on fixed-price incentive contracts. This was a memorandum report with no recommendations.

Inspector General, Department of Defense, 9AC-0021.02, "Draft
Report on the Audit of the Administration of the Contract
Closeout Process at the Defense Contract Management Region,
Los Angeles," September 10, 1990.

The report stated that contract closeout was not timely, and that administrative contracting officers did not make required fund reviews or recover overpayments on fixed-price incentive contracts. The audit also identified internal control weaknesses in these same areas. Recommendations were made to the Defense Logistics Agency to revise the Defense Logistics Agency Manual 8105.1, "Contract Administration Manual for Contract Administration Services," to specify time frames for contracts terminated for convenience in section 3 of the Contract Administration Report and to require overage reporting of contracts terminated for convenience that remain in section 3 in excess of those time frames. The report recommended that the Defense Contract Management Region, Los Angeles, establish a working group to closeout all overage contracts, provide training to administrative contracting officers on the new fund review procedures, and include the contract closeout process in administrative contracting officers' performance plans.

U.S. Army Material Command Subject Matter Assessment

The assessment on the contract closeout process stated that funds were not deobligated promptly and overpayments existed on contracts.

Air Force Audit Agency, Project No. 7066411, "Audit of Closeout
of Physically Completed Contracts With Unliquidated Obligations,"
July 14, 1988.

The report stated that management controls over the closeout process for physically complete contracts with unliquidated obligations were not effective, that the Air Force did not complete contract fund reviews for about three-fourths of the

SYNOPSIS OF PRIOR AUDIT REPORTS ON ADMINISTRATION
OF THE CONTRACT CLOSEOUT PROCESS (Continued)

contracts reviewed, that no coordination was initiated with paying offices to reconcile potential differences in fund balances, and that procuring contracting officers were not completing timely final closeout actions on physically complete contracts. The report recommended that the Director of Contract and Manufacturing Policy, Headquarters, U.S. Air Force, issue a supplement to Federal Acquisition Regulation (FAR) 4.804-5 directing procuring contracting officers to initiate contract funds reviews within 30 days after physical completion of each contract; coordinate contract fund reviews with accounting and finance offices; and instruct the buying activities to emphasize the importance of closing out physically complete contracts within FAR time frames. One method was recommended to increase emphasis to include in performance appraisals an evaluation of the timeliness of closing out contracts. The Director of Acquisition and Logistics Systems agreed to act on all recommendations except the one that pertained to performance appraisals. Specific corrective actions included a request to the Director of Contract and Manufacturing Policy to submit a Defense Federal Acquisition Regulation Supplement change to require contract fund reviews and deobligation of excess funds within 30 days after physical completion of each contract. The Director of Contract and Manufacturing Policy will encourage the use of warranted contracting officers and will request the Air Force Logistics Command to monitor the timeliness of contract closeouts and propose alternatives to establishing performance standards.

Defense Logistics Agency, Report No. DCASR LA-DI 6-88, "Report on the Audit of Contract Administration Report (CAR) System," May 13, 1988.

This report stated that contract data included in the Contract Administration Report were not always current and accurate, and that management attention needs to be increased on open but dormant contracts. The report recommended that Defense Contract Administration Services Region, Los Angeles, take action to resolve the delinquent contract problem in section 1; close out all overage contracts in section 2; transfer contracts into the appropriate section of the Contract Administration Report within a reasonable time after cancellation or termination actions; establish priority in determining disposition over inactive contracts reported as dormant; deobligate excess funds on dormant contracts; and reclassify or close out dormant contracts resulting from pending settlement of overhead rates. The Defense Contract Administration Services Region, Los Angeles, Office of Comptroller concurred with the report findings. The Contract Management Directorate generally concurred with the audit findings and recommendations. The responses did not specifically state what actions would be taken to correct the reported deficiencies.

SYNOPSIS OF PRIOR AUDIT REPORTS ON ADMINISTRATION
OF THE CONTRACT CLOSEOUT PROCESS (Continued)

U.S. Army Audit Agency, Report No. HQ 87-705, "Contract Closeout Process," June 9, 1987.

The report stated that the interests of the Army were not properly protected by the contract closeout process, and that delays in the closeout process included delays in the deobligation of funds, the recovery of Government-furnished property and the recovery of overpayments to contractors. The report recommended that all information documents that discuss the requirements of the contract closeout process be prepared, published, and circulated; that performance standards on contract closeout be established for contracting personnel; that contract closeout be monitored Army-wide and included in coverage by Army inspection and review teams; that coordination with non-Army activities responsible for contract closeout be improved; that contractors be given incentives for timely completion of actions affecting contract closeout; that the Army instruct all contracting offices on the requirement to use checklists of closeout actions and actions to be taken when contractors delayed submission of overhead. The Director for Contracting, Office of the Assistant Secretary of the Army (Research, Development and Acquisition), agreed with all the recommendations in the report. Specific actions were to develop a desktop handbook on contract closeout, establish standards on contract closeout in performance plans, establish an Army-wide reporting system to monitor contract closeout, and instruct contracting officers to use checklists to monitor the progress of contract closeout.

U.S. Army Audit Agency Report No. MW 86-206, "Audit of Contract Administration," June 30, 1986.

This report stated that the U.S. Army Materiel Command placed a low priority on the closeout of contracts and lacked an adequate system to monitor actions needed to close contracts. Closeout checklists were not used to ensure that appropriate actions were taken prior to contract closeout, and contracting personnel were not aware of reasons for delays or of actions needed to close contracts. The report recommended that a policy statement be issued on the importance of the contract closeout process, that a checklist be developed and used by the contracting personnel, that the active contract report show when contracts exceed the closeout time frames in the Federal Acquisition Regulation, that commands furnish summary information on the closeout process for analysis and corrective action, that completed contracts exceeding the closeout time frames be reported to management, and that the U.S. Army Materiel Command monitor the effectiveness of contract closeout by the buying commands. The U.S. Army Materiel Command agreed with the report recommendations.

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DEFENSE LOGISTICS AGENCY
THE DEFENSE CONTRACT MANAGEMENT COMMAND
CAMERON STATION
ALEXANDRIA, VIRGINIA 22304 6190



IN REPLY
REFER TO

DLA-A

17 JUL 1990

SUBJECT: Fiscal Year (FY) 1991 Appropriation Act Changes
Affecting Contract Closeout

TO: Commanders of DCM Districts
ATTN: Directors, Contract Management

1. Congress recently passed the FY 91 Appropriation Act. Provisions of the act require the closeout of all procurement appropriation accounts on 30 September of the fifth fiscal year after the period of availability for obligation ends.
2. Prior to this legislation, when the period of availability for obligation ended, expired funds retained their FY identity for a two-year period. After two years all obligated, but unliquidated balances, were transferred to a M Account which was not governed by any time constraints. This allowed obligations to be cleared against the account whenever the associated contracts were closed.
3. Under the new procedures, when the period of availability for obligation ends, the balances of the appropriation remain in an expired category. These funds are available to liquidate obligations and fund valid upward obligation adjustments for five years. After five years all balances (obligated and unobligated) are canceled. Obligations outstanding after the five year period must be charged to a current appropriation account of the agency available for the same purpose. There will no longer be any M Accounts.
4. The time period governing availability for obligation varies by the type of funding. Generally the timeframes are 3 years for procurement funds, 2 years for Research, Development, Test & Evaluation (RDT&E), and 1 year for Operations & Maintenance (O&M). The law provides for gradual implementation of the closing of various accounts. The first milestone requires identification of payments required to be made from obligated balances that expired at the end of FY 83 or earlier by 6 March 1991. A timetable for transition procedures is provided as Enclosure 1. Payment for the obligations identified as expired at the end of FY 83 or prior must be made by 4 May 1991 or they will have to be made out of current appropriations.
5. These changes make it imperative that contracts are closed in accordance with the timeframes. After the end of each time period, funds for payment or adjustment of any remaining contractual obligations will no longer be available. To meet remaining obligations, for those contracts that are not closed, current year funding must be requested from, and obligated by the purchasing activity. The purchasing activities will not be receptive to use of current funding to meet old obligations resulting from resolution of administrative actions long after the items or services have been delivered.

DLA-A PAGE 2

SUBJECT: Fiscal Year (FY) 1991 Appropriation Act Changes Affecting Contract Closeout

6. All steps necessary to close affected contracts must be taken. A partial list of recommended actions is provided as Enclosure 2. Attention should be given to completion of outstanding contract reconciliations. We strongly encourage partial close out and settlement on those contracts where there are outstanding and all amounts cannot be settled. Prompt and aggressive management attention must be given to accomplishing the best effort toward resolution of outstanding issues.

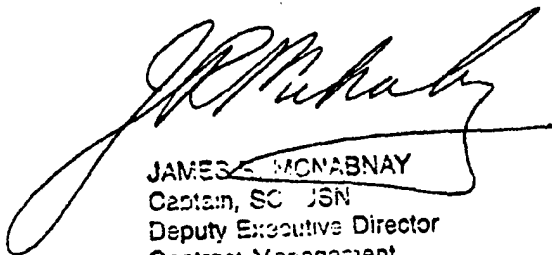
7. We recommend that you identify those contractors who have not submitted adequate overhead rate proposals for the affected years. Every effort should be made to impress upon them the necessity of submitting a proposal. The Defense Contract Audit Agency (DCAA) has instructed their Regional Directors to program and prioritize these audits to allow for completion by 28 February 1991 for FY 85 and before. DCAA will not provide for the usual 60 days allowed for contractor rebuttal of their findings. If the contractors nonconcur, DCAA will issue a Form 1 and forward the audit to the Administrative Contracting Officer (ACO) for resolution. They have also instructed their Regional Directors to give priority attention to reviewing final Public Vouchers submitted under any affected contracts.

8. DCAA provided the list at Enclosure 3 of contractors who have not submitted acceptable rate proposals. This information, used in conjunction with your recent Report on Status of Open Overhead Negotiations (RCS DD-DR&E(SA)1558), should enable you to identify those contractors requiring your immediate attention. Also included for your information is a listing provided by DCAA reflecting contractor overhead years that their records show as audited but not settled (Enclosure 4).

9. Request you provide a status report to Headquarters DLA, ATTN: DLA-AC by 15 January 1991. Include in your report the number of contracts and unliquidated obligations that will fall under the March and September 1991 transition dates. Also include information pertaining to contracts that are in litigation or under investigation. Also provide the name and phone number of the person in your District responsible for contract closeout issues. Any questions or suggestions should be directed to Manette Audet, AV 284-7644 or Commercial (703) 274-7644. The information in this letter should be given the widest possible dissemination.

3 Encl

1. Transition Procedures
2. Recommended Actions
- *3. Missing Proposals
- *4. Open Overhead Years



JAMES S. MCNABNEY
Captain, SC USN
Deputy Executive Director
Contract Management

*These enclosures do not appear in this report.

TRANSITION PROCEDURES

1. 6 March 1991 - All obligated balances for appropriations that expired at the end of FY 83 and before are canceled. Generally, this means that any amounts owed for contracts entered into in 1983 using;

1983 O&M Appropriations,
1982 RDT&E Appropriations, and
1981 Procurement Appropriations,

and prior appropriations are canceled and are no longer available to clear contract obligations. Amounts paid after 6 March 1991, will be charged against current appropriations. It should be noted that costs associated with these contracts will be incurred subsequent to the year of award.

An exception to this provision is that funds do not have to be canceled if there is documentary evidence that, as of 6 March 1991, the associated payment will be made by 4 May 1991.

2. 30 September 1991 - All obligated balances that expired at the end of FY 84 are canceled. This means that any amounts owed for contracts entered into in 1984 using;

1984 O&M Appropriations,
1983 RDT&E Appropriations, and
1982 Procurement Appropriations,

are canceled and are no longer available to clear contract obligations.

3. 30 September 1992 - All obligated balances that expired at the end of FY 85 are canceled. This means that any amounts owed for contracts entered into in 1985 using;

1985 O&M Appropriations,
1984 RDT&E Appropriations, and
1983 Procurement Appropriations,

are canceled and are no longer available to clear contract obligations.

4. 30 September 1993 - All obligated balances that expired at the end of FY 86 are canceled. This means that any amounts owed for contracts entered into in 1986, 1987, and 1988 using;

1986, 1987, 1988 O&M Appropriations,
1985, 1986, 1987 RDT&E Appropriations, and
1984, 1985, 1986 Procurement Appropriations,

are canceled and are no longer available to clear contract obligations.

RECOMMENDED ACTIONS

1. Complete reconciliations of Fixed Price Contracts
2. Complete negotiations of outstanding DCAA Form 1s and open overheads, where possible.
3. For those contractors whose rates were audit determined, and any where negotiations have been successfully concluded, ensure that contractors submit their final Public Vouchers.
4. Ensure that contractors submit overhead proposals for open years.
5. Encourage expansion of the use of quick closeout procedures especially where contractors may have few cost type contracts and there is not a significant cost impact on the Government.
6. Accomplish partial closeout and settlement where all outstanding issues and amounts pending payment cannot be settled.

Enclosure 2

ACTIVITIES VISITED OR CONTACTED

Office of the Secretary of Defense

Office of the Comptroller of the Department of Defense,
Washington, D.C.
Assistant Secretary of Defense (Production and Logistics),
Washington, D.C.

Department of the Army

U.S. Army Missile Command, Redstone Arsenal, AL

Defense Agencies

Defense Contract Audit Agency, Alexandria, VA
Defense Logistics Agency, Alexandria, VA
Defense Contract Management District Mid Atlantic,
Philadelphia, PA
Defense Contract Management Area Operations, Baltimore, MD
Defense Contract Management Area Operations, Philadelphia,
PA
Defense Plant Representative Office, General Electric,
Moorestown, NJ
Defense Plant Representative Office, International Business
Machines, Manassas, VA

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AUDIT TEAM MEMBERS

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Salvatore D. Guli, Program Director
Linda A. Pierce, Project Manager
Rayburn H. Stricklin, Project Manager
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Douglas B. Reed, Team Leader
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Thomas Smith, Auditor
R. Steven Silverstein, Auditor
Beth A. Kilborn, Auditor
Billy J. McCain, Auditor
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FINAL REPORT DISTRIBUTION

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Secretary of the Army
Assistant Secretary of the Army (Financial Management)
Department of the Army Inspector General

Department of the Navy

Secretary of the Navy
Assistant Secretary of the Navy (Financial Management)
Auditor General, Naval Audit Service

Department of the Air Force

Secretary of the Air Force
Assistant Secretary of the Air Force (Financial Management
and Comptroller)
Air Force Audit Agency

Defense Activities

Director, Defense Contract Audit Agency
Director, Defense Logistics Agency
Commander, Defense Contract Management District Mid Atlantic
Director, Defense Logistics Studies Information Exchange

Non-DoD Activities

Office of Management and Budget

U.S. General Accounting Office,
NSIAD Technical Information Center

Congressional Committees:

Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
Senate Ranking Minority Member, Committee on Armed Services
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Ranking Minority Member, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Operations
House Subcommittee on Legislation and National Security,
Committee on Government Operations