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United States  
Department of Defense



Controls Over Contract Obligation Data  
in the Logistics Modernization Program

# Report Documentation Page

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## Acronyms and Abbreviations

AMC	Army Materiel Command
AWCF	Army Working Capital Fund
CECOM	Communications-Electronics Life Cycle Management Command
DFAS	Defense Finance and Accounting Service
FMR	Financial Management Regulation
LMP	Logistics Modernization Program
MOD	Miscellaneous Obligation Document
PADDS	Procurement Automated Data and Document System
PEO EIS	Army Program Executive Office, Enterprise Information Systems
TACOM	TACOM Life Cycle Management Command
UCA	Undefinitized Contract Action
U.S.C.	United States Code



INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
400 ARMY NAVY DRIVE  
ARLINGTON, VIRGINIA 22202-4704

June 15, 2009

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)/  
DOD CHIEF FINANCIAL OFFICER  
AUDITOR GENERAL, DEPARTMENT OF THE ARMY

SUBJECT: Controls Over Contract Obligation Data in the Logistics Modernization Program  
(Report No. D-2009-087)

We are providing this report for review and comment. We considered management comments on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. Comments the Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer; Commander, U.S. Army Materiel Command; and the Commander, Communications-Electronics Life Cycle Management Command were responsive. However, the comments from the Army Program Executive Officer, Enterprise Information Systems were only partially responsive. We request additional comments on Recommendation B.2. by July 15, 2009.

Please provide comments that conform to the requirements of DoD Directive 7650.3. If possible, send your comments in electronic format (Adobe Acrobat file only) to [auidbo@dodig.mil](mailto:auidbo@dodig.mil). Copies of your comments must have the actual signature of the authorizing official for your organization. We are unable to accept the / Signed / symbol in place of the actual signature. If you arrange to send classified comments electronically, you must send them over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 601-5868 (DSN 329-5868).

*Patricia A. Marsh*  
Patricia A. Marsh, CPA  
Assistant Inspector General  
Defense Business Operations





# Results in Brief: Controls Over Contract Obligation Data in the Logistics Modernization Program

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## What We Did

We evaluated the effectiveness of controls over the recording and reporting of contract obligations in the Logistics Modernization Program (LMP) system. We compared contract line obligations recorded in the Procurement Automated Data and Document System to the corresponding purchase order obligations recorded in LMP. We researched LMP and Procurement Automated Data and Document System records to identify causes for differences in recorded contract obligations. In addition, we reviewed miscellaneous obligation documents recorded as of September 30, 2007, for compliance with established laws and the DoD Financial Management Regulation.

## What We Found

The accuracy of obligations recorded for purchase orders has significantly improved since the Army Program Executive Office, Enterprise Information Systems implemented system process changes in May 2005, and the Communications-Electronics Life Cycle Management Command (CECOM) established better internal control procedures. However, CECOM had not fully documented its processes and controls, and its internal controls over miscellaneous obligation documents were not adequate. We identified a material internal control weakness. CECOM failed to comply with established laws and regulations when obligating funds at fiscal year-end. As a result, CECOM overstated the obligation balance on the FY 2007 Army Working Capital Fund Statement of Budgetary Resources by at least \$24.4 million.

## What We Recommend

We recommend that the Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer revise the guidance for obligating undefinitized contract actions. We recommend that the Commander, U.S. Army Materiel Command require that the Life Cycle Management Commands implement standard operating procedures for processing and controlling LMP commitment and contract obligation data. We recommend that the Army Program Executive Officer, Enterprise Information Systems formalize a plan to change LMP system functionality to correctly process contract and accounting data when there are differences between units of measurement on the purchase requisition and the purchase order. We recommend that the Commander, CECOM develop standard operating procedures that fully document processes and controls.

## Management Comments and Our Response

The Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer; the Commander, U.S. Army Materiel Command; and the Commander, CECOM agreed with the recommendations. The Army Program Executive Officer, Enterprise Information Systems agreed with Recommendation B.2.; however, the comments were only partially responsive. See the full text of the comments in the Management Comments section of the report. We request additional comments from the Army Program Executive Officer. Please see the recommendations table on the back of this page.

<b>Management</b>	<b>Recommendations Requiring Comment</b>	<b>No Additional Comments Required</b>
Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer		B.1.
Commander, U.S. Army Materiel Command		A.1.
Army Program Executive Officer, Enterprise Information Systems	B.2.	
Commander, Communications- Electronics Life Cycle Management Command		A.2. and B.3.

Please provide comments by July 15, 2009.

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# Introduction

## Objective

Our audit objective was to evaluate the effectiveness of controls over the recording and reporting of contract obligations in the Logistics Modernization Program (LMP) system. See Appendix A for a discussion of the scope and methodology and prior audit coverage related to the objective. See Appendix B for a glossary of common terms used in the report.

## Background

LMP represents the Army's business system modernization effort to provide an integrated logistics and accounting system to manage the Industrial Operations, Army and the Supply Management, Army activity groups of the Army Working Capital Fund (AWCF). LMP integrates the business processes of sales forecasting, order entry, manufacturing, distribution, materiel management, inventory, and financial information management. The Army Program Executive Office, Enterprise Information Systems (PEO EIS) has program management responsibility for LMP.

Implementation of LMP began in July 2003 at Headquarters, U.S. Army Materiel Command (AMC); the Communications-Electronics Life Cycle Management Command (CECOM); Tobyhanna Army Depot; and the Defense Finance and Accounting Service (DFAS) field sites at Rock Island, Illinois, and St. Louis, Missouri.<sup>1</sup> AMC and the PEO EIS plan to begin the second deployment in March 2009 at the Aviation and Missile Life Cycle Management Command, the Corpus Christi Army Depot, and the Letterkenny Army Depot. AMC and the PEO EIS are planning the third deployment for January 2010 at the TACOM Life Cycle Management Command, the Anniston Army Depot, the Red River Army Depot, the Rock Island Arsenal, the Sierra Army Depot, and the Watervliet Arsenal.<sup>2</sup>

A SeeBeyond interface passes data between LMP and other DoD automated systems.<sup>3</sup> At CECOM, the Logistics Readiness Center used LMP to generate purchase requisitions for AWCF materiel and for repair and maintenance of repairable inventory assets. The funded purchase requisition creates a commitment document that is recorded in the LMP Financial Accounting Module, which has a General Ledger component and a Funds Management component. The General Ledger component contains the U.S. Standard General Ledger accounts. The Funds Management component is used to manage the budget funding authority and shows funds committed for each purchase requisition and

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<sup>1</sup> The DFAS St. Louis field site relocated to DFAS Columbus, Ohio, in July 2007.

<sup>2</sup> The TACOM Life Cycle Management Command was formerly known as Tank and Automotive Command. It is now simply referred to as TACOM.

<sup>3</sup> SeeBeyond Technology Corporation, now part of Sun Microsystems, Inc., develops business integration application software.

funds obligated for the related purchase order.<sup>4</sup> The purchase requisitions process through the SeeBeyond interface to the CECOM Contracting Center,<sup>5</sup> which uses the Procurement Automated Data and Document System (PADDS) to prepare the contracts for purchases of materiel and maintenance and repair services. PADDS returns the contract data back through the SeeBeyond interface to LMP, which updates the commitment and obligation data recorded in the LMP Financial Accounting Module.

After the initial fielding of LMP in July 2003, CECOM reported significant problems with the accuracy of obligations recorded in LMP. In its review of obligations recorded in LMP for FYs 2003 through 2005, the U.S. Army Audit Agency reported that as of September 30, 2003, CECOM had reported a \$221.7 million difference between the obligations recorded in LMP and the manual records kept by operating personnel.<sup>6</sup> In addition, CECOM reported in October 2003 that more than 20 percent of contract line items were rejected during the SeeBeyond interface process between PADDS and LMP. By September 30, 2005, CECOM reported that the contract line reject rate had significantly decreased to about 8 percent. As a result of the improvements in LMP financial reporting processes, CECOM gave an unqualified certification to the FY 2005 financial reports generated by LMP. CECOM attributed the decrease in rejected contract lines to improved LMP functionality, more management reports, and better training of operating personnel.

The Combined Statement of Budgetary Resources, part of the AWCf principal financial statements, identifies the sources of budget resources and the obligations incurred during the reporting period. For FY 2007, the Army reported that the obligations incurred by the AWCf Industrial Operations and Supply Management, Army activity groups totaled \$16.8 billion.

## **Review of Internal Controls**

We identified a material internal control weakness for CECOM as defined by DoD Instruction 5010.40, “Managers’ Internal Control Program (MIC) Procedures,” January 4, 2006. CECOM had not implemented procedures for preparing year-end miscellaneous obligation documents that complied with established laws and regulations. As a result, CECOM overstated the year-end obligation balance reported on the FY 2007 AWCf Statement of Budgetary Resources by at least \$24.4 million.<sup>7</sup> Implementing Recommendations A.1. and B.3. will improve internal controls. We provided a copy of this report to the senior CECOM official responsible for internal controls.

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<sup>4</sup> In LMP, “purchase order” is synonymous with “contract award.” A contract can consist of multiple contract line item numbers that identify the items of supply or services included in the contract. The corresponding purchase order number in LMP will show the same data for each contract line item number.

<sup>5</sup> Effective October 1, 2008, the CECOM Contracting Center, formally known as the CECOM Acquisition Center, was organizationally realigned from CECOM to the Army Contracting Command.

<sup>6</sup> U.S. Army Audit Agency Report No. A-2007-0163-FFM, “FY 03 - FY 05 Obligations Recorded in the Logistics Modernization Program,” July 27, 2007.

<sup>7</sup> Office of the Assistant Secretary of the Army (Financial Management and Comptroller) memorandum, “Management Representations for the Fiscal Year (FY) 2008 Department of the Army’s Working Capital Fund Principal Financial Statements Taken as a Whole,” November 8, 2008, states that an omission or misstatement involving \$10.6 million or more is material.

## **Finding A. Recorded Obligations**

Since the PEO EIS implemented system process changes and CECOM established better internal control procedures, the accuracy of obligations recorded for purchase orders in LMP has significantly improved. CECOM reported that the percentage of contract lines rejected during the PADDSS-to-LMP interface decreased from 16.9 percent in May 2005 to 3.7 percent in May 2007. In addition, our comparison of contract line obligations recorded in PADDSS to the purchase order contract line obligations recorded in LMP showed that almost all obligations accurately posted in LMP. Although CECOM has implemented improved processes and internal controls, it has not fully documented the processes and controls. As a result, AMC lacks assurance that these processes and controls will be applied uniformly and consistently in the event of personnel changes or during future LMP deployments. CECOM should fully document its controls and procedures and AMC should require the other Life Cycle Management Commands to implement these controls and procedures upon future deployments of LMP.

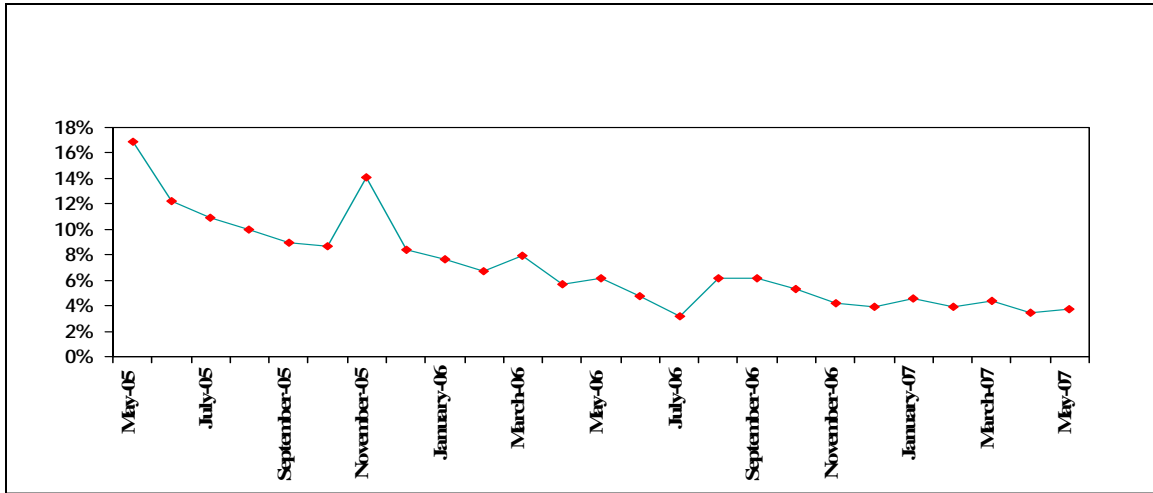
### **Improvement Initiatives**

As a result of problems encountered in recording and reporting commitment and obligation data during the initial fielding of LMP, the PEO EIS and CECOM took actions to improve LMP system processes and internal controls. In May 2005, the PEO EIS rewrote the PADDSS-to-LMP interface process, increasing the frequency of PADDSS file transfers from two or three per month to three per day. The PEO EIS also developed additional reports to track and monitor the transfer of purchase requisition and contract data between systems. In addition, CECOM implemented internal control procedures to ensure the accuracy and completeness of contract data passed to and from LMP and PADDSS and the prompt correction of erroneous data. These control procedures included the following.

- The Logistics Readiness Center monitored the purchase requisition commitments and purchase order obligations recorded in the General Ledger and Funds Management components of the LMP Financial Accounting Module and reconciled them daily.
- The Contracting Center used LMP and PADDSS reports to verify that all LMP-generated purchase requisitions passed to PADDSS and that the PADDSS-generated contract line data passed to LMP.
- The Resource Management Directorate used a PADDSS-generated text file of contract lines to verify that the data posted accurately in LMP or that rejected transactions went to the Suspended Contract Listing. In addition, the Contracting Center used the Suspended Contract Listing to monitor and report the status of contract lines rejected during the PADDSS-to-LMP interface.

These combined actions resulted in a significant decrease in the percentage of contract lines rejected during the PADDs-to-LMP interface. The percentage of contract lines rejected decreased from 16.9 percent in May 2005 to 3.7 percent in May 2007, as shown in the following graph.

**PADDs-to-LMP Transaction Reject Rates From May 2005 Through May 2007**



## Results of Contract Obligations Match

The accuracy of obligations recorded for purchase orders in LMP has significantly improved since May 2005. We compared the contract line obligations recorded in PADDs to the corresponding purchase order obligations recorded in LMP. We matched obligations by comparing the contract line item number and dollar amount recorded in PADDs to the purchase order line item number and the dollar amount recorded in the LMP Financial Accounting Module. The PADDs file included 8,705 contract obligations recorded from May 1, 2005, through June 30, 2007, and the LMP file included 8,261 obligations recorded from May 1, 2005, through August 17, 2007. We reviewed contract obligation data beginning with May 1, 2005, because that is when the PEO EIS rewrote the PADDs-to-LMP interface process and increased the frequency of PADDs file transfers. We reviewed 118 of 444 mismatches and concluded that almost all the obligations posted accurately in LMP. We brought the exceptions we identified to the attention of CECOM personnel. The following table shows the data match results.

**PADDs/LMP Obligation Data Match Review**

<b>Matches</b>	<b>Net Dollar Value</b>	<b>Contract Lines</b>
Contract Obligations in PADDs	\$3,692,331,867	8,705
Contract Obligations in LMP	3,622,106,529	8,261
<b>Difference</b>	<b>\$ 70,225,338</b>	<b>444</b>
<b>Mismatches Identified:</b>		
No Matching Contract Line in LMP	\$45,925,991	404
Different Obligation Amount in LMP	24,299,347	40
<b>Total Mismatches</b>	<b>\$70,225,338</b>	<b>444</b>

We judgmentally sampled 78 of the 404 instances where the contract line item number in PADDs did not have a purchase order line item number in LMP. With the assistance of CECOM personnel, we researched PADDs and LMP records to determine causes for the missing contract line items in LMP.

- The data match review flagged 69 of the 78 mismatches because the PADDs data file included all open contract line items, but the LMP data file included only active purchase order line items that cited CECOM funds.<sup>8</sup>
- Five mismatches resulted from delays in correcting contract line items that rejected to the Suspended Contract Listing when the data passed from PADDs to LMP. CECOM personnel researched and correctly posted these five contract line items to LMP after August 17, 2007, the cutoff date of the LMP data file.
- Only 4 of the 78 contract lines did not have a matching purchase order line item recorded in LMP. We informed CECOM personnel of the four mismatches, and they researched and posted the purchase order line items in LMP. CECOM personnel did not give a specific reason for the purchase order line items not posting correctly in LMP.

We also reviewed 40 mismatches for which the contract line item number had different obligation amounts recorded in PADDs and LMP.

- Fifteen mismatches resulted when the contract line item from PADDs was split and recorded in LMP as two separate line items on the same purchase order. During the initial fielding of LMP in July 2003, these 15 contract line items were recorded as part active and part inactive on the purchase order. The obligation amounts recorded for the active and inactive line items in LMP agreed with the total contract line item value in PADDs.
- Three mismatches resulted from delays in correcting contract amendments that had rejected to the Suspended Contract Listing during the PADDs-to-LMP interface. CECOM personnel researched and correctly posted these three contract line item amendments to LMP after August 17, 2007, the cutoff date of the LMP data file.
- Another 13 mismatches were the result of contract amendments processed for undefinitized contract actions (UCAs). (See finding B for more details on UCAs.) These contract amendments processed before the PEO EIS improved LMP

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<sup>8</sup> LMP retains a record of both active and inactive purchase orders recorded since CECOM fielded the system in July 2003. LMP codes the purchase order as inactive once the purchase order, goods receipt, and invoice receipt amounts match.

functionality for processing UCAs and amendments in June 2006. We provided information on the 13 contract lines to CECOM personnel, and they corrected the purchase order line items in LMP.

- The remaining nine mismatches were primarily the result of contract amendments from PADDs failing to post in LMP, or CECOM personnel making manual adjustments to the dollar amount or purchase quantity of the purchase order line item in LMP. CECOM personnel could not provide an explanation for the contract amendments not posting in LMP or the manual adjustments. We provided the information on these purchase order line items to CECOM and DFAS Columbus personnel, who then researched and corrected the LMP financial data.

In addition, we did a reverse data match of obligations by comparing the purchase order line item number and the dollar amount recorded in LMP to the contract line item number and the dollar amount recorded in PADDs. The data comparison identified 37 mismatches for which the purchase order number in LMP did not match a contract line item number in PADDs. The Contracting Center entered 29 contract lines into PADDs after June 30, 2007, the cutoff date for the PADDs data file. The other eight mismatches involved cancellations of contract line items that were recorded in LMP as of August 17, 2007. These eight contract lines rejected to the Suspended Contract Listing during the PADDs-to-LMP interface, but CECOM personnel did not correct them until after August 17, 2007. The data match also identified the same 40 differences discussed in the preceding paragraph.

## **LMP Deployment**

In preparation for fielding LMP at the Aviation and Missile Life Cycle Management Command in March 2009, AMC and the PEO EIS have developed detailed plans for migrating data from a legacy system, the Commodity Command Standard System, to LMP. The data migration plans include validating the accuracy of PADDs contract data in the legacy system and performing three tests to validate that the data accurately loaded into LMP. Effective implementation of the data migration plans should ensure that the contract data in PADDs and LMP accurately correspond, when fielding LMP at the Aviation and Missile Life Cycle Management Command.

However, as demonstrated at CECOM, effective controls and procedures are required to ensure the accuracy and completeness of the purchase requisition and the contract line item data passing between the two systems. CECOM had procedures and controls in place to monitor and verify the completeness and accuracy of the data. However, CECOM had neither fully documented the procedures and controls for monitoring, verifying, correcting, and reporting on contract data passing between the two systems, nor assigned responsibility to ensure that they were implemented and uniformly followed in the event of personnel changes. Rather, CECOM focused its resources on processing daily transactions and working with the PEO EIS to improve LMP processes and reports. CECOM should develop standard operating procedures to fully document its processes and controls over LMP and PADDs contract data, and AMC should require that the

Aviation and Missile Life Cycle Management Command and the TACOM implement similar standard operating procedures upon fielding of LMP. These controls and procedures include but are not limited to:

- daily monitoring and reconciliation of the purchase requisitions and purchase orders recorded in the General Ledger and the Funds Management components of the LMP Financial Accounting Module,
- verifying that all LMP-generated purchase requisitions pass to PADDs,
- ensuring that the contract line item data in PADDs post accurately to LMP or rejects to the Suspended Contract Listing, and
- requiring monthly reports on the number and status of contract lines rejected during the PADDs-to-LMP interface.

## **Conclusion**

The PEO EIS and CECOM have significantly increased the accuracy of contract obligation data recorded in LMP by improving system processes and internal control procedures. However, CECOM has not fully documented its processes and controls for monitoring, correcting, and reporting on the purchase requisition and contract data passed to and from LMP and PADDs. As a result, AMC lacks assurance that these processes and controls will be applied uniformly and consistently in the event of personnel changes or during future LMP deployments. CECOM should fully document its processes and controls over commitment and obligation data passed to and from LMP and PADDs. In addition, AMC should require that the Aviation and Missile Life Cycle Management Command and TACOM Life Cycle Management Command implement similar processes and controls when they deploy LMP.

## **Recommendations, Management Comments, and Our Response**

**A.1. We recommend that the Commander, U.S. Army Materiel Command, require that the Aviation and Missile Life Cycle Management Command and the TACOM Life Cycle Management Command implement standard operating procedures for processing and controlling commitment and contract obligation data based on the procedures developed by the Communications-Electronics Life Cycle Management Command when it deploys Logistics Modernization Program.**

### ***Army Materiel Command Comments***

The Commander, AMC agreed and stated that AMC is working with the CECOM Life Cycle Management Command to finalize the standard operating procedures by April 30, 2009. AMC will incorporate the final standard operating procedures into the LMP deployment implementation plan.

### ***Our Response***

The Commander, AMC comments are responsive. No further comments are required.

**A.2. We recommend that the Commander, Communications-Electronics Life Cycle Management Command develop standard operating procedures that fully document existing processes and controls over commitment and contract obligation data passed to and from the Logistics Modernization Program and the Procurement Automated Data and Document System.**

### ***Communications-Electronics Life Cycle Management Command Comments***

The Commander, CECOM agreed and stated that it will develop standard operating procedures to document existing control procedures for commitments and obligations by April 30, 2009.

### ***Our Response***

The Commander, CECOM comments are responsive. No further comments are required.

## **Finding B. Miscellaneous Obligation Documents**

CECOM did not comply with established laws and the DoD Financial Management Regulation (FMR), volume 3, when obligating AWCF funds at fiscal year-end using miscellaneous obligation documents (MODs). Of the \$27.6 million obligated on two MODs at FY 2007 year-end, at least \$16.7 million was an invalid or a duplicate obligation. In addition, CECOM processed a \$7.7 million invalid obligation transaction. As a result, CECOM overstated the year-end obligation balance reported on the FY 2007 AWCF Statement of Budgetary Resources by at least \$24.4 million. The Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer should revise the DoD FMR, volume 3, and require DoD Components to commit and obligate the fiscal year budget funding authority in effect at the time the UCA is definitized. The PEO EIS should formalize a plan to change LMP system functionality to correctly process contract and accounting data when there is a different unit of measurement used on the purchase requisition than is used on the purchase order. In addition, CECOM should develop standard procedures for verifying, documenting, and approving year-end MODs.

### **Obligation Process**

CECOM received funding authority totaling \$1.9 billion to operate the AWCF Supply Management, Army activity group for FY 2007. The funding authority sets the limit on the total obligations CECOM can incur for the fiscal year.

Section 1501, title 31, United States Code (31 U.S.C. 1501) states that an amount should be recorded as an obligation when supported by documentary evidence of a binding agreement between an agency and another party. The obligation must be made during the period of the appropriation's availability and must be used to acquire specific goods or services. DoD FMR, volume 3, chapter 8, "Standards for Recording and Reviewing Commitments and Obligations," sets forth the basis for determining the amount and the accounting period in which commitments and obligations should be recorded under various circumstances. DoD Components are responsible for recording commitments to meet only bona fide needs of the period for which funds are appropriated. The amount recorded as a commitment is the estimated cost of goods and services being acquired. A commitment document ensures that funds are available prior to incurring an obligation. DoD Components are responsible for recording obligations only when supported by documentary evidence of the orders placed, contracts awarded, or services received. When the obligation amount is not known at the time it should be recorded, the DoD Component should make a best estimate, based on a thorough analysis of available transaction data. DFAS Indianapolis Regulation 37-1, "Finance and Accounting Policy Implementation," requires the fund holder to use DD Form 2406, "Miscellaneous Obligation Document," to document and support an estimated obligation.

UCAs allow the contractor to begin performance before agreeing to the final contract terms, specifications, or price. UCAs are used only to meet urgent requirements and only after confirmation that no other contracting method will fulfill the urgent need. Section 2326, title 10, United States Code (10 U.S.C. 2326), “Undefinitized Contractual Actions: Restrictions,” restricts the use of UCAs to an urgent requirement of a DoD Component and establishes limitations on the obligation of funds, the definition of terms, and allowable profit for UCAs. Contracting officers for UCAs may not obligate the DoD Component to an amount that is equal to more than 50 percent of the negotiated overall ceiling price until the contract terms, specifications, and price are finalized. Contracting officers are generally required to finalize the terms and conditions of UCAs within 180 days of initiation, before more than 50 percent of the estimated contract price is obligated or before more than 40 percent of the work is completed, whichever occurs first.

## **Fiscal Year-End Obligations**

CECOM personnel recorded invalid or duplicate obligations totaling at least \$24.4 million at FY 2007 year-end. In late September 2007, CECOM, with assistance from the LMP contractor, queried the Funds Management component of the LMP Financial Accounting Module to find the purchase orders in LMP that had an undefinitized contract amount and to find any purchase requisitions with an outstanding commitment amount.<sup>9</sup> The data query identified 15 purchase orders with undefinitized amounts totaling \$13.8 million and 214 purchase requisitions with outstanding commitment amounts totaling \$13.8 million. On September 30, 2007, CECOM processed transactions to decrease the funds committed for each of the 214 purchase requisitions. At the same time, CECOM recorded two MODs to obligate the total \$27.6 million using FY 2007 AWCF funding authority. CECOM personnel stated that personnel within the AMC Office of the Deputy Chief of Staff for Resource Management (G-8) instructed them, as part of the fiscal year-end closeout process, to obligate funds for the undefinitized part of the UCAs and for the purchase requisitions with an outstanding commitment amount. On October 1, 2007, CECOM recorded a commitment for each of the 214 purchase requisitions using FY 2008 funding authority. On October 22, 2007, CECOM reversed the two MODs.<sup>10</sup>

We selected a judgmental sample of 4 of the 15 UCAs, valued at \$13.2 million and 10 of the 214 purchase requisitions valued at \$3.6 million, to determine whether a valid obligation existed as of September 30, 2007. We concluded that valid obligations did not

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<sup>9</sup> UCAs contain a not-to-exceed price and firm obligation amount. The not-to-exceed price is the negotiated overall contract ceiling price. CECOM contracting officers set the obligation amount at 49 percent of the not-to-exceed price. The difference between the not-to-exceed price and the obligation amount is the undefinitized part of the purchase order. LMP was not designed to retain an outstanding commitment amount for the undefinitized part of the UCA.

<sup>10</sup> Reversing the MOD generated a debit to the Downward Adjustment to the Prior-year Obligations account (general ledger account code 4871) and a credit to the Allotments Realized account (general ledger account code 4610). The effect of reversing the MOD was a transfer of funding authority from FY 2007 to FY 2008.

exist as of September 30, 2007, for the 4 UCAs and the 10 purchase requisitions. In addition, CECOM recorded a \$7.7 million invalid obligation transaction for an additional UCA.

### ***Undefinitized Purchase Orders***

CECOM did not comply with 10 U.S.C. 2326 when it recorded obligations in the accounting records at fiscal year-end for the undefinitized part of the four UCAs totaling \$13.2 million. According to 10 U.S.C. 2326, contracting officers using UCAs may not obligate an amount that is equal to more than 50 percent of the negotiated overall ceiling price until they definitize the contract terms, specifications, and price for the contractual action. CECOM contracting officers complied with this requirement and obligated, as part of the contract, only 49 percent of the contract ceiling price. The following is an example of contract terms included in a letter contract for one of the UCAs issued by CECOM: “A not-to-exceed price of \$5,686,527.00 has been set for this contract, subject to downward negotiation only. CECOM funded this procurement at 49 percent of the not-to-exceed price until definitization takes place.”

The contract administration data for this UCA, dated July 2, 2007, showed funds obligated of \$2,786,398.23, or 49 percent of the not-to-exceed price. CECOM recorded an obligation for the same amount in LMP. On September 30, 2007, CECOM personnel recorded an additional obligation of \$2,913,601.20 for the undefinitized part of the UCA.<sup>11</sup> In using the MOD to obligate an additional amount for the undefinitized part of the UCA, CECOM followed their normal business practice and DoD FMR, volume 3, chapter 8, paragraph 080507C guidance. However, paragraph 080507C does not comply with 10 U.S.C. 2326 and conflicts with guidance in paragraphs 080507A and B regarding the obligation amount to record in the financial records. Paragraph 080507 states:

- A. When the offer and acceptance are sufficiently specific and definitive to show the purpose and scope of the final contract to be executed, a letter contract or a letter of intent and any amendments to them accepted in writing by the contractor are documentary evidence to support the recording of an obligation. The obligation shall be recorded in the amount stated as the maximum liability under the letter or amendment.
- B. The maximum liability may be a limitation on the amount of obligations that may be incurred pending execution of a definitive contract. In this case, the estimated amount of the definitive contract, over and above the obligation recorded under the letter of intent, shall be carried as a commitment, pending execution of the definitive contract ...
- C. Commitments cannot be carried past the fiscal year end. A miscellaneous obligation document must be recorded at fiscal year end.

The guidance in paragraph 080507C does not comply with 10 U.S.C. 2326. The DoD FMR states that DoD Components will record a miscellaneous obligation at fiscal year-end for the undefinitized part of the contract. However, the statute states that

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<sup>11</sup> LMP showed a not-to-exceed price of \$5,699,999.43 or \$13,472.43 more than the letter contract price of \$5,686,527.00, which increased the obligation for the undefinitized part of the UCA from \$2,900,128.77 to \$2,913,601.20.

contracting officers may not obligate more than 50 percent of the overall ceiling price until they definitize contract terms, specifications, and price. Three of the four UCAs were not definitized until the first and second quarters of FY 2008. The Contracting Center definitized the fourth contract on September 29, 2007. However, Logistics Readiness Center personnel erroneously included it as a duplicate obligation in the year-end MOD.

In addition, paragraphs 080507A and B conflict with paragraph C guidance. Paragraph 080507A states that an obligation should be recorded in the amount stated as the maximum liability under the letter contract. Paragraph 080507B states that the estimated amount over and above the recorded obligation amounts should be carried as a commitment, pending execution of a definitive contract. However, paragraph 080507C states that a commitment cannot be carried past the fiscal year-end and a miscellaneous obligation must be recorded at fiscal year-end. The guidance can be interpreted to mean that a valid contractual obligation exists only at fiscal year-end.

The noncompliant and conflicting guidance resulted in inconsistent and inaccurate reporting of obligations on the monthly and fiscal year-end AWCF financial reports. The Office of the Under Secretary of Defense (Comptroller) should delete the DoD FMR requirement to record a miscellaneous obligation at fiscal year-end for the undefinitized amount of the UCA. In accordance with 10 U.S.C. 2326, the DoD FMR should require DoD Components to obligate funding authority in the fiscal year in which the UCA is definitized. In addition, CECOM should discontinue the current business practice of obligating 100 percent of the value of UCAs at fiscal year-end.

### ***Purchase Requisitions***

CECOM recorded an invalid or duplicate obligation for the 10 purchase requisitions with outstanding commitment balances of \$3.6 million recorded in the LMP Financial Accounting Module as of September 30, 2007. CECOM, following its normal business practice, recorded a miscellaneous obligation for the outstanding commitment balances of the purchase requisitions recorded in the Funds Management component of the LMP Financial Accounting Module. CECOM personnel stated that they processed the miscellaneous obligation to retain FY 2007 funding authority. The obligation of funds at fiscal year-end on a MOD in the absence of an agreement between an agency and another party in anticipation of specific, definite needs violates 31 U.S.C. 1501 and DoD FMR, volume 3. One of the 10 open purchase requisitions we reviewed had an outstanding commitment balance of \$165,000 that was no longer valid. It was not valid because of a previous error in attempting to correct the open purchase requisition. Although the LMP Funds Management component showed an unobligated balance for the other nine purchase requisitions, our review showed that obligations had already posted in the Financial Accounting Module to the Undelivered Orders, Obligations Unpaid account (general ledger account code 4801).

The PEO EIS and CECOM had identified, but had not yet formalized, a plan to correct an LMP system problem affecting recorded commitment balances for purchase requisitions when different units of measurement are used on the purchase requisition and purchase

order. In recognition of the problem, the PEO EIS has developed a report that identifies purchase requisitions and purchase orders with different units of measurement. The July 2008 report identified 131 purchase requisitions and purchase orders with different units of measurement. However, CECOM has not developed standard operating procedures for using the report to monitor and manage the effects of the differences on financial data.

Unit-of-measurement differences often occur on purchase requisitions and purchase orders for repair and maintenance of inventory items. For example, 1 of the 10 purchase requisitions prepared by the Logistics Readiness Center showed a quantity of 11 each, a unit price of \$64,127, and a total value of \$705,397. However, the contract issued by the Contracting Center stated a quantity of *1 lot* for a total cost of \$705,397 (the *1 lot* was intended to capture all 11 items requisitioned). The contract data posted to the LMP Funds Management component as a quantity order of *1 each* and a purchase order obligation amount of \$705,397. In addition, an obligation for \$705,397 posted to the Undelivered Orders, Obligations Unpaid account (general ledger account code 4801). However, LMP reduced the commitment amount of the purchase requisition in the LMP Funds Management component by only \$64,127 (*1 each* for \$64,127), and the purchase requisition continued to show an open order quantity of *10 each*, with an open commitment balance of \$641,270.

As a result of these transactions, both the general ledger and the LMP Funds Management component showed an outstanding commitment balance of \$641,270 (\$705,397 less \$64,127) for the purchase requisition. They also showed that funds were fully obligated for \$705,397 on the purchase order. This overstated the amount of open commitments and understated the allotted funds available on the monthly financial reports. By including the outstanding commitment balance of \$641,270 as part of the year-end MODs, CECOM recorded a duplicate obligation. Of the 10 open purchase requisitions that we reviewed, 9 had \$3.4 million of duplicate obligations caused by variances in the unit-of-measurement quantities, and one purchase requisition involved an invalid commitment for \$165,000 caused by an error in attempting to correct the purchase order. Because the 10 purchase requisitions reviewed were duplicate or invalid obligations and CECOM followed a consistent business practice when obligating outstanding commitments for purchase requisitions, we concluded that many of the other 204 open purchase requisitions, valued at \$10.2 million, were also likely to have invalid or duplicate obligations.

The PEO EIS should formalize a plan to change LMP functionality to correctly process contract and accounting data when different units of measurement are used on the purchase requisition and the purchase order. CECOM should develop standard operating procedures for using the report on unit-of-measurement differences and continually monitor the effects these differences have on reported financial data. In addition, CECOM should discontinue the practice of recording a MOD for the outstanding

commitment balances of open purchase requisitions at fiscal year-end and should verify that there is documentary evidence that a valid contract or purchase order exists before recording a MOD.

### ***Undocumented Obligation Transaction***

CECOM personnel processed an invalid \$7.7 million obligation transaction on September 30, 2007. The transaction was not included as part of the two MODs we reviewed. We identified this transaction when reviewing obligation reversals processed after FY 2007 year-end close. Logistics Readiness Center personnel stated that they processed the transaction to obligate funds for an open UCA, but later determined that they had already finalized the UCA. Personnel explained that this problem occurred because of time constraints at fiscal year-end and miscommunication among staff regarding the contract status of the UCA. Logistics Readiness Center personnel processed the obligation transaction for the estimated amount of the UCA without preparing the MOD and the supporting documentation identifying a specific contract action and dollar amount. On October 26, 2007, personnel reversed the obligation. CECOM should develop written procedures requiring that estimated obligations be supported by a DD Form 2406 and include the supporting documentation and evidence of management review and approval.

### **Conclusion**

CECOM improperly used MODs to record invalid or duplicate obligations, violating 31 U.S.C. 1501, 10 U.S.C. 2326, and the DoD FMR and therefore overstating the year-end obligation balance on the FY 2007 ACWF Statement of Budgetary Resources by at least \$24.4 million. The Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer should revise DoD FMR, volume 3, chapter 8, to enforce 10 U.S.C. 2326 limitations on obligating funds for UCAs and to prevent the use of a MOD to obligate the undefinitized amount of a UCA at fiscal year-end. To correctly record contract and accounting data when there are different units of measurement on the purchase requisition and the purchase order, the PEO EIS should formalize a plan to change LMP functionality, and CECOM should develop procedures to monitor the effects on financial data until the PEO EIS corrects LMP functionality. To ensure that miscellaneous obligations are valid, CECOM should stop obligating the outstanding commitment balances of open purchase requisitions at fiscal year end and develop standard operating procedures for verifying, documenting, and approving year-end MODs.

### **Recommendations, Management Comments, and Our Response**

**B.1. We recommend that the Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer revise DoD Financial Management Regulation, volume 3, chapter 8. Specifically, delete the requirement that DoD Components record a miscellaneous obligation at fiscal year-end for the undefinitized amount of an**

**Undefinitized Contract Action, and require that DoD Components commit and obligate the fiscal year budget authority in effect at the time an Undefinitized Contract Action is definitized.**

### ***Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer Comments***

The Acting Deputy Chief Financial Officer agreed and stated that the Office of the Under Secretary of Defense (Comptroller) has revised DoD FMR, volume 3, chapter 8, and has issued it for electronic coordination. The draft changes to the DoD FMR will delete the requirement that DoD Components replace a recorded commitment with a miscellaneous obligation at year-end. The draft changes also require that DoD Components commit and obligate the fiscal year budget authority in effect at the time an Undefinitized Contract Action is definitized. The target date for issuing the final changes to the DoD FMR was April 30, 2009.

### ***Our Response***

The Acting Deputy Chief Financial Officer comments are responsive. No further comments are required.

**B.2. We recommend that the Army Program Executive Officer, Enterprise Information Systems formalize a plan to change the Logistics Modernization Program system functionality to correctly process contract and accounting data when there are differences between units of measurement on the purchase requisition and the purchase order.**

### ***Program Executive Officer, Enterprise Information Systems Comments***

The Army PEO EIS agreed and stated that the LMP Program Management Office has performed an initial analysis of possible systemic changes (changes to system functionality) to correctly process contract and accounting data when there are differences between units of measurement on the purchase requisition and the purchase order. Although system functionality changes would result in contract obligation data posting correctly in LMP, the changes would likely result in incorrect posting of financial and logistics data when the material receipt and invoice posted. The Army PEO EIS stated that the best and most effective way to resolve the issue is to change business processes for new contracts and require the Contracting Centers to use the same quantity and unit-of-measurement in the contract as used on the initial purchase requisition.

The PEO EIS further stated that the LMP Program Management Office continues to investigate the initial changes to system functionality and quantify the impact on financial and logistical data of material receipts and invoices. The LMP Program Management Office will communicate the results of its analysis to the Army business community by April 24, 2009. The PEO EIS stated that if his office identifies system functional changes to address the financial and logistical aspects of processing contract obligations,

material receipts, and invoices with unit-of-measurement differences, incorporating these changes into LMP would follow the established system development lifecycle. The established development lifecycle includes prioritizing of the required work by Headquarters, AMC, and scheduling the documentation, development, and testing phases in the LMP Integrated Program Master Schedule.

### ***Our Response***

The Army PEO EIS comments are partially responsive. The LMP Program Management Office indicated that the initial changes to system functionality (“systemic changes”) would likely result in incorrect posting of financial and logistical data when subsequent material receipts and invoices are processed. However, it continues to review system solutions to the problem. The PEO EIS stated that the most effective way to resolve the problem is to change business processes for new contracts and require the Contracting Centers use the same quantity and unit of measurement on the contract as used on the purchase requisition. However, the Army business community has stated that the PEO EIS should change LMP functionality to process unit-of-measurement differences.

The PEO EIS and the Army business community need to agree on a course of action to resolve the problem of incorrect posting of financial and logistical data caused by differences between the units of measurement on the purchase requisition and the purchase order. The July 2008 report developed by the LMP Program Management Office for CECOM identified 131 purchase requisitions and purchase orders with unit-of-measurement differences that caused a \$17.4 million overstatement of open commitments and a corresponding understatement of allotted funds available on the monthly financial statements. As the LMP Program Management Office deploys the system to the other AMC Life Cycle Management Commands, the adverse effect on financial reporting could materially increase. In addition, it is a core financial system requirement that a system must be able to automatically close commitment documents and document lines upon issuance of an obligating document. The PEO EIS and the Army business community (primarily AMC) need to agree on a definitive plan of action to either change current contracting business practices or change LMP to correctly process accounting and logistics data when there are differences between units of measurement on the purchase requisition and purchase order. We request that the Army PEO EIS provide comments on a definitive plan of action in response to the final report.

**B.3. We recommend that the Commander, Communications-Electronics Life Cycle Management Command develop standard operating procedures for processing year-end miscellaneous obligations and managing unit-of-measurement differences. Specifically, require that the Logistics Readiness Center:**

**a. Discontinue the current business practice of obligating the undefinitized part of Undefinitized Contract Actions at the end of the fiscal year.**

**b. At fiscal year-end, review all open purchase requisitions and verify that documentary evidence supports the existence of a valid obligation before recording a miscellaneous obligation document.**

**c. Use DD Form 2406, “Miscellaneous Obligation Document,” to document support of all estimated obligations and for management review and approval.**

**d. Use the report on unit-of-measurement differences to continually monitor the effects on reported financial data.**

### ***Communications-Electronics Life Cycle Management Command Comments***

a. The Commander, CECOM agreed and stated that personnel no longer obligate the undefinitized part of UCAs at fiscal year-end.

b. The Commander, CECOM agreed and stated that personnel conduct periodic reviews of open commitments throughout the year and review open commitments on a daily basis at fiscal year-end. CECOM will close out open commitments for purchase requisitions that personnel cannot obligate by September 30.

c. The Commander, CECOM agreed and stated that the year-end process requires the use of the DD Form 2406 to record miscellaneous obligations. While personnel did not fully document the procedures until FY 2008, CECOM personnel did use the DD Form 2406 to support the FY 2007 year-end miscellaneous obligation.

d. The Commander, CECOM agreed and stated that CECOM uses an LMP query to track and monitor unit-of-measurement differences. In response to Recommendation B.3.b., the Commander also stated that closing out some of the open commitments that relate to unit-of-measurement differences can negatively impact the item manager’s ability to properly manage secondary items as invalid quantities of due-ins would remain on the LMP records. CECOM personnel will use the report to clean up these invalid due-ins.

### ***Our Response***

The Commander, CECOM comments are responsive and meet the intent of the recommendations. No further comments are required.

## Appendix A. Scope and Methodology

We conducted this audit from May 2007 through March 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We evaluated the effectiveness of controls over the recording and reporting of contract obligations in LMP. We reviewed the initiatives taken by the PEO EIS and CECOM to improve LMP system processes and internal controls and analyzed the percentage of contract lines rejected during the PADDSS-to-LMP interface. We requested a data file of all open contract line items recorded in PADDSS. We also obtained a data file of all active purchase order line items citing CECOM funds recorded in LMP since implementation in July 2003. The Data Mining Directorate, Office of the Deputy Inspector General for Auditing, used Audit Command Language software to match contract obligations recorded in PADDSS to the purchase order obligations recorded in LMP. Specifically, the Data Mining Directorate used the contract line item number to match the obligations recorded in PADDSS from May 1, 2005, through June 30, 2007, to the purchase order obligations recorded in the LMP Financial Accounting Module from May 1, 2005, through August 17, 2007. We excluded from our data analysis contract obligation data recorded in PADDSS and LMP before May 1, 2005. Instead, we focused the review on obligation data processed since May 1, 2005, when the PEO EIS rewrote the PADDSS-to-LMP interface, increased the frequency of PADDSS file transfers, and developed additional monitoring reports. We judgmentally sampled 78 of the 404 contract line item numbers in PADDSS that did not have a matching purchase order contract line item number in LMP. We also reviewed the 40 matching contract line item numbers with different dollar amounts in PADDSS and LMP. With the assistance of CECOM personnel, we analyzed the mismatches to identify the reasons for differences in the recorded obligations. We also did a reverse data match, comparing purchase order obligations recorded in LMP to the contract obligations recorded in PADDSS, and reviewed the 37 identified mismatches. In addition, we reviewed the data migration plans that AMC and the PEO EIS are using to validate contract data accuracy before fielding LMP at the Aviation and Missile Life Cycle Management Command in March 2009.

We reviewed CECOM procedures and controls over the use of MODs at fiscal year-end. We reviewed DoD FMR, volume 3, guidance on recording commitments and obligations for consistency with requirements set forth in 31 U.S.C. 1501 and 10 U.S.C. 2326. We interviewed CECOM personnel to determine the process for preparing and processing the FY 2007 year-end MODs. From the two MODs processed by CECOM at fiscal year-end, we selected a judgmental sample of 4 UCAs valued at \$13.1 million and 10 purchase requisitions valued at \$3.6 million to determine whether a valid obligation existed as of September 30, 2007. In addition, we reviewed other obligation reversals processed after

FY 2007 year-end closing to determine whether a valid obligation existed as of September 30, 2007. In addition, we coordinated with the PEO EIS to determine plans for changing LMP functionality to correctly process contract and accounting data when different units of measurement are used on the purchase requisition and the purchase order.

### ***Use of Computer-Processed Data***

We used computer-processed data to perform this audit. Specifically, we used contract and accounting data from PADDs and LMP. With the assistance of the Data Mining Directorate, we performed limited tests of the reliability and accuracy of the data elements recorded in PADDs and LMP. In order to ensure the reliability and accuracy of PADDs data, we verified that the contract data in PADDs matched the source contract documents stored in the Electronic Document Access system. With assistance from CECOM personnel, we analyzed the discrepancies. Our analysis identified an acknowledged LMP system problem affecting the recorded commitment balance for a purchase requisition when there is a unit-of-measurement discrepancy between the purchase requisition and purchase order.

### ***Use of Technical Assistance***

A senior auditor from the Data Mining Directorate, Office of the Deputy Inspector General for Auditing, assisted on this audit by importing transaction data from LMP and PADDs into Audit Command Language software and executing data comparisons to identify missing or inaccurate contract obligations recorded in the two systems.

### **Prior Coverage**

During the last 5 years, the Government Accountability Office (GAO), the Department of Defense Inspector General (DoD IG), and Army Audit Agency (AAA) have issued six reports discussing LMP. Unrestricted GAO reports can be accessed over the Internet at [www.gao.gov](http://www.gao.gov). Unrestricted DoD IG reports can be accessed at [www.dodig.mil/audit/reports](http://www.dodig.mil/audit/reports). AAA reports are restricted to military domains and GAO. They can be accessed at [www.aaa.army.mil/reports.htm](http://www.aaa.army.mil/reports.htm).

### **GAO**

GAO Report No. 05-441, “Army Depot Maintenance – Ineffective Oversight of Depot Maintenance Operations and System Implementation Efforts,” June 2005

GAO Report No. 04-615, “DoD Business Systems Modernization – Billions Continue to be Invested with Inadequate Management Oversight and Accountability,” May 2004

### **DoD IG**

DoD IG Report No. D-2007-065, “Controls Over the Prevalidation of DoD Commercial Payments,” March 2, 2007

## **AAA**

AAA Report No. A-2007-205-FFM, “Logistics Modernization Program System Federal Financial Management Improvement Act of 1996 Compliance – First Deployment Functionality,” September 7, 2007

AAA Report No. A-2007-0163-FFM, “FY 03 – FY 05 Obligations Recorded in the Logistics Modernization Program,” July 27, 2007

AAA Report No. A-2007-0154-ALR, “Follow up Audit of Aged Accounts – U.S. Army Communications-Electronics Life Cycle Management Command,” July 2, 2007

## Appendix B. Glossary

**Commitment.** A commitment is an administrative reservation of funds based upon firm purchase requisitions, orders, directives, and equivalent instruments. A commitment transaction ensures that funds are available before incurring an obligation.

**Definitized Contract.** A definitized contract is a contract action for which the Government and contractor have agreed to the final contract terms, specifications, and price.

**Contract Line Item Number.** A contract line item number identifies an item of supply or services on a contract, to include the item description, quantity, unit price, and total price.

**Enterprise Resource Planning System.** An enterprise resource planning system records every business transaction that takes place within the business process and provides real-time updates to the system databases and all connected systems to reflect each transaction. LMP is a Systems Application and Products (SAP<sup>®</sup>)-based enterprise system.

**Obligation.** An obligation is a legal reservation of funds based on the dollar value of orders placed, contracts awarded, services received, and similar transactions during an accounting period that will require payment during the same or future period.

**Purchase Order.** A purchase order is an LMP-generated document containing the contract data elements received from PADDs. One contract data element is the obligation amount. In LMP, “purchase order” is synonymous with “contract.”

**Purchase Requisition.** The purchase requisition is a request for the procurement of a specific quantity of material or services from external or internal supply sources. Logistics Readiness Center personnel prepare the purchase requisition, which creates a commitment in the LMP Financial Accounting Module before the purchase requisition passes to PADDs, where the Acquisition Directorate awards the contract for the requested material or services.

**Undefinitized Contract Action.** An undefinitized contract action is a contract action for which the contract terms, specifications, or price are not agreed upon before the contractor starts the work required by the contract.

# Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer Comments



COMPTROLLER

OFFICE OF THE UNDER SECRETARY OF DEFENSE  
1100 DEFENSE PENTAGON  
WASHINGTON, DC 20301-1100

MAR 24 2009

MEMORANDUM FOR PROGRAM DIRECTOR, DEFENSE BUSINESS  
OPERATIONS, OFFICE OF INSPECTOR  
GENERAL, DEPARTMENT OF DEFENSE

SUBJECT: Response to Draft Audit Report, "Controls Over Contract Obligation Data in  
the Logistics Modernization Program," (Project No. D2007-D000FI-  
0186.000)

This memorandum forwards the Office of the Under Secretary of Defense  
(Comptroller) response to subject Department of Defense, Office of Inspector General  
draft audit report. A copy of the response is attached.

The Department appreciates the opportunity to respond on the subject report. My  
point of contact is [REDACTED]. He may be reached by phone at [REDACTED].  
[REDACTED]

A handwritten signature in cursive script, appearing to read "D. Smith".

David P. Smith  
Acting Deputy Chief Financial Officer

Attachment:  
As stated

**DOD OIG DRAFT REPORT DATED MARCH 2, 2009  
PROJECT NO. D2007-D000FI-0186.000**

**CONTROLS OVER CONTRACT OBLIGATION DATA IN THE LOGISTICS  
MODERATION PROGRAM**

**OFFICE OF THE UNDER SECRETARY OF DEFENSE (COMPTROLLER)  
(OUSD)(C) COMMENTS TO THE DOD OIG RECOMMENDATION**

**RECOMMENDATION B.1:** We recommend that the Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer revise DoD Financial Management Regulation volume 3, chapter 8. Specially, delete the requirement that DoD Components record a miscellaneous obligation at fiscal year-end for the undefinitized amount of an Undefinitized Contract Action, and require DoD Components commit and obligate the fiscal year budget authority in effect at the time an Undefinitized Contract Action is definitized.

**OUSD(C) RESPONSE:** Concur. Volume 3, chapter 8 has been issued for electronic coordination and has been revised to delete the requirement to replace a commitment with a miscellaneous obligation document at year-end. The change also requires DoD Components commit and obligate the fiscal year budget authority in effect at the time an Undefinitized Contract Action is definitized. The expected completion date is April 30, 2009.

# Army Materiel Command Comments



REPLY TO  
ATTENTION OF:

DEPARTMENT OF THE ARMY  
HEADQUARTERS, U.S. ARMY MATERIEL COMMAND  
9301 CHAPEK ROAD  
FORT BELVOIR, VA 22060-5527

27 MAR 2009

AMCIR

MEMORANDUM FOR Inspector General, Department of Defense, ATTN: [REDACTED]  
400 Army Navy Drive, Arlington, VA 22202-4704

SUBJECT: Comments to DODIG Draft Report, Controls Over Contract Obligation Data in the  
Logistics Modernization Program (D2007-D000FI-0186.000) (D0719)

1. The U.S. Army Materiel Command (AMC) has reviewed the subject draft report and is providing the enclosed comments responding to the recommendations addressed to AMC. Further, AMC endorses the U.S. Army CECOM Life Cycle Management Command's comments (encl 2).

2. The point of contact for this action is [REDACTED]

2 Encls

KATHRYN A. CONDON  
Executive Deputy to the  
Commanding General

**Command Comments**  
**D2007-D000FI-0183.000**  
**Controls Over Contract Obligation Data in the Logistics Modernization Program**

**Finding A:** Recorded Obligations

**Summary of Finding:** Since the PEO EIS implemented system process changes and CECOM established better internal control procedures, the accuracy of obligations recorded for purchase orders in LMP has significantly improved. CECOM reported that the percentage of contract lines rejected during the PADDs-to-LMP interface decreased from 16.9 percent in May 2005 to 3.7 percent in May 2007. In addition, DODIG's comparison of contract line obligations recorded in PADDs to the purchase order contract line obligations recorded in LMP showed that almost all obligations accurately posted in LMP. Although CECOM has implemented improved processes and internal controls, it has not fully documented the processes and controls to ensure that they are applied uniformly and consistently in the event of personnel changes or during additional LMP deployments. CECOM should fully document its controls and procedures and AMC should require the other Life Cycle Management Commands to implement these controls and procedures upon future deployments of LMP.

**Recommendation A.1:** We recommend that the Commander, Army Materiel Command, require that the Aviation and Missile Life Cycle Management Command and the TACOM Life Cycle Management Command implement standard operating procedures for processing and controlling commitment and contract obligation data based on the procedures developed by the Communications-Electronics Life Cycle Management Command when it deploys Logistics Modernization Program.

**AMC Comments:** Concur. The U.S. Army Materiel Command is working with the CECOM Life Cycle Management Command to finalize completion of standard operating procedures with targeted completion date of 30 April 2009. The standard operating procedures will then be incorporated into the implementation plan for deployment to LMP.

Enclosure 1

# Communications-Electronics Life Cycle Management Command Comments



**DEPARTMENT OF THE ARMY**  
HEADQUARTERS, U.S. ARMY CECOM LIFE CYCLE MANAGEMENT COMMAND  
FORT MONMOUTH, NEW JERSEY 07703-5000

REPLY TO  
ATTENTION OF

AMSEL-IR (36-2b)

19 March 2009

MEMORANDUM FOR COMMANDER, Army Materiel Command, ATTN: AMCIR  
██████████, 9301 Chapek Road, Fort Belvoir, VA 22060-5527

SUBJECT: Command Response to HQDA/AMCIR Tasker 9068-703: DA  
90310482 - DODIG Final Draft Report - Controls over Contract  
Obligation Data in LMP (D0719) (UNCLASSIFIED)

1. The CECOM Life Cycle Management Command Reply to subject report is enclosed.
2. If you have any questions, please contact ██████████ CECOM LCMC Internal Review Office, ██████████
3. One Vision, One Mission - The Warfighter.

Encl  
as

*for* *Domenic A. Drazic*  
LEONARD R. MONTFORD  
Colonel, GS  
Chief of Staff

*Encl 2*

Command Comments

D2007-D000FI-0183.000

Controls Over Contract Obligation Data in the Logistics Modernization Program

**Finding A:** Recorded Obligations

**Summary of Finding:** Since the PEO EIS implemented system process changes and CECOM established better internal control procedures, the accuracy of obligations recorded for purchase orders in LMP has significantly improved. CECOM reported that the percentage of contract lines rejected during the PADDs-to-LMP interface decreased from 16.9 percent in May 2005 to 3.7 percent in May 2007. In addition, DODIG's comparison of contract line obligations recorded in PADDs to the purchase order contract line obligations recorded in LMP showed that almost all obligations accurately posted in LMP. Although CECOM has implemented improved processes and internal controls, it has not fully documented the processes and controls to ensure that they are applied uniformly and consistently in the event of personnel changes or during additional LMP deployments. CECOM should fully document its controls and procedures and AMC should require the other Life Cycle Management Commands to implement these controls and procedures upon future deployments of LMP.

**Additional Facts:** None

**Recommendation A.2:** We recommend that the Commander, Communications-Electronics Life Cycle Management Command, develop standard operating procedures that fully document existing processes and controls over commitment and contract obligation data passed to and from the Logistics Modernization Program and the Procurement Automated Data and Document System.

**CECOM LCMC Comments:**

A.2: Concur with finding and will develop SOPs to document existing control procedures for both commitments and obligations.

**Target Completion Date:**

April 30, 2009

Command Comments  
D2007-D000FI-0183.000

Controls Over Contract Obligation Data in the Logistics Modernization Program

**Finding B:** Miscellaneous Obligation Documents

**Summary of Finding:** CECOM did not comply with established laws and the DoD Financial Management Regulation (FMR), volume 3, when obligating AWCF funds at fiscal year-end using miscellaneous obligation documents (MODs). Of the \$27.6 million obligated on two MODs at FY 2007 year-end, at least \$16.7 million was an invalid or a duplicate obligation. In addition, CECOM processed a \$7.7 million invalid obligation transaction. As a result, CECOM overstated the year-end obligation balance reported on the FY 2007 AWCF Statement of Budgetary Resources by at least \$24.4 million. The Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer should revise the DoD FMR, volume 3, and require DoD Components to commit and obligate the fiscal year budget funding authority in effect at the time the UCA is definitized. The PEO EIS should formalize a plan to change LMP system functionality to correctly process contract and accounting data when there is a different unit of measurement used on the purchase requisition than is used on the purchase order. In addition, CECOM should develop standard procedures for verifying, documenting, and approving year-end MODs.

**Additional Facts:** None

**Recommendation B.3:** We recommend that the Commander, Communications-Electronics Life Cycle Management Command develop standard operating procedures for processing year-end miscellaneous obligations and managing unit-of-measurement differences. Specifically, require that the Logistics Readiness Center:

- a. Discontinue the current business practice of obligating the undefinitized part of Undefinitized Contract Actions at the end of the fiscal year.
- b. At fiscal year-end, review all open purchase requisitions and verify that documentary evidence supports the existence of a valid obligation before recording a Miscellaneous Obligation Document.
- c. Use DD Form 2406, "Miscellaneous Obligation Document," to document support of all estimated obligations and for management review and approval.
- d. Use the report on unit-of-measurement differences to continually monitor the effects on reported financial data.

**CECOM LCMC Comments:**

B.3.a - Concur. CECOM LCMC no longer financially obligates the undefinitized piece of Undefinitized Contract Actions on Miscellaneous Obligation Documents, but instead releases the unobligated portion of this requirement prior to year end close. This referenced obligation is not the contractual obligation but the obligation as it pertains to how the financial systems are handled. The CECOM Contracting Center conducts its UCA contractual obligations IAW with established policies and regulations.

B.3.b – Concur. Reviews of open commitments are and continue to be of utmost importance to CECOM LCMC and are conducted on a periodic basis throughout the fiscal year. At year end, open commitments are reviewed on a daily basis in order to ensure funds have been properly obligated. CECOM LCMC will close out all unobligated purchase requisitions that will not be obligated by 30 September and are not properly supported. However, some of these open commitments will relate to the unit of measure differences that currently exist in LMP. Because LMP is such an integrated system, closing out some of these transactions can negatively impact the item manager's ability to properly manage secondary items as invalid quantities of due ins would remain on the LMP records. This situation has yet to be corrected within the LMP system. Clean up of these invalid due-ins is an extensive manual process conducted by CECOM LCMC.

B.3.c – Concur. The existing CECOM LCMC year end process requires the use of DD Form 2406 to record year end Miscellaneous Obligation Documents. This process, while not fully documented until FY08, was in place for FY07 year end close and the DD Form 2406 was used to support the year end Miscellaneous Obligation Document used on 30 Sep 07.

B.3.4 – Concur. CECOM LCMC uses an internal developed LMP query on unit of measure differences created by our G-8 to track and monitor these purchase requisitions that are awarded in lot sizes instead of quantities.

**Target Completion Date:** 30 Sep 09

# Program Executive Officer, Enterprise Information Systems Comments



REPLY TO  
ATTENTION OF

**DEPARTMENT OF THE ARMY**  
OFFICE OF THE PROGRAM EXECUTIVE OFFICER  
ENTERPRISE INFORMATION SYSTEMS  
(PEO EIS)  
9350 HALL ROAD, SUITE 141  
FORT BELVOIR, VIRGINIA 22060-5526

SFAE-PS

8 April 2009

MEMORANDUM FOR Inspector General, Department of Defense, ATTN: [REDACTED]  
[REDACTED] 400 Army Navy Drive, Arlington, VA 22202-4704

SUBJECT: Comments to DODIG Draft Report, Controls Over Contract Obligation Data in the Logistics Modernization Program (D2007-D000FI-0186.000)

1. The Program Executive Officer, Enterprise Information Systems (PEO-EIS) has reviewed the subject draft report and is providing the enclosed comments responding to the recommendation addressed to PEO-EIS.
2. The point of contact for this action is [REDACTED]  
[REDACTED]

A handwritten signature in blue ink, appearing to read "Gary L. Winkler", written over a circular stamp or watermark.

GARY L. WINKLER  
Program Executive Officer

Encl

**Command Comments**  
**D2007-D000FI-0183.000**  
**Controls Over Contract Obligation Data in the Logistics Modernization Program**

**Finding A: Recorded Obligations**

**Summary of Finding:** Since the PEO EIS implemented system process changes and CECOM established better internal control procedures, the accuracy of obligations recorded for purchase orders in LMP has significantly improved. CECOM reported that the percentage of contract lines rejected during the PADDs-to-LMP interface decreased from 16.9 percent in May 2005 to 3.7 percent in May 2007. In addition, DODIG's comparison of contract line obligations recorded in PADDs to the purchase order contract line obligations recorded in LMP showed that almost all obligations accurately posted in LMP. Although CECOM has implemented improved processes and internal controls, it has not fully documented the processes and controls to ensure that they are applied uniformly and consistently in the event of personnel changes or during additional LMP deployments. CECOM should fully document its controls and procedures and AMC should require the other Life Cycle Management Commands to implement these controls and procedures upon future deployments of LMP.

Recommendation B.2. We recommend that the U.S. Army Program Executive Officer, Enterprise Information Systems, formalize a plan to change the Logistics Modernization Program system functionality to correctly process contract and accounting data when there are differences between units of measurement on the purchase requisition and the purchase order.

**PEO-EIS Comments:** Concur. Based on initial analysis into possible systemic changes to correctly process contract and accounting data when there are differences between units of measurement on the purchase requisition and the purchase order, the Program Management Office, Logistics Modernization Program (PMO-LMP) continues to assert that the best and most effective way to resolve this issue is by changing the business processes for new contracts to have the same quantity and unit of measure as the initial purchase requisition. While the previously discussed systemic changes would result in contractual obligation data being posted correctly, it would likely result in later incorrect financial and logistics postings with material receipt and invoicing. These postings would be based on the quantities and units of measure on the material receipt and invoicing documents, which is in turn based on those in the contract.

PMO LMP is continuing to investigate the systemic changes, as well as to further quantify financial and logistics impacts at the time of material receipt and invoicing based on this approach, which will be communicated to the Army business community<sup>1</sup> no later than 24 April 2009. In addition to this analysis, any additional systemic changes to overcome the financial and logistics impacts at the time of material receipt and

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<sup>1</sup> The Army business community is undergoing a significant governance model change that treats the Army as an enterprise. Therefore, the Army business community is represented by the Enterprise Process Owners Council (provisional) and its associated end-to-end business process teams.

invoicing will be investigated and communicated to the community. If systemic changes are identified to address all financial and logistics aspects of contract obligations, material receipt and invoicing, the incorporation of the changes in the system would need to follow the established development lifecycle. This includes the prioritization of the work to be accomplished by Headquarters, Army Material Command and the scheduling of the documentation, development and testing in the LMP Integrated Program Master Schedule.

Enclosure <sup>2 of 2</sup>





Inspector General  
Department of Defense

